3 IT Merger Integration and IT Carve-Out – Fostering External Growth and Disinvestment with IT

Acquiring enterprises and streamlining the portfolio during an external growth strategy are just as much integral parts of the life cycle of large enterprises as innovation and customer orientation are the supporting pillars of internal growth. Just as IT as an enabler for business strengthens the innovation capability of the company and increases customer bonding – thereby forming the basis for internal growth – it is also a success factor for external growth. The merger integration of enterprises always means integrating IT as well, and divesting a business unit always means that the IT system of this business unit is de-integrated from the overall enterprise as well – also called IT carve-out.

As soon as a sector has entered into a consolidation phase, companies are forced to pursue growth through mergers as well as the goal of internal growth or they face becoming the object of a takeover themselves. A comprehensive A.T. Kearney study illustrates the development of consolidating sectors based on a 'Consolidation curve' (figure 1.14). Here the sectors are listed according to the degree of concentration in the individual sector as a percentage of the sum of the market share of the three largest enterprises of the relevant sector in relationship to world markets, as well as their position in the consolidation life cycle. In each of the four phases of the 'merger endgame' of an industry, IT plays a decisive role:

- In the opening phase, there are numerous start-ups, spin-offs of major enterprises or industry segments, which have been liberalized or deregulated. In this phase the number of market participants in an industry increases, until by the end of this phase the highest number of enterprises in an industry has been achieved. For the enterprises in this phase, the issue is to win market share as fast as possible and at the same time build up market penetration barriers to keep out other companies and to obtain first mover advantages. In all this IT plays a decisive role – not only for start-up enterprises.
- With the transition to the accumulation phase, enterprises begin to encounter growing cost pressures caused by consolidation, and with rapid growth they reduce their high costs through economies of scale. With the numerous acquisitions that must be integrated in this phase, the capability to integrate IT in the merger integration is essential for the company's survival.
- The third phase demands focus. After the rapid growth of past years, most global corporations are now streamlining their portfolios, to divest themselves of divisions not belonging to the core business. The number of acquisitions is on the decline, but

their complexity is considerably higher. This also increases the requirements on IT merger integration and calls for the capability of disintegrating the IT of individual business units before a sale.

- The last phase of the consolidation wave reaches only a few market giants of a given industry. They face the challenge of constantly having to reinvent their core business, in order to survive this phase. Innovative IT investments and at the same time the lowest possible IT spending are key success factors here.

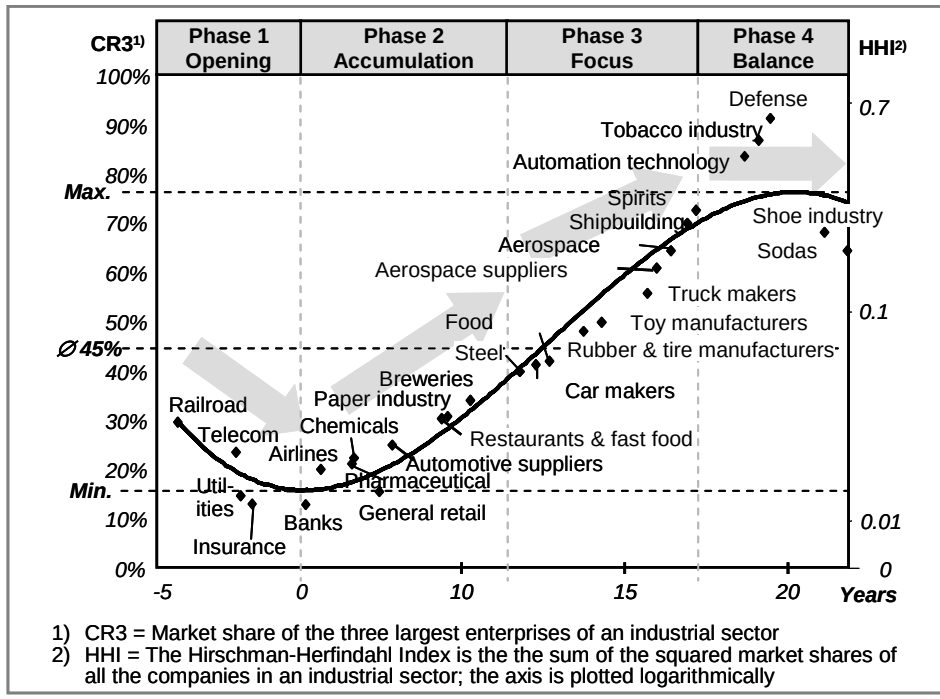

Figure 1.14: The consolidation curve; Source: A.T. Kearney

Fostering growth through mergers and acquisitions is a risky business. 52 percent of mergers destroy the value of the company instead of increasing it. However, one-quarter of all enterprises realize value increases through mergers and subsequent merger integration that which clearly lie above the sector average.

