

Treasury's Role in the Merger Integration Process

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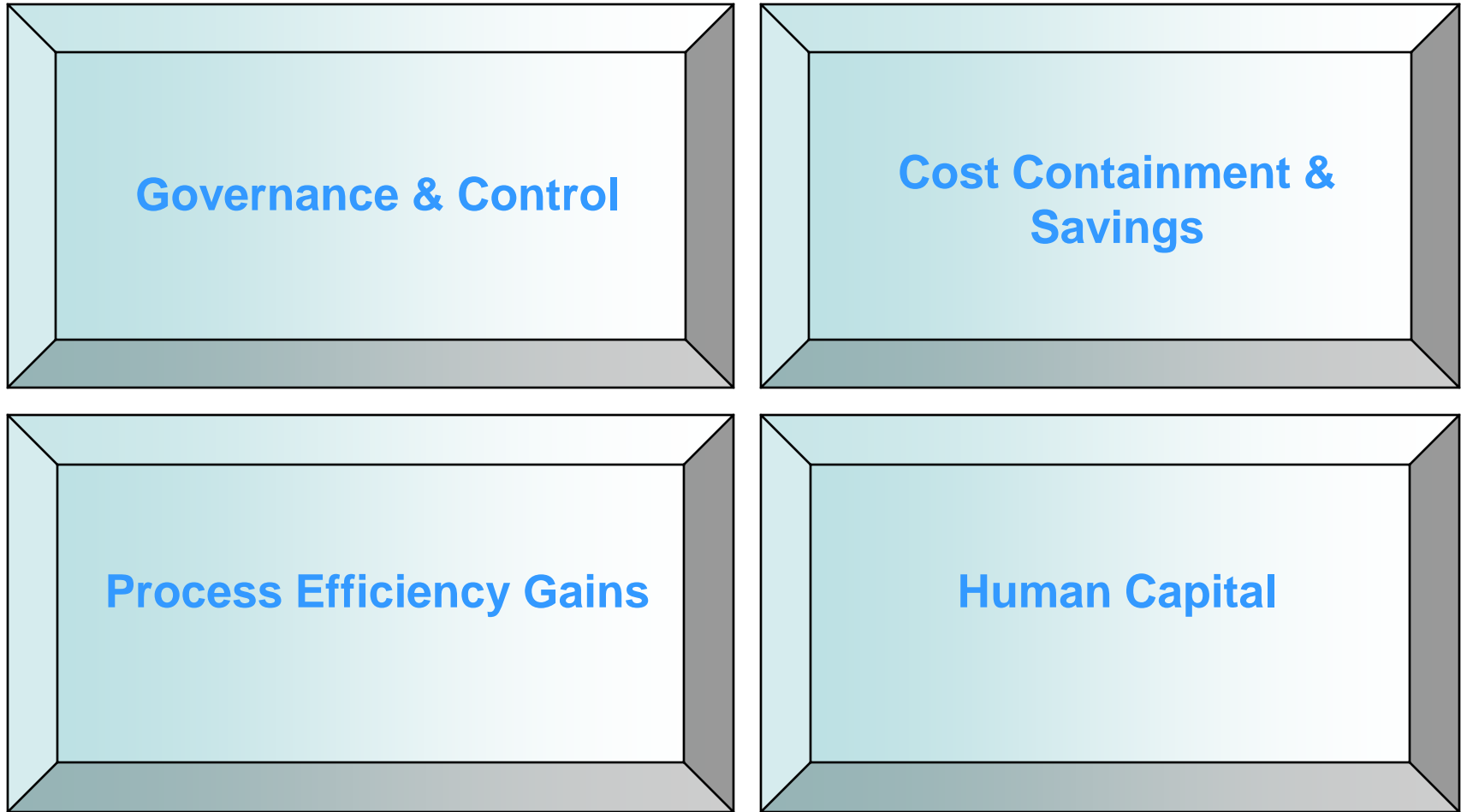
Why talk about Treasury integration?

- Treasury has been slow to penetrate its company's merger and acquisition activities
- When it has, its involvement has generally begun near the close of a transaction and is of an operational or tactical nature
- These tactical issues cover basic areas such as:
 - Where is the Cash?
 - Whose names should the bank account be in and at which institutions?
 - What is the state of bank and treasury systems to gain access to data?
- There is a need to focus on more strategic issues relating to treasury that can contribute greatly to the success of an M&A event

Merger/Integration Challenges for Treasury

- An effective integration depends on having a detailed execution plan that is structured to support the goals of the acquisition
- The execution plan must include pre- as well as post-merger elements, requiring treasury to be involved at the earliest possible planning states
- The post-merger plan should include short-term (30/60/90 day), as well as medium to long-term integration goals
- In its evolving role from tactical integrator of critical financial functions, there needs to be a greater focus on creating synergistic value through treasury's efforts in the integration process

