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Achieving the Right Flavor:

A Study of Designing a Cultural Integration Process

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Abstract

The success rate of acquisitions in meeting both company and shareholder expectations is, by numerous reports, very low. One of the central culprits in hindering expected value of acquisitions is the integration of the two companies' cultures. This report details an approach used to develop an assessment process to systematically assess the differences between two cultures and further develop interventions to address these differences. In addition, the authors identify lessons learned to put into practice in future cultural integrations.

Achieving the Right Flavor:

Designing and Developing a Cultural Integration Process

Assessing, Developing and Integrating Corporate Cultures

Description of the Situation

A large Midwest company (Chocolatier Financial Services, fictional name used for this paper) in the financial services industry has identified expansion through acquisition as one of its approaches to overall growth. In this pursuit, it has begun the acquisition of another similar but smaller financial services company (Company B) also in the Midwest. Chocolatier has a history of growth through acquisition, and the management of the company has determined that in order to better capture the potential synergies of the target company, it must put more emphasis on the integration process. In particular, the area of cultural integration has been identified as a weakness in previous integrations. In this acquisition, a special emphasis is being put on the cultural integration of the two companies. While the two companies are similar in age (about 30 years old), and both have expanded through acquisition, Chocolatier is significantly larger that Company B. The acquisition will extend the reach of Chocolatier and solidify their entrance into a complementary line of business.

Background

When using words like culture or values, it often generates skepticism for the business person. The topic of conversation is typically about tangible items that are known to impact shareholder value – EPS, EBIT, ROI, IRR, margins and revenue growth. While these measures can be tallied on a calculator, organizational culture is categorically an intangible. Culture is the behavior of employees and the manner in which they execute against major objectives. Culture is "the way we do things around here". Examples include routine things like expected work times and dress; executive perks; parking assignment; rewards and recognition; titles; how information is communicated; how conflict is dealt with; hiring and termination practices; how empowered the workforce is to make decisions; the degree of clarity around goals, the difference in overall compensation between management and employees; what level of staff receive stock options; the degree to which risk is tolerated; the emphasis on innovation; the degree to which the company is technologically-oriented; etc. It is the how, not the what. A company's culture is essentially its personality, and it differentiates one organization from the other. (Schein, 2004)

Recipe first, then ingredients

There is evidence that suggests that there is a positive correlation between those companies with strong cultures and those companies with increased revenues, higher stock prices, improved net incomes and stronger employee commitment. For mergers and acquisitions, these studies have also shown a correlation between cultural differences and failure to meet shareholder expectations (Bekier & Shelton, 2002; Henry, 2003; Mergerstat, 2003). Cultural differences stand out as a critical factor in prolonging the integration and causing synergy milestones to be missed. It is no wonder that two companies merging with two distinct corporate cultures could have trouble integrating. Perhaps the most frequently cited case of corporate mismatch is the Novell purchase of WordPerfect in 1994 for $1.4 billion in stock. At that time, WordPerfect was the world leader in word processing software. However, in January of 1996, Novell sold WordPerfect to Corel for $200 million. This represented a loss of $1.2 billion, or 86% to the shareholders. In the shareholder suits that followed, Novell's inattention to the tremendous differences in the two cultures was cited as one of the main reasons for this failure. When Novell tried to impose its bureaucratic processes onto WordPerfect, the young, casual, entrepreneurial behaviors of the WordPerfect workforce were stifled. Productivity went down and time to market and cost went up. Soon the advantage of WordPerfect to Novell was lost, and it was sold to Corel (Hackney, 1995).

This article illustrates a case study to describe a culture integration approach designed to assess organizational cultures, highlight potential culture clashes between the given cultures and consider relevant interventions. The case study presented in this article has five components: 1) creating an organizational culture model; 2) assessing the organizational culture; 3) understanding the results and highlighting potential culture clashes between the assessed cultures; 4) identifying applicable interventions; and a 5) review of lessons learned. At the time of this writing, several of the mentioned interventions have been implemented while several interventions are at the post-planning/pre-intervention phase.