A similar pattern can be seen with disinvestment – the divesting of company assets or business units. Especially for enterprises that grow rapidly and extensively through mergers and acquisitions, the subsequent portfolio adjustment is an important building block for the success of the company. With professional disinvestment management, the strategically correct disinvestment candidates in the enterprise are identified, removed

from the company and sold to the highest bidder – and this is all carried out within a manageable timeframe. IT carve-out is a critical process for severing entire parts of a well-functioning unit without having a negative effect on the operations of the company, and at the same time giving the newly-founded company full capacity to act.

Transformation processes of this scope are not possible today without also modifying IT systems. Thus, the evaluation of IT should be an integral part of mergers and disinvestment:

- In the case of fostering growth through mergers, the compatibility of the IT of the company being acquired is already analyzed with the IT-assisted business processes of the acquiring company in the preparatory due diligence phase (for example one company uses Baan, a different SAP application – incompatible!), the synergy potential (for example by consolidating computer centers) must be assessed for IT efficiency, and the hidden chances and risks through large up-and-running or abandoned IT projects must be realistically evaluated. Although many buyers devote themselves to evaluating products, financial situations, company location, synergies and other factors with a lot of commitment and thoroughness, they fail to adequately involve the IT department. Over the course of the integration, IT then often proves to be an important factor for successful company integration – or a hindrance. As part of merger integration, the business processes of both business units must then be linked together – at least whenever the acquired business unit is to be "melted" with the buyer company and not just temporarily kept as a financial investment. As the majority of business processes are usually IT-assisted, a common IT landscape is formed. The building of a comprehensive IT platform ensures the success of the external growth strategy down the line.
- As part of divesting a business unit, in the preparatory phase of the sale the previously integrated IT of the business unit being sold is severed from that of the parent company, thus creating an independent company. This includes, for example, the separation of an SAP system as an independent client or the separation of e-mail and other IT infrastructure systems, including the separation of important contract agreements with the most important suppliers of hardware, software and IT services.

As varied as the requirements on IT merger integration and IT carve-out are in various company situations – it is important to analyze and solve the issues from four IT dimensions:

1. *IT organization:* Step and process organization, distribution of duties/responsibility, process depth/outsourcing, management, application development/maintenance etc.
2. *IT systems:* ERP systems, mail systems, special applications, databases, operating systems etc.

3. *IT infrastructure:* LAN, WAN, server, operations systems etc.
4. *Agreements and licenses:* Software licenses, IT service agreements, maintenance agreements, user rights to company's own and third-party owned software, rights to data files etc.

As the type and scope of the necessary activities are strongly dependent on the background situation of the IT system and the organizational complexity of the merger or disinvestment, the timeframe for the IT merger integration project can be from 3 to 18 months. Close collaboration with the IT specialists right from the initial phases of acquisition planning and due diligence and/or the disinvestment planning and carve-out will keep down existing risks and accelerate the subsequent integration/disintegration process.

Successful mergers with IT merger integration

In the past, the greater the strategic significance of IT became– not only for the efficiency of the business processes but also for success on the market side – the larger the role of IT became in the preparation and implementation of company integration. The strategic goal of the merger and the extent to which the IT systems of the merging companies overlap will determine the focus of IT as part of merger integration. Depending on whether the merger is 'horizontal', i.e. the products and markets strongly overlap, or whether the goal is expansion of the product, or geographical expansion or making full use of IT synergies with low market and product synergies, IT will be allotted different tasks (figure 1.16):

- *Same market/product overlapping:* A merger in the same market with strong product overlapping is usually motivated to achieve cost synergies in purchasing, production and administration. In this case IT efficiency gains are top priority. If the merging companies have identical activities, often one of the two IT platforms will form the future platform for the joint company and the other platforms are 'switched off'. If a total IT merger does not seem right for the specific company situation, cost-cutting can nevertheless be achieved in the IT infrastructure (computer centers, networks, e-mail systems etc.), at the IT suppliers (hardware/software/services) as well as standardization of the applications particularly in the financial area.
- *Product expansion*: If the acquiring company sees the goal of the merger to be product expansion in related markets, an IT concept similar to those used in mergers with product overlapping is suitable. It should be first determined whether the new or supplementary new products can be supported on the existing IT platform, possibly with lower, product-specific IT expansions.