The Four Quadrants of Value



I. Governance and Control

One of the first responsibilities is to gain control of the acquired company's financial assets, as well as redirect the decision-making processes within treasury. Some key actions include:

- Gaining immediate control of acquired company's cash, investment, and banking activities
- Identifying and mitigating financial risk issues such as currency, interest rate, commodity, credit, etc. Including controlling the management and execution of derivatives
- Oversight and control for the granting of guarantees, customer credit, and payment terms
- Identifying and controlling all financial/treasury technology
- Reviewing, revising, and integrating policies, procedures, and SOX 404 documentation of the acquired company's into the acquirer's

II. Cost Containment and Savings

In the treasury space, savings can come from reduced banking fees due to consolidation, more efficient and combined treasury processes, and staff reduction due to the combination and service outsourcing. Even greater savings can be found by treasury working with the business units in the following areas:

- Developing a better understanding of pricing formulas to measure the impact of market factors such as currency, commodity and interest rates
- Supporting the redesign of the planning processes through more accurate cash flow forecasting methodologies, forecasted balance sheets and budget rate selection
- Supporting the business side of the integration by acting as in-house consultant to business units to help resolve the issues that “touch” the treasury/financial space

III. Process Efficiency Gains

Increased process efficiency will not only allow the treasury area to function more smoothly, but also, when properly thought out and implemented, these changes can contribute to additional savings. Since these efficiencies are generally unique to each company, the following represent steps to identify and achieve process efficiency:

- Immediately identify a treasury liaison contact in the acquired company's treasury
- Determine an optimal, combined treasury organization future state
- Establish efficient data collection methods
- Assess technology needs of the combined treasuries and perform a "gap analysis" to determine additional technology and system requirements
- Determine the need/benefit of alternative financial structures such as netting, pooling, finance companies, trading companies, etc. This element must be coordinated with the acquiring company's tax department

IV. Human Capital

Too often the human capital elements of a merger are ignored and the main focus is on the business integration itself, creating insecurity in both the acquiree and the acquirer. Some important early steps to be taken related to the treasury space may include:

- Perform a detailed task/needs review for the combined company
- Quickly identifying key “at risk” staff vital to the integration’s success and have confidential discussions regarding their career paths in the new organization
- Communicating a clear, forward-looking plan to the treasury staffs of both companies
- Identify a treasury leader tasked with handling integration, process improvement and change management coordination issues and responsible for establishing, where possible, two-way communication with treasury staff

Treasury Integration Areas

The entire gamut of treasury functions needs to be mapped into the company's overall M&A planning process early on to add value to the future state treasury organization and the company as a whole

- **Forecasting & Planning**
 - Cash flow
 - Currency exposures
 - Variance analysis
- **Corporate Finance**
 - Capital structure design & management
 - Short & long-term borrowing strategy
 - Short & long-term investment strategy
 - Dividend policy
 - Medium/Long-term Equity and Debt Financing
- **Governance & Controls**
- **Inter-company Financing & Vehicles**
 - Loans & dividends
 - Netting & cash pooling
 - Transfer pricing
 - Tax advantaged strategies
- **Insurance Risk**
- **Investor Relations**
- **Treasury Systems**

Treasury Integration Areas (cont'd)

- **Bank Relations**

- Relationship management - investment & cash management banks
- Guarantee & bank line management
- Account monitoring & documentation
- Cash management services
- Compensation and account analysis

- **Cash & Liquidity Management**

- Collections & disbursements - manual, electronic
- Receivables & payables management/cash flow interface
- Cash concentration
- Investment portfolio management
- Commercial paper issuance
- Float management

- **Financial Risk Management**

- Currency, interest rate, credit, equity, & commodities
- Exposure definition, identification & quantification
- Business specific strategies
- Ongoing strategy development & implementation
- Trade execution, confirmation monitoring, performance analytics & reporting

Treasury Integration Areas (cont'd)

- **Treasury Systems**
 - Application management
 - Technical infrastructure
 - User support modeling & services
 - Data maintenance and updating
- **Risk Measurement & Business Analytics**
 - Financial risk measurement, scenario analysis & risk tolerance
 - Business support and liaison
 - Counterparty risk analysis
 - M&A support
 - Business analytics
- **Accounting & Reporting Considerations**
 - Derivative valuation
 - Mark-to-market pricing
 - FAS 133
 - SEC disclosure & other regulatory reporting issues
- **Employee Benefits (Administration, Compensation/Options, Pensions and Asset Management)**

Critical Treasury Topics to Examine

- **Treasury Organization: Roles and Responsibilities**
- **Policy, Procedures and Controls / SOX 404**
- **Management Reporting**
- **Cash Management and Banking**
- **Investing & Bank Debt**
- **Financial Risk Management**
- **Treasury and Risk Systems**
- **Pensions and Savings Plans**
- **Other Liabilities**
- **Staff Migration/Attrition**
- **Investor Relations Impact**
- **Execution Plans**