The Taste Test: A Case Study

Chocolatier Financial Services (abbreviated Chocolatier) intended to use acquisitions as one piece of its growth strategy. Chocolatier had a history of double-digit growth, and had acquired a number of companies. As Chocolatier prepared for its largest acquisition to date, the management team took the time to reflect on past integration activities.

The magnitude of this acquisition and its complement to Chocolatier's existing core products and the potential to enhance return on shareholder value caused the management team to emphasize the importance of a successful integration. Noting previous merger mistakes, Chocolatier's management decided to include culture as a key focus of their integration efforts. Chocolatier's first challenge was to identify a suitable model and plan of action. A merger integration team was assembled with leadership representatives from both organizations. Even though Chocolatier clearly acquired Company B, the merger integration team wanted to assess and adopt the best practices from each culture and integrate them into the unified company.

Everything but the Kitchen Sink: Creating an Organizational Culture Model

High performing cultures have been linked to better than average stock returns; increased revenues and improved net incomes; the ability to support sustainable change; and improved staff motivation and staff performance (Deal & Kennedy, 2000). In other words, high performing cultures are responsible for overall corporate strength. It is this rationale and body of research that has lead Chocolatier down the path of focusing on cultural integration.

Knowing what you want (successful integration of company culture) is not enough to help you achieve your goal. There are many aspects involved in identifying, then integrating an organization's culture. An important element is to define an excellent company culture. This becomes the benchmark against which to measure the existing company culture and note areas for improvement. For Chocolatier, there were two related but independent purposes in performing a cultural assessment. Given that this was Chocolatier's first culture assessment, there was a need to diagnose the cultures, identify the differences between the two cultures and to determine which best practices to adopt. In the case of Chocolatier, this was the more immediate need. The second was a future *potential* endeavor of taking the merged companies to the next level and developing a "high performing culture". For Chocolatier, plans to develop a high performing culture were targeted for the post-close phase of the project. To accomplish this, there are a variety of methods to consider. In Chocolatier's case, in the approach we selected, we began with scientific data collection, then moved to the synthesis of the data relationships into a model, followed by testing those relationships. Overall, this approach drives the ultimate focus on data collection and model development.

Developing the Instrument

The leap from theory to practice includes an assessment of the current state. There are several well-known methods for identifying and assessing corporate culture characteristics. These range from an indirect approach (e.g., reviewing analysts' reports, annual reports, press releases, etc.) to a direct method (e.g., interviews, work place observations, focus groups, etc.). Variables that determine which method to use include quality of results, cost, time and accessibility. For the purposes of this project, Chocolatier decided to use a culture survey as the means for gathering this information. A survey was determined to be less time consuming and less expensive than more labor intensive methods. The survey was seen as a compass, directing Chocolatier to which future areas and potential culture differences to address.

In determining which survey to use, an extensive search was initiated to identify possible vendors. After completing a thorough search, the company decided to develop its own survey. This was based on the belief that it would be less expensive, provide more company-specific information and be easier for reuse.

To embark on this initiative, several hundred adjectives and phrases characterizing culture were created to characterize organizational culture. These were identified by the office of merger integration through interviews and research of critical issues for the merger integration process. This was conducted in the pre-close due diligence phase of the integration, knowing that subsequent post-close focus groups would help validate the results. An initial list was put together pairing opposites, and a pilot project was initiated with a small group of employees. Originally, there were 6 domains on the CMI. From this initial pilot, Chocolatier was able to statistically determine which items loaded onto the major domains of the assessment and condense the number of domains with the use of Scree Plot. This was accomplished by running the statistical test of factor analysis. Factor analysis helped to determine the statistical structure of the CMI items and the degree to which they measure the given domains of the CMI. The process began with exploratory analysis with the attempt to define factors in mathematical terms. The goal was to identify which factors on the CMI accounted for the most variance. This process resulted in selecting three factors which accounted for 58% of the variance. This suggests that the factors described the relations among the CMI variables well. After condensation, the factors were transformed by rotation. The rotated factors helped to divide up the variance in a more useful manner.