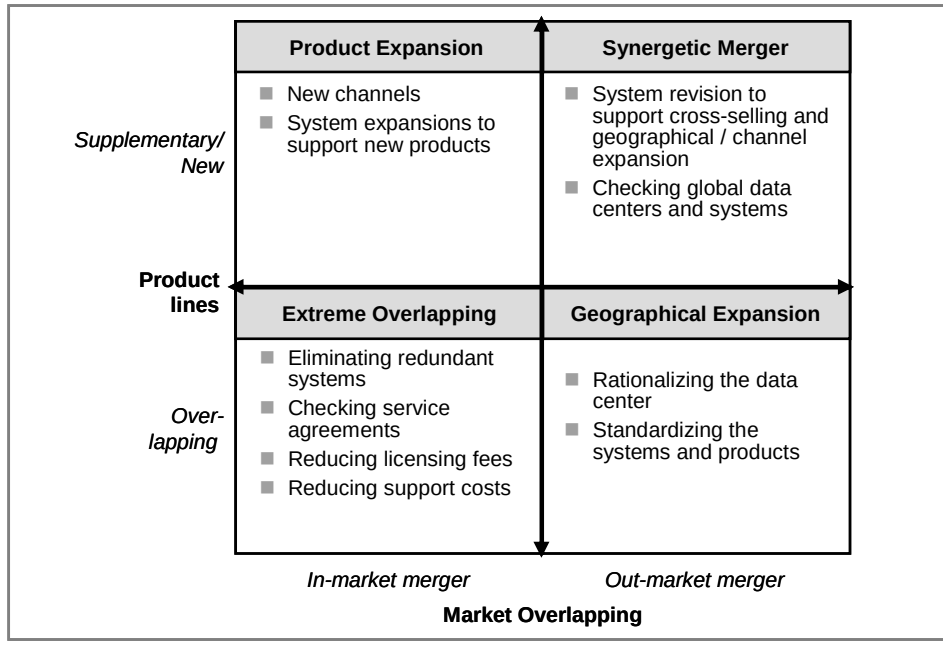

Figure 1.16: Technology focus in the context of a merger; Source: A.T. Kearney

- *Geographical expansion*: For mergers with product overlapping in a geographical market that is new for the company, there are often great differences in the requirements on the IT systems in individual markets. Particularly if the new market is also culturally very different, difficulties can arise, for example in consumer behavior or in the taxation and legal framework conditions of a consolidation. This applies, for example, to market penetration in China when acquiring a local company with a similar product range. It would then make sense to look for synergies in the IT infrastructure as well as in the IT systems for the same products in both markets. However, due to the objectively existing differences and great geographical distances, the decision is often made in favor of differing IT systems, each of which covers the special country-specific (for example legal) requirements particularly well. The benefit of such country-specific applications often surpasses by far the impact on costs due to IT standardization. Synergies can therefore only be achieved selectively via IT interfaces or cross-functional IT systems – particularly in the areas of financial consolidation, controlling, purchasing and sales/revenues planning and production program planning, and depending on the sector also in inventory systems and logistics.
- *Synergetic merger*: New business fields, which show somewhat lower synergies to prior company activities, can, for example, aim at approaching new customer groups, for example if an automobile manufacturer takes a stake in end customer business.

Here the possibility of using common IT systems is often restricted to finance management (especially cash flow management and balance sheet consolidation) and to controlling and purchasing. An exception is entry in the upstream or downstream value creation phases. Here the value added chain of the company being acquired is directly connected to the value added chain of the acquiring company. Here IT synergies can be expected in particular at the interfaces as well as in comprehensive planning and capacity utilization control systems (for example comprehensive yield management systems in integrated tourism service providers for the revenue-optimized capacity utilization control of travel agents, flights, hotels and on-the-spot services). Efficiency gains in the scope of IT in a synergetic merger are restricted to general IT infrastructure synergies (for example WAN, computer centers) and joint IT suppliers.

Common to all forms of mergers is the necessity of an integration process to reduce the loss of customers or employees – naturally this also applies to IT employees. Time is an essential factor here. Therefore, as early as the preparation phase of a merger the three important tasks of IT merger integration should be taken into consideration as part of merger integration, and enough time planned for them (see figure 1.17):

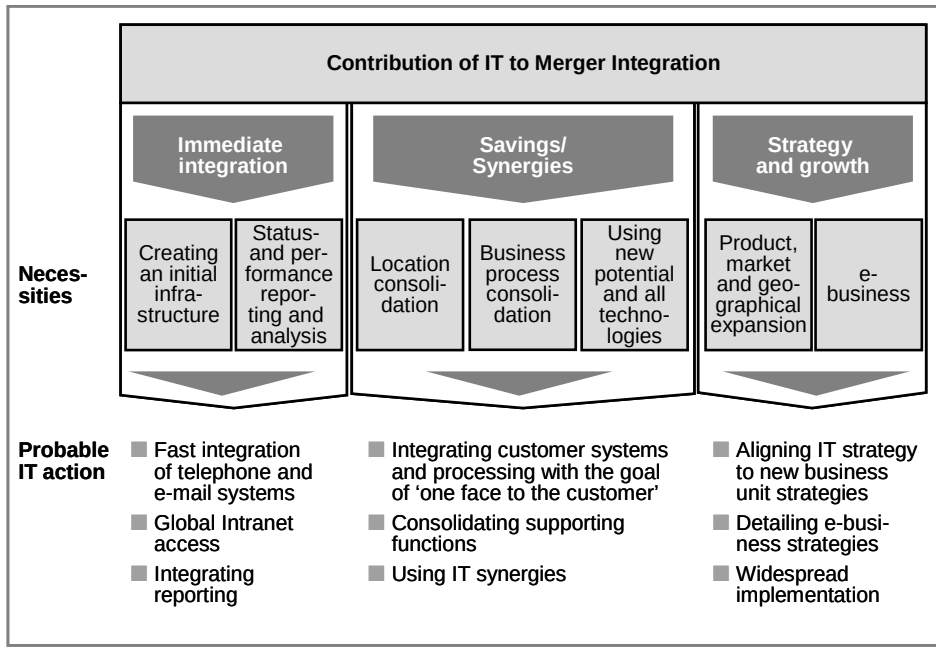

Figure 1.17: The role of IT in merger integration; Source: A.T. Kearney

1. Integration in the IT landscape of the acquiring company, to ensure communication and work capability in the merging companies from 'Day 1' of the merger.
2. Cost reduction and realization of IT synergies, among others through the harmonization and standardization of business-neutral IT processes and IT systems, as well as IT infrastructure, support in consolidating the location (particularly computer centers and help desks) and the consolidation of IT organization.
3. Support of the long-term strategy and growth goals of the company through rapid adaptation of IT strategy to new company goals, to ensure the success of the merger down the line, as well as building a comprehensive IT platform as the basis for further external growth.

