Unethical Practices Spoil the Value of Mergers, Acquisitions, and Divestitures

an eprentise white paper

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The acquisition has been announced. Company A is going to sell the B part of its business to Company C. The entire organization is trying to complete the close in a very short window. The regulatory team needs to file all the paperwork set up the new legal entities and the change in ownership. The finance team is trying to close the books and make the necessary close transactions, HR is busy with realigning benefits and determining the transfer packages for those employees going with business unit B, and Company C is doing all the HR capital acquisition. The legal teams are focused on the transition services agreement, on actually closing the sale of Company B for Company A, and on the acquisition by Company C. In the meantime, the executives of both companies are focused on planning for the new companies; Company A is planning what they will do with the capital that they receive from the sale, and Company C is planning on getting value from the acquisition, and determining how Company B will align with their future vision. With all the hoop-la surrounding the deal, little attention is paid to day-to-day transactions.

In fact, many of the usual controls are bypassed, and especially the accounting team focuses on paying the outstanding bills, ramping up collections so that the final financials can be prepared. In my experience working with many large companies going through a divestiture or an acquisition and from an informal survey of several large suppliers and service contractors, the chaos presents a unique opportunity for suppliers. These suppliers will often send an invoice to Company A, the same invoice to Company B, and then again to Company C. This could be easily construed as a defensive move, wanting to be sure that someone pays the bill, but unsure of which entity will actually pay it. However, it is very often a common practice with large suppliers when there is an acquisition in play, to create multiple invoices, pad the bills, mark them as overdue, or even charge for services not provided. My experience in the business world (and that of several others whom I asked) tells me that vendors very frequently bill all three companies and very often get paid by two or all three of them. It's easy to see how individual invoices can get overlooked during the transition period, and assumptions of who has the responsibility for particular invoices can lead to duplicate or even triple payments. Further, in my experience, these suppliers do not return the excess payment(s). In fact, for one company that I talked to, duplicate billings to companies doing an acquisition accounted for more than 20% of their annual revenue. This practice is, of course, unethical and, if multiple vendors are doing the same thing, can cost Companies A, B, and C hundreds of thousands of dollars and can quickly eat into the value of the acquisition.

There are four major steps that companies can take to circumvent these costly oversights.

1. As part of the transition, clearly separate individual transactions that will belong to each organization. There are several ways to separate the data: If Company A is responsible for invoices, then Company B or Company C should not even be able to view those transactions. If Company B is responsible, then the purchases, orders, or contracts should be closed out in Company A. If Company C is going to assume the liability, then there should be a list or open transactions provided to Company C of all the "to-be-paid" items. If there is a split order between Company A and Company B, then the actual transaction should be split along with the liabilities and related payment information. The transaction line items that a company is not responsible for should be end-dated or closed.
2. Each of the companies should routinely run cost recovery software or procedures to identify potential duplicate invoices or payments. Company A and B should identify duplicate payments

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while they are still on the same system during the transition period, and then, after the close date, Company B should work with Company C to make sure that suppliers are taken care of, but that there are no multiple transactions.

3. Close out as many individual transactions as possible before the close date to limit the number of open transactions during the transition period.
4. Maintain a comprehensive audit trail of these procedures before, during and after the M&A takes place. Consider utilizing automated audit tools to help auditors from each company, as well as external auditors, divide the audit scope, include detailed notes, and follow a structured and transparent approval hierarchy. It is critical to have drill down transparency into audit data in order to identify any exceptions and properly document audit conclusions.

This transition planning should take place as early as possible to minimize the effort and the confusion for the accounting team and reduce costs for Companies A, B, and C.

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