The major domains of the assessment are leadership, decision making and planning. The *validity* refers to the degree to which the instrument measures what it intends to measure. The *reliability* refers to the degree to which the instrument consistently measures what it intends to measure. The statistical properties of the survey reflect the domains. The leadership, planning and decision making domains account for 58% of the variance. The leadership domain has an alpha reliability of .8698; planning domain has an alpha reliability of .7587; and decision making has an alpha reliability of .5906. Two of the three domains have alpha reliability of >.70. Revisions are underway to the survey to remove items that inadequately correlate to the underlying dimensions of the survey and to incorporate items that correlate more positively to the decision making domain.

Subsequent pilots allowed us to winnow, what has been named Culture Merger Integration Survey (*CMI)*, down to its existing format of 52 item pairs. Participants, a broad range of Chocolatier employees, were prompted through the company's e-mail system to click on a link to a secure internet website where the assessment was administered. Employees found this process more convenient to complete than paper-based surveys.

The scale used on the CMI is a bipolar adjective 7 point scale. On either end of the scale are the 52 characteristics describing organizational behavior in the areas of leadership, decision making and planning. The 7 points allow the respondent to select to what degree they evaluate their organization on the 52 characteristics. Adjectives with higher values were derived from previous research on characteristics of high performing cultures (Deal & Kennedy, 2000; Kotter & Heskett, 1992; Dennison, 1997). Table 1 displays the bipolar adjective scale with two items and their definitions from the CMI. Table 1 shows items specifically from the leadership domain on the CMI.

Measure Twice, Pour Once: Assessing the Organizational Culture

The CMI Survey was designed to assess the operational behavior of an organization on three broad organizational factors: leadership, planning and decision-making. The CMI instrument, a self-report questionnaire, was used for three primary reasons: 1) to discover the *current state* of the culture in Chocolatier, 2) to identify potential cultural clashes between the two companies, and 3) to understand gaps between high-performing cultures and the actual organizational culture (current state). Cutoff scores were determined to differentiate higher from lower performing cultures. From previous research, cutoff scores were derived from a benchmarking study. By comparing average scores on behaviors from high performing cultures to those same behaviors identified on the CMI, scores were grouped into high, average and lower performing organizational cultures (Deal & Kennedy, 2000; Kotter & Heskett, 1992; Dennison, 1997). These scores are particularly helpful when comparing *current state* to *ideal state*. They are also helpful in determining which culture characteristics to *adopt* when comparing two companies.

Data Collection. The CMI Survey was administered to managers from both companies. Efforts were made to administer the survey to a representative group given several categories within the two companies: location, business unit, functional area and management level in the organization. Chocolatier had 210 who responded to the survey with a response rate of 57% and Company B had 239 who responded to the survey with a 90% response rate.

Chocolatier leadership decided early on to use an “adopt and go” strategy to integrate the two companies. This method identifies the strongest existing procedures, processes and practices in the two companies and adopts them going forward. Trying to achieve a more perfect “high performing” culture was seen as too difficult during the integration phase and deferred to a future post-close integration stage. Sampling efforts involved selecting representative participants from the demographics of each company, including business unit, department, position level and geographical location. Fifty-seven percent of the intended population responded from Chocolatier and 92% of the intended population responded from Company B. In both cases, adequate responses were obtained**.** The response differential was attributed to the general lack of opportunity historically for Company B employees to “tell their story”. They were, in effect, “feedback deprived”. Chocolatier employees, on the other hand, was given regular opportunities through various surveys and forums to voice their opinions and were weary of feedback mechanisms.

The Proof is in the Pudding; Comparing the Results

Chocolatier’s culture results. Figure 1 shows the scores for the three domains of leadership, decision making and planning for Chocolatier and Company B. As outlined in Figure 1, the CMI scores for Chocolatier indicated that this corporate culture, when compared to other high performing cultures, is categorized as a mid-range performing culture, with employees who appear to have adequate confidence in its current leadership guiding the business, with ample strength in planning and noted deficits in the area of decision-making.