IT integration not only supports the primary goals of the merger, but also functions as a driver during the entire integration process, as it also has a positive influence on the other success factors of merger integration:

- Lack of communication is one of the most frequent causes of mergers failing. IT creates the prerequisites for effective communication with all the parties involved in the merger – both inside and outside the company – from 'Day 1' of the merger.
- Delays during the integration process are another main cause of mergers failing, as uncertainty about the sense of the merger among the employees of the company and among external market players, as well as not least of all investors and analysts, can have disastrous consequences. Rapid IT merger integration can lead to rapid success, which counteracts this danger and also enables up-to-date and realistic reporting on the implementation progress of the synergies in the business processes, in purchasing and in marketing.
- If product quality deficits arise after the merger, this can endanger customer satisfaction and lead to losses of market share, which would have almost irrevocable consequences for the company. These are often a result of non-standardized processes and systems, due to inadequate IT merger integration.
- The loss of important carriers of know-how and other experts in the company can also lead to quality deficits and irritations with customers and suppliers. IT merger integration, which opens up new perspectives and possibilities to act, is an essential contribution towards being able to retain valuable employees in the company.

Ensuring capacity to act from day one through rapid IT integration

Immediately after the acquisition and as one of the first integration measures, an IT 'start-up infrastructure' is set up. It integrates the newly-acquired company in the communication of the acquiring company and opens up the communication channels for the installed change management program. Additionally, it facilitates the transition of the

Tip for rapidly ensuring ability to act on Day 1:

Fast availability is more important than perfection: The initial IT infrastructure is essentially temporary in character; thus more attention should be paid to rapid availability than perfection and performance.

control functions to the new top management personnel through regular, comprehensive reporting and controlling as well as performance and status management of the operational integration efforts (for example the implementation of synergies in purchasing).

Communication channels for sending out e-mail to all employees, e-mail circulars, telephone directories and Intranet are considered a matter of course in most enterprises today. But in times of a merger they are not. One of the first duties of IT merger integration, therefore, is to ensure that from the first day of the corporate merger onwards, the senior executives are able to inform all the employees about the strategic orientation of the company, the status quo of the merger and the chances and risks in the market with memos sent through a standardized e-mail and telephone system with a directory.

At the same time, an important issue for the senior executives is to receive complete information about the up-to-the-minute business operations and financial situation of the enterprise, to be able to make strategic decisions, develop cost-cutting potential and, if necessary, comply with instructions from the supervisory authorities. At the same time, it is important to prevent future risks to the integration process early on, in order to maintain their accountability towards external market partners. To this end as well, the in-house reporting must already be fully functioning from the first day of the merger and optimally supported by the IT system.

In the preparatory phase of the merger the central short-term IT requirements must first be identified, which is necessary to ensure the capacity to act of the new senior management staff. The processes for the final balance of the acquired company must be completely supported and the reporting department for the new company management must be in place. For the period of transition to the new management, communication strategies and organization plans must be developed for IT and, not least of all, the prerequisites for realizing cost-cutting measures in the medium-term and supporting corporate strategy with IT must be established.

Realizing cost cutting and synergies

IT merger integration makes an important contribution to merger integration through the generally high cost reductions that can be realized through the synergies of the merger. This applies first and foremost to the business processes after the merger as well as purchasing volumes and sales.

The goal of supporting the implementation of the synergies should be top priority during IT integration activities. Particularly with mergers between enterprises having similar products, the managers of the acquired company strive for cost synergies across the entire value added chain (research and development – purchasing – production – marketing – customer services as well as in administrative and supporting processes). As IT supports all these processes, it makes sense to use it in the implementation of organizational and process synergies as an enabler for the integration. Only if one of the companies simply 'superimposes' its existing process and system landscape over the other company – which seldom happens – will the processes and organization of IT remain as they are. In all other cases major IT adjustments are necessary, even to the point of completely replacing old systems and introducing new IT systems. This leaves 'no stone unturned' in IT after a merger.

During the preparations for 'Day 1' the existing and planned IT initiatives for the integration of the two merging enterprises must already have be identified and evaluated. As the resources and budgets for implementing IT integration are generally limited, the initiatives must be prioritized and implemented in the correct order. Two goals of the new company management are key here: Besides the realization of cost-cutting potential it is important to achieve fast and visible success, in order to make all interest groups – particularly supervisory boards, shareholders and analysts – clearly aware of the value of the merger. An important matter is signaling continuity to external market partners. Integrating customer systems and processes of both merging enterprises with the goal of a standardized market presence ('one face to the customer') is an important step here. Of course this also applies to the interfaces to suppliers and other interested parties, for example supervisory authorities.