Appendix

Treasury M&A Checklist

Treasury Organization: Roles and Responsibilities

- **Develop model of Treasury Organization:**
 - Identify and map treasury functions
 - Determine extent of Treasury activities performed by Corporate office and business units
 - Measure extent of technical expertise of Treasury department
 - Identify unique treasury experience requirements that need to be supported
 - Asset securitization
 - Commodity risk management
 - Working capital management
 - Define future state Treasury resource requirements, including skills and people needed

Policy, Procedures and Controls / SOX 404

- **Determine new/revised treasury processes and procedures for the merged entity**
- **Evaluate the treasury systems that will support the merged entity. From a SOX 404 perspective, residual legacy systems create issues**
- **Update policies to reflect the merged entity**
- **Evaluate and update all SOX 404 documentation to reflect new procedures, processes, systems and hand-offs**
 - Develop testing strategies for new treasury control environment
 - Execute treasury testing strategies
 - Remediate identified issues

- **Information pertaining to Treasury integration issues to PMO**
- **Development of the Treasury reporting requirements of the combined organization**
 - Treasury reporting requirements for all levels of the organization
 - Frequency of required reporting
- **Design and implementation of new Treasury management report to different levels of the organization**

Cash Management & Banking

- **Develop understanding of business activities generating collections and disbursements**
 - High Value/Low Volume versus Low Value/High Volume
 - Domestic versus cross border
 - Local currency versus foreign currency
- **Determine supporting cash management infrastructure requirements**
 - Lockboxes
 - Disbursement accounts
 - Payroll requirements (check, electronic, direct deposit)
 - Cash concentration
- **Inventory existing bank relationships and accounts**
 - Bank, account number, purpose and type
 - Bank fee/service prices
 - Foreign currency accounts
 - Petty cash
 - Authorized signers and signatory limits

Cash Management & Banking

- **Map electronic cash management services**
 - Workstation(s)
 - Balance reporting
 - Security procedures for wires
 - Access and passwords
 - Cash accounting and bank account reconciliations
- **Determine key dates**
 - Interest and/or principal payments
 - Fees
 - Lease payments
 - Other settlement dates

Investing & Borrowing

- **Investing**
 - Investment policy
 - Schedule of investments indicating related portfolio return
 - Who is authorized to invest?
 - Confirmation process
- **Borrowing**
 - Determine all existing debt arrangements
 - Prepare debt amortization schedule
 - Identify potential “events of default”
 - Determine extent of collateralized or securitized debt

Financial Risk Management

- **Review financial risk management policies (foreign exchange, interest rate, & commodity)**
- **Determine business activities that generate financial exposures**
- **Quantify financial risks (anticipated and booked)**
- **Obtain details of open contracts**
 - Spots and forwards
 - Options, futures or other derivative products
- **Prepare listing of authorized company traders, confirmation procedure, trading banks**
- **Review recently reported underlying gains/(losses) primarily for foreign exchange**
- **Understanding accounting impact of gains/(losses)**
- **Determine status of FASB 133 compliance**

Treasury Systems

- **Evaluate the treasury system needs of the combined organization, both short term and long term.**
- **Benchmark the treasury system needs to the current treasury system's capabilities and functionality and identify gaps.**
- **If material gaps are identified, evaluate alternative treasury systems.**
- **Implement and transition to the new treasury system.**

Pensions and Savings Plans

- **Plan documents**
- **Amendments**
- **Summary plan descriptions**
- **Loan policy documents**
- **Administrative procedure documents**
- **Administration forms**
- **Recent participation allocation statements, summary annual report**
- **Historical plan contribution levels**
- **Actuarial valuations**
- **Trust asset information**

Other Liabilities

- **Leases**
 - All terms and conditions, including events of default, change of control clause
 - Escalation and adjustment clauses
 - Renewal and purchase options

- **Letters of credit**
 - Trade or standby
 - Purpose, fees
 - Any change must be approved by beneficiary

- **Guarantees/comfort letters**

Staff Migration/Attrition

- **Sensitivity to human factor**
 - Define future state Treasury resource requirements
 - Conduct detailed interviews with Treasurer and direct reports to identify potential candidates
 - Develop task absorption plans
 - Begin transition discussions with potential candidates

Execution Plans

- **Develop communications for organizational change impact on Treasury groups**
 - New organizational structure
- **Identify Treasury integration team members**
- **Develop Treasury integration plans and timelines**
 - Identify critical tasks/functions to be integrated from acquired entity
- **Design new banking structure to optimize liquidity management and efficiencies**
 - Develop bank integration work plan/timeline
- **Schedule regular meetings to discuss progress and issues of the Treasury integration**
- **On going communication with:**
 - PMO on Treasury issues
 - Staff on Treasury merger/integration issues