Company B's Cultural results. Figure 1 shows the overall results for Company B. When compared to other high performing organizations, these scores suggest a mid-range performing culture with moderate scores in leadership and decision making and lower scores in planning. Results from the CMI showed that Company B had clear room for growth in each of the domains; however, its score on planning revealed a risk to the sustainability of the business.

Is it Cherry Pie or Rhubarb, and Does it Matter? Cultural Differences

Is there a significant difference on each of the average domain scores for the two companies? To assess whether there was a significant difference, hypothesis testing was conducted with the assumption that the two groups were independent of each other. The index used to find the significance of the difference between the means of the two samples was the t-test for independent samples. While there were differences between the two groups on the individual CMI items, the individual items did not have enough precision to articulate the differences. The intent was to uncover whether there were significant and practical differences between the two companies on any of the given domains. Results showed that similarities existed when comparing the two companies on the decision making domain. Significant differences were found in the area of leadership while the most significant difference for Chocolatier and Company B was in planning. Table 2 shows the differences between the two companies on four of the items in the leadership domain.

Based on the findings from the CMI Survey, Chocolatier clearly presented itself as stronger in leadership than Company B. This was consistent with anecdotal data identified in the due diligence phases of the integration work. This is attributed to the fact that Company B was still run much like a privately held company even though they were publicly traded.

Chocolatier's leadership style was depicted as one of open communication, empowering their employees in decision making, and delegating projects when necessary in the context of a democratic environment. On the other hand, Company B's leadership style was marked by closely held communication, and hierarchical decision making in the context of an autocratic setting.

Table 2 shows differences between the two companies on eight of the planning items on the CMI Survey. Overall, Chocolatier scored higher than Company B in planning, particularly in clear strategy, goals and priorities; however, in the area of long-range planning, Chocolatier scored unexpectedly lower than Company B. In further analysis, this apparent discrepancy can be explained by the fact that Chocolatier's focus was on the integration of Company B. The planning, therefore, was short-term, tactical and time-limited.

In the area of planning, Company B scored significantly different from Chocolatier. There were several underlying concerns related to planning. Not only were executives from Company B used to executing "on the fly" and seemed to have tremendous luck with this haphazard approach, but Company B's communication followed a similar pattern. According to the survey, communication was not always thought out or planned ahead of time.

A dab of this…a dab of that: Interventions

Validation and Intervention Planning. A Culture Team, comprised of key players from both Chocolatier and Company B, was assembled by the merger integration office to orchestrate the Culture project. Team members were selected based on their roles and sphere of influence in their respective organizations. Special efforts were made to include representatives from the business, human resources, communications, merger integration and organizational development. While the Culture Team had HR as part of its membership, the team was driven by non-HR integration leads. The Culture Team retained the support of a consultant to assist with collecting data and the culture assimilation process. The Culture Team's primary goal was to identify potential cultural differences and to prescribe interventions to help managers deal with those differences. Expected outcomes for this team included identifying differences, validating the survey findings, developing a plan and executing this plan.

The Culture Team decided that it was critical to validate the overall findings from the CMI Survey and to dig deeper on areas that needed further clarification. The merger integration team also recognized the potential bias of the culture assessment given the timing, being the pre-close phase. The decision was made to conduct focus groups with representative employees from both companies to validate the findings from the CMI. From this perspective, the CMI Survey served as the compass and the focus groups served as the road map. In fact, the CMI Survey revealed the general direction that the Culture team needed to follow. Focus groups highlighted the specific roads for the companies to arrive to their unified destination. Additionally, focus groups were used to validate survey results, collect employee feedback about their greatest concerns, and attempt to resolve discrepancies and to assist in change management efforts.