Tips for achieving cost savings and synergies:

- *Concentrate on rapid results, not on technological perfection:* It is also important here not to strive for a perfect IT solution, but rather for implementting the doable quickly. By modularizing the existing IT landscape that supports the integration requirements, we can avoid a sequence in the processing of the IT requirements that is technically-driven and removed from the realization of operational synergies, possibly even opposed.
- *Financing initiatives for business process integration from IT optimization:* With a sufficient IT budget, generally speaking IT can easily finance the necessary initiatives from its own cost savings. The IT cost potential after a merger lies among others in a reduction of various existing IT products, particularly in the area of software development, in joining and standardizing software licenses, in standardizing the office environment and in consolidating data, IT services and the IT infrastructure, if necessary through outsourcing (*cf.* Part 3 of this book).

The employees are also a critical target group in the first period after integration. The existing resources necessary for implementing future IT projects and any gaps must be recognized right away, in order to show existing employees new perspectives and to retain know-how within the company.

In the area of reducing costs after the merger, IT has two 'construction sites' to work on: the IT initiatives that aim at delivering cost reductions in business processes, as well as the cost reducing potential within the IT department itself – whereby the former should have clear priority here. Through the support of the business-oriented goals of the merger – be it location consolidation, business process consolidation or the market-side utilization of targeted growth and new technologies – in the first period after the merger IT merger integration can make the best contribution to the long-term success of a merger.

The measures for integrating business processes incur varying levels of expenditure and promise varying levels of synergy potential. IT should give priority to supporting those which have the highest potential. This operational prioritizing criteria leads to a number of changes in the scope of IT, for example shared suppliers of both merging enterprises can only be recognized if the IT of the enterprises each provides an appropriate database. To begin with, IT should therefore support the new company initiatives through a rapid IT merger integration (particularly of the IT organization and IT systems), through a rapid alignment of the business processes, harmonization of the information flow, and joint project planning and control instruments, before cost cutting in the IT department can be realized.

Takeover of an international manufacturing company by a German conglomerate

A German conglomerate took over the majority stake in an international manufacturer headquartered in France. There were production locations in France, Asia and in the USA. As is usual in this industrial sector, there was no order-based production. The company's inventories often lasted for many months. Due to the tense market situation in the specialized market segment of the newly-acquired company and the negative revenue contribution to the group results, it quickly became clear that the purpose of the acquisition – profitable market development in a short time – could only be achieved through better company management and a closer relationship to the proprietor.

Without integrating the IT landscapes, managing and controlling the manufacturing company with the existing human resources was not possible. Additionally, the systems used by the manufacturing company and the quality of the installed IT services were far from corresponding with the standard in the rest of the conglomerate.

> The task of IT merger integration consisted in harmonizing not only the group processes, particularly the inventory management, billing and controlling, with the group standards, but also improving the communication between the enterprises through the integration, in particular, of e-mail and directory services, thus cementing them more closely. As part of this, the French ERP system was replaced with only marginal modifications by the standard SAP template of the conglomerate. The technical infrastructure – particularly the operating system and the e-mail system – were standardized, and the locations of the new company were linked via VPN technology and smaller locations via DSL to the group network. Comprehensive training measures assisted the French employees in their conversion to the new IT systems.
>
> After only a few weeks the technical integration of the infrastructure, including the standardization, was complete. The introduction of the SAP template, however, proved to be more complicated than planned. The head office of the group had seriously underestimated the scope of the enormously important user training courses for aligning the business processes at the location. Only after head office had intervened with support could the initial difficulties be overcome.

Fostering long-term external growth strategies

After the first cost and potential benefit from a merger have been realized, the IT department can devote its attention to setting up an IT architecture, which supports all the strategic and operative requirements of the new company down the line. For processes with strategic relevance, e.g. for securing market shares or for distinguishing the company from the competition, for operative and transaction processes and databases, middleware and IT infrastructure, the existing IT solutions must be checked, evaluated and if necessary new solutions initiated.

IT strategy is aligned to the new corporate strategy, to identify new solutions that will foster further growth in the long term. Depending on the focus of the merger, these solutions can apply to e-business or cross-selling. These also include unavoidable trivialities like the multilingualism of the systems or transaction-oriented online processing in 24-hour operations, which is possible due to globalization (loss of backup and maintenance windows), and also more fundamental business-driven changes, for example in the acquisition of additional country units with marketing and production units with connected European or global production and logistics.

Aligning IT strategy is a suitable occasion, regardless of the current necessity of IT integration, to also secure any future merger plans of the company with suitable IT projects. Particularly if the enterprise has geographical expansion plans it is a good idea to systematically develop IT into an international platform for realizing product or process innovations – i.e. to pursue a ‘platform strategy’.

Contrary to the standardization of processes, a platform strategy orientates itself to IT at the product and/or customer segments and allows not only similarities but also specific dissimilarities (for example a product that is the same all over Europe, but which has a different name in each of the countries, with different marketing and pricing). Realizing the IT platform therefore aims at achieving synergies without complete standardization.

This task becomes more demanding, the more a company grows into a globally thinking and operating corporation. The country-specific orientation still evident in many industrial sectors must make way for a global structure with universal global responsibilities for individual business units, to be able to offer identical products and services all over the world. A correspondingly worldwide uniform IT architecture with worldwide uniform business processes is the prerequisite, for example, for developing the advantages of a global customer management from uniform coordination and universal organization – with the lowest possible level of country-specific individuality.

The telecommunications industry is currently following such product or customer segment driven IT platform strategies in the area of cellular communications. Based on the goal of pan-European branding and therefore universal customer bonding as well as a high level of recognition, Vodafone, for example, with 'Vodafone Live!' creates a uniform product in Germany, Ireland, Italy, the Netherlands, Portugal, Spain, Sweden and the UK with increasing system networking in the background. Similar goals are achieved by MMO2 with its 'XDA', as well as Orange with 'Orange World' and KPN/E-Plus with 'i-mode'. Deutsche Telekom aims to realize IT platforms, for example in the area of billing. All these telecommunications providers harmonize major parts of their product-related IT as well as the accompanying business process-oriented and administrative IT systems, in order to realize such an IT platform. Other parts of IT, which have no direct relation to such European telecommunication products, are not affected by IT platform building.

The effectiveness and efficiency advantages of a product-driven or customer-segment-driven IT platform will become clear in these examples:

- The telecommunication provider is given more strategic options for marketing its products (for example, simultaneously in several countries vs. in only one country) and can increase customer bonding as well as the turnover per customer (for example through pan-European availability of the product for business travelers).
- The time-to-market becomes shorter because the development resources are consolidated and solutions can be shared. This means that sales can be realized sooner.
- Cost reductions arise from avoiding multiple developments and from consolidating demand according to joint IT solutions for building IT platforms.

It is equally important that, particularly in European or global enterprises, establishing common products and IT platforms has the positive side effect of improving the mutual understanding of the senior executives and employees of the individual country locations, thereby strengthening cultural integration.

When such a comprehensive IT platform is established, a picture of the IT landscape is created that is differentiated according to products and customer groups. Based on a common IT system for products or customer groups, the business processes and IT systems in further areas can also be harmonized and integrated, for example, financial processes by realizing a comprehensive financial shared services center on the basis of uniform IT systems. Whether or not this makes sense in individual cases is determined by the portion of standardized products and/or customer groups there is. For example, in a European conglomeration with 20 percent (or less) international and 80 percent local products, the comprehensive European IT platform is oriented to the support of the comprehensive 20 percent, while the IT support of all other processes is more locally oriented. If the relationship should shift in the medium or long term, building a pan-European standardized IT platform would seem the obvious choice, in which any peculiarities of the local products and country-specific differences can be taken into due consideration.

It is not only the telecommunications industry that is building European or global IT platforms. Globally operating automobile manufacturers also already have such IT platforms or are in the process of creating them, not only in passenger cars but also in the commercial vehicle segment. And the major aerospace manufacturers and suppliers are also creating these kinds of IT platforms, for example to shorten product development time through 24-hour development according to the ‘follow-the-sun’ principle, or for shifting specific manufacturing jobs to low-wage countries. Many other industries are also working on the basis of global IT platforms on such globalization themes.

Checklist: Does your company use IT for smooth integration of mergers or takeovers?

***For 'Day 1'*:**	***Yes***
■ Are the existing IT structures of both enterprises analyzed and are short-term opportunities as well as medium-term needs for action identified?	❑
■ Has a plan for fastest-possible realization of a comprehensive reporting for control of the merger progress been set up?	❑
■ Have data network connections between important subsidiaries and locations been set up?	❑
■ Are the e-mail directories consolidated so that the employees have a uniform system to work with?	❑
■ Is access for all employees to the Intranet assured?	❑
■ Can a controlling/merger control tool be implemented?	❑
■ Are the legal requirements, among others from the financial and taxation point of view, supported and/or fulfilled by IT?	❑
For implementing merger goals:	
■ Have the strategic goals of the IT merger integration been approved?	❑
■ Are the IT implementation measures for fulfilling the synergy goals clearly outlined and prioritized, responsibilities allocated, milestones date-planned and implementation budgets allocated?	❑
■ Are the roles and responsibilities coordinated in the scope of the IT of the new organization?	❑
■ Does continual and non-conflicting communication take place with all internal and external parties?	❑

Divesting operations successfully with IT carve-out

Regularly checking corporate strategy, evaluating the current strategic positioning and the chances for growth are normal measures that are taken in most enterprises. In the past few years the search for cost-cutting possibilities and improvement potential was high on the agenda of many senior executives. It is especially important to check all business units for their strategic contribution to the overall success of the company, to verify their proximity to the core business as well as their growth potential and the sustainability of market success. If at the same time disinvestment candidates are identified, the question arises of their value and growth potential and not least of all a potential buyer who would be prepared to pay the highest possible price for the business unit.