There were several areas where the Culture Team needed to partner with other functions in the organizations to accomplish its goals. One aspect was in the area of retention of key talent. In this case, HR played a lead role in conducting capability analysis and structured interviews to select key leadership from both companies.

Two leadership initiatives were planned by the Culture Team. Since leadership from Company B scored significantly lower on the leadership domain, the plan included assisting leaders from Company B to adapt to higher performing behaviors. First, leaders from Company B will undergo a similar assessment and feedback process as Chocolatier, so they will receive individualized feedback on their leadership strengths and weaknesses. Second, after understanding personal weaknesses, leaders from Company B are expected to participate in executive coaching and development to close gaps and set them up for success.

To manage the considerable change created by integrating the two companies, several change management initiatives were adopted. First, leaders from both companies will go through change management training. In general, when employees are not open to change, the leaders will be encouraged to focus on building trust and communicating openly before introducing change. Second, the employee focus groups are used to clear up any misconceptions and hear employee concerns. This allows employees to not only recognize the fear of change, but also to create a sense of buy-in to the merger. Third, the Culture Team will partner with the communications department to distribute timely and planned communication regarding the merger. Finally, in addition to the financials, success of the entire endeavor will be measured by employee retention, customer retention, achieving integration synergies, employee productivity, employee satisfaction on annual survey and the speed and ease of adoption of new policies, procedures and practices.

Stick a Fork in me…I'm done! Summary and Recommendations

Incompatible or conflicting cultures often have been cited as obstacles in integrating companies successfully. By assessing the cultures and understanding potential culture clashes, relevant interventions can be identified.

Rationale Revisited

By developing, piloting and refining the instrument, Chocolatier was able to create a credible data collection instrument for current and future projects. This makes the process of comparing the company culture with those of the acquired companies, an easier task. In addition, the analysis of the data helps create an internal database, which can be used over time for ongoing gap analyses and change management. It is also possible to compare and contrast different business units within the Chocolatier and determine if the differences are critical enough to require change efforts.

While there is some initial cost in the development of the instrument, the cost is more than offset by the ability to administer the instrument over time, ease of administration and having business specific (versus generic) interpretations of the data. The instrument can also change over time as the company changes.

Lessons learned

The process of designing and developing a cultural integration process was not all *smooth sailing*. In fact, there were many areas in retrospect Chocolatier would have done differently.

1. Get early executive and HR support. The HR/OD group often feels ownership of such processes and is reluctant to let them be developed independently. Initial roadblocks occurred because of putting the project ahead of collaboration. Early collaboration and consensus building is critical to the final success of the project. Without the early and frequent involvement of HR and key business executives, the project is doomed for failure.
2. The Culture Team must be cross-functional and cross-organizational. The team cannot be dominated by HR/OD professionals. Early credibility suffered because it was initially seen as another HR initiative. HR/OD should guide the process, but representation should include all areas that will be affected including operations, sales, marketing, IT and finance. These initiatives are often viewed as “soft” by business people, and without the right composition on the Culture Team, the project will struggle.

3. Allow time when you are building your own instrument to do the proper research and follow a scientific approach. The pressure to get survey results quickly so that early interventions could be developed competed with the time necessary for a systematic scientific approach.Initial returns were hampered by being expedient rather than thorough and disciplined. By having a series of pilots followed by rigorous statistical analysis, the survey will ultimately be robust and have the consistency and reliability required for credible results.
4. Enlist an expert in statistical analysis and test design. Whether internal or external, these skills are a must for developing a viable instrument. Without such expertise, confidence levels in the instrument and intended measures weaken.
5. Make the results actionable. Too many surveys end with the data rather than data that lead to action items. Interventions should be specific, measurable, and realistic. Execution is paramount. Without execution there is no need for a survey.

This has been an experiment in designing a culture integration process which utilizes culture assessment to facilitate the integration of two cultures. Chocolatier developed a robust approach with a repeatable integration process and actionable results. While it is still new, the early results are promising. If successful, Chocolatier believes the process will dramatically improve the time to identify, plan and execute on integrating culture issues.