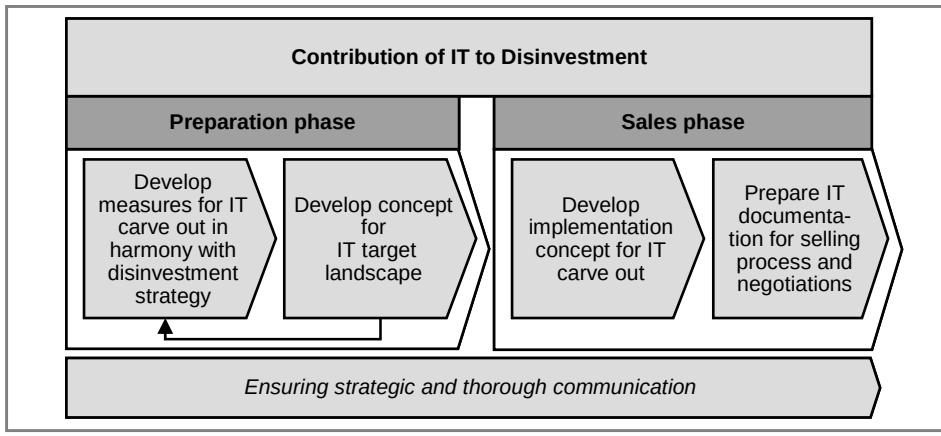

Figure 1.18: The role of IT in disinvestment; Source: A.T. Kearney

IT carve-out plays a critical role in this process – not only in the preparatory but also in the selling phase of disinvestment (figure 1.18). It must ensure that the company being divested is already independently capable of doing business before the sale is completed, to enable rapid integration with the buyer. An insufficient IT carve-out in the preparatory phase can considerably reduce the value of the company unit for a buyer.

Preparing business units for disinvestment

Before the actual selling process begins all necessary measures must be in place to make the company being divested independent and capable of doing business. In the preparation phase of disinvestments, the IT department has to identify the IT dependencies between the divesting company and the disinvestment candidate in accordance with the disinvestment strategy of the company, and to define the requirements on IT carve-out.

This also includes the analysis of the IT cost structures for the company to be divested and the evaluation of possible risks arising through the removal of the business unit, to avoid possible conflicts with the buyer after the sale.

From the perspective of a company-wide optimized IT support, generally speaking it is advisable to carefully weigh up doing without partial solutions and redundant structures in individual business units and rather to consider harmonizing and standardizing IT applications and infrastructure as well as procurement processes in IT. In the case of a disinvestment, however, shared hardware and software, as well as common network resources hinder the divested business unit's capacity to do business independently. Before the sale, therefore, assets such as hardware and software licenses must be transferred to the business unit being divested in accordance with requirements; jointly used agreements must be distributed. If the business unit being divested continues to use the centralized IT resources of the parent group, e.g. the computer center, service agreements must be drawn up to bridge the time gap until the IT integration into the divesting company and the switch to its centralized IT resources have been completed. If possible, however, the company being divested should avoid continued use of the assets of the former parent company, as the proportionate calculation of the costs for the use and maintenance of these assets often provides reason for disagreements with the new owner after the sale.

Tip for preparing a disinvestment:

Pay attention to apparently unimportant factors: For carrying out IT carve-out, you need correct and up-to-the-minute service and cost data for the business unit being divested. Apparent trivialities gain enormous significance here, for example the establishment of a precise measuring procedure for the use and billing of telephone and network services. Advisable is a separate contract with the telephone/ network operator. Here again, cost breakdowns after a disinvestment are often the cause of disagreements – particularly in the case of major changes to the breakdown of human resource expenditure.

In the preparation phase, the divesting company sets down the necessary measures in a disinvestment concept and prepares an implementation plan. At the end of this phase the disinvestment is prepared to the point of ensuring that a smooth disinvestment of the business unit will ensue. It is the task of the IT department to prepare a concept for the future IT landscape of the business unit being divested and to identify some initial solutions as well as potential 'quick wins' for the disinvestment. For the business unit being divested the IT requirements must be set down and prioritized according to operational benefit criteria. The existing IT infrastructure and IT systems must be checked and compared with the best practices of the sector-specific IT landscape.

Divesting four business units of a technology conglomeration

A conglomerate wanted to divest its fully integrated technology unit. When preparing the disinvestment the company unit was divided up into four parts, which would clearly fetch a higher selling price when sold to investors than the entire business unit together. Up to that point, a central IT department was responsible for the entire infrastructure as well as the commercial applications (SAP R/3) and the office communication of all of the locations in Germany.

Before the disinvestment took place, the central IT department was outsourced to an IT service provider. To control the situation, the position of CIO was established in the company. While the foreign companies, who had access to their own IT systems, simply allowed themselves to be allocated to one of the newly-created business units, the six locations in Germany were closely interwoven. Therefore, the IT landscape had to firstly be divided into four independent units, which were then to be integrated into the IT landscapes of the individual investors to maximize value.

To begin with, the IT landscape was analyzed: Which commercial and scientific systems were present? Which IT costs arise where? Which inputs (users, end devices etc.) exist? What is the IT organization like? What technical infrastructure is there? Next, in each of the new business units a lean CIO organization for IT planning and controlling as well as control of the IT service providers was established.

The existing operative SAP systems were copied for the new business units and the data distributed accordingly. One system was segmented through a client copy, which technically speaking was the simpler solution, although in retrospect there were high SAP operating costs and a more complicated archiving system. The second system was completely reinvented (‘green meadow’ concept) and preselected data was entered.

In retrospect, this concept proved to be the best practice. For economic reasons, both of the new small, low-staff business units introduced slimmer ‘package’ ERP systems such as Datev or Navision. During the segmentation process the SAP system was spared a release change – these investments were not covered by a higher sales price.

The division of the infrastructure was an issue at the locations that were used by several business units: every business unit should only have access to its own data and applications. This of course meant foregoing the IT synergies. To avoid a cost explosion, particularly expensive infrastructure components like firewalls, servers, routers, etc. were to be shared as before.

To begin with, the existing IT assets such as PCs, servers etc. were distributed as well as possible among the business units and the shared components were left with the residual company. The local networks, including the user structures, mail,

server, etc., as well as the WAN and the telephone infrastructure, particularly the billing, were severed and the data files also distributed to the business units.

In addition, existing software, hardware and IT service agreements were distributed among the business units and inputs and requirement structures were adapted, whereby the original conditions were to remain the same for the business units for as long as possible. This proved to be especially difficult in the case of the service agreement with the IT outsourcer, as the contractual risk had risen for him for one, and for another it had become difficult for him to realize synergies between the four business units. In particular the specification of inputs – decisive criteria for profitability – shrunk considerably. Together with the IT service provider, therefore, consolidation activities were carried out that permitted him to offer the four business units new agreements at normal market conditions. Additionally, new service agreements were completed for utilization of the infrastructure overlapping more than one business unit between the residual companies and the business units at normal market conditions.

Tip for the selling phase of a disinvestment:

Ensure continual communication: The migration of important carriers of know-how can considerably reduce the value of the business unit being sold. Therefore, continual communication between the staff and between the IT department and the disinvestment team in the company are absolutely essential.

Chiefly due to regulations and legal reporting obligations, the electronic archiving of historical data – particularly marketing, product and personnel data remained IT activities. For the remaining commercial activities of the residual companies (processing, pensioners etc.) a simple Datev ERP solution was set up, which was transferred to the ERP system of the disinvestor after the entire business unit was dissolved.

Supporting the sales phase with IT carve-out

During the actual disinvestment of the company, IT disintegration plays a special role. A ‘disinvestment highway code’ sets down the necessary steps and differentiates between short-term necessary measures and those activities that are only carried out in response to specific requests from the buyer, in accordance with his conditions. In the short term and in any case it is essential to sever the e-mail system. The more complicated and far more important separation of, for example, the production planning and control systems as well as further logistics or R&D systems should, on the other hand, be discussed with the buyer. It would be ideal to switch from the former IT landscape directly to the IT systems of the buyer, while safeguarding the disinvestment item’s capacity to act, with-

out having to set up a temporary IT landscape of their own, particularly for logistics and finance systems.

In order to safeguard the disinvestment item's capacity to act, the new company must avail of autonomous IT services. For this, the IT department must ensure not only IT services that are vital to survival, but also guarantee their payment. In framework agreements for hardware and software as well as for maintenance, an agreement is made to keep the existing contracts for the interim period. For billing and reporting, however, a separate system as well as a separate accounting cycle for the divested company is an absolute must. This can be done within the framework of an SAP system that is, as before, shared.

If the number of users and employees and the revenues and complexity of the divested company are not critical for the ERP software used to date, there are two alternatives:

- Selecting a simple, less complex but sufficiently functional package software and the migration of data from the old system
- Sharing a simple ERP system, which is made available by an IT service provider, for example as part of a workstation (ASP) operation model.

If it makes economic sense to continue using the existing ERP system, there are two feasible alternatives:

- Creating a client copy and selectively erasing data that is no longer needed. This is less complex in terms of technology and content, but means that use of the system is basically the same as before.
- Setting up a new client on the basis of a template and input the old data. This is more complicated in terms of content, but enables the adjustment to the requirements of the divested company and helps get rid of 'dead wood'.

For the actual sales negotiations and the transition of the disinvestment item to the buyer it is the job of the IT department to make the various IT options for the new company, including a cost outline, and the data structures of the new company transparent for the buyer, here again in order to avoid the danger of later conflicts.

Checklist: Can you avoid the most important risks of IT disinvestment?

	Yes
■ Does the business unit being divested have capacity to act alone?	❑
■ Is the IT organization of the disinvestment item prepared for future requirements in terms of the number and qualifications of its employee?	❑
■ Are the ERP systems of the divesting company and the business unit to be divested separated from one another?	❑
■ Have all necessary licenses, assets and agreements for the business unit to be divested been prepared?	❑
■ Is the transition of IT services to the buyer of the business unit contractually safeguarded?	❑
■ Are all rights to data and programs clarified?	❑