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Table 1.0 Sample Items from Culture Merger Integration Scale

Autocratic Tightly controls employees, directive, more hierarchical; dominating leadership	O O O O O O O	**Democratic** Inclusive environment, values participation and input from employees
Closely Supervised Tight management of employees, leaves employees uncertain about authority and, with the need to *check-in* for permission	O O O O O O O	**Empowered** Promotes employees' independence; employees are entrusted with responsibility and authority to complete tasks

Table 1. CMI items, including definitions, displayed from the leadership domain.

Figure 1.0 Score Comparison of Chocolatier & Company B

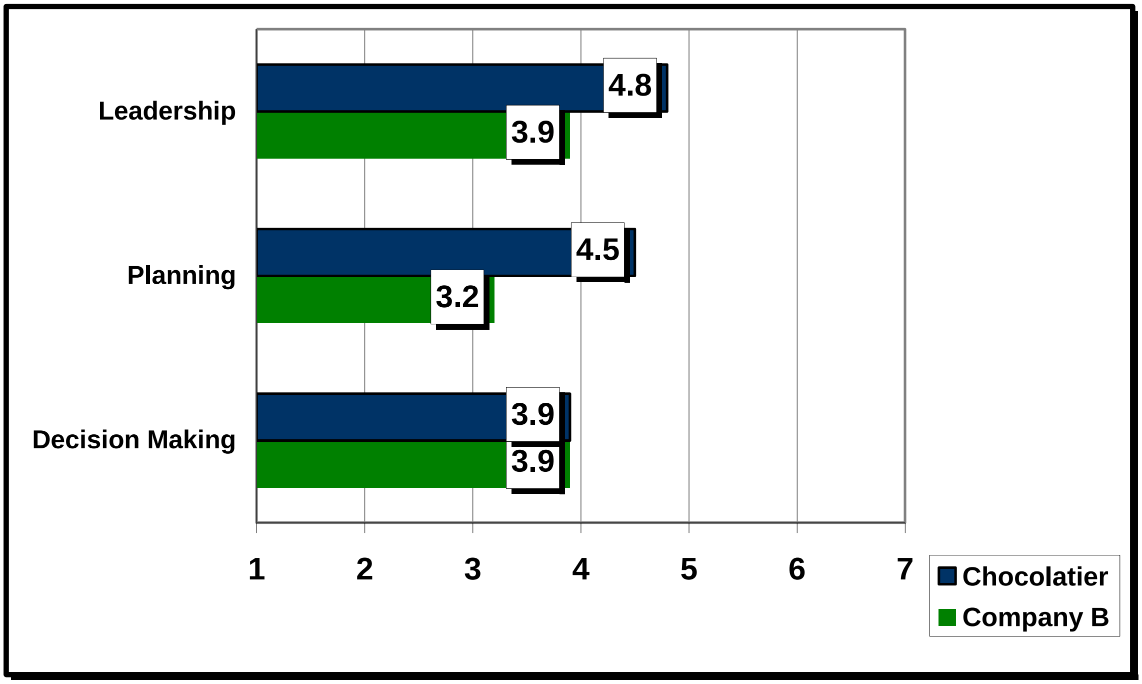

Figure 1. The comparative scores depicted for the three domains of leadership, decision making and planning for Chocolatier and Company B.

Table 2.0 CMI Item Scores (Leadership & Planning Items)

Item	**Chocolatier**	**Company B**
Open	5.6	3.4
Empowered Decision	4.4	3.4
Delegate	5.1	4.1
Democratic	4.3	2.8
Planned Communication	4.7	3.6
Clear Strategy	4.5	3.1
Proactive	4.6	2.9
Clear Goals	4.7	3.4
Clear Priorities	4.8	3.0
Strategic	4.1	3.1
Long Range Planning	2.5	3.7
Performance Rewards	3.8	5.1

Table 2. The individual scores displayed for the two companies on four of the items in the leadership domain and eight items in the planning domain.

BIOGRAPHY

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