



Mergers & Acquisitions Leverage

Transforming insights into M&A solutions

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Introduction

Coming off one of the strongest years in terms of deal numbers and value, corporate and private equity executives anticipate continued acceleration of deal flows in 2019, according to Deloitte's recent "The state of the deal: M&A trends 2019". However, as 2018 closed out, there was a significant drop in deal volume in Europe and an almost 20 percent drop in China. These drops were offset by deals in Japan and India, where deal flow mirrored the volatility and turbulence being observed in markets around the world.

A great number of deals focused on the stability and sustainability of competitiveness and positioning. Regulatory challenges continued on a global basis, with anti-trust assuming greater importance. Finally, while 2017 did not see major moves from the private equity sector, 2018 saw more strategic plays from these firms as they deployed substantial capital around the globe.

In this issue, we focus on the critical elements in achieving and executing a successful deal:

- Andrea C. Mindell highlights the importance of effective and strategic communications, including the need to recognize nuances in comparison to business as usual.
- Piotr Bednarczuk and Alistair Lester share their views on qualifying and quantifying risk effectively, early in the deal flow. They also note how overlooked human capital risks impact a deal's success.
- Harish Venkatachalam unravels the complex, opaque and sometimes irregular Indian market for deals, especially inbound deals.
- Margaret M. Doyle takes on the importance of a thorough understanding of compliance, especially for multi-country or overseas deals, given the costly and complicated efforts required to rectify inadequacies.
- Finally, Rachel Perlman dives deep into managing a divestiture from a people perspective.

The thoughts shared in this edition are a brief summary of our experiences while working on deals globally across a multitude of industries and markets. If these or any related issues are of interest to you, please do not hesitate to reach out so that we may more specifically share our insights.

Jaidev Murti
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M&A Communication Essentials

Don't get caught off guard!

Guidance for communication leaders

Most HR communication leaders are skilled at using communications to drive awareness, understanding and action for events like benefits enrollment, and changes to compensation, benefit or employee development programs. But what happens when an organization decides to pursue a merger, acquisition or divestiture? Do normal communication skills still work?

The answer is yes and no: a lot of the “normal” communication skills that are successful are the same ones needed to lead the communications for a merger, acquisition or other corporate transaction. Corporate transactions present some unique challenges that require a special type of communication leader: someone who can think strategically, is nimble and comfortable with ambiguity, has cultivated a strong internal network and can deliver within especially demanding time frames.

Confidentiality and changing dynamics surrounding these types of transactions mean there's minimal time to develop and implement an M&A communication strategy. And yet, it's a crucial business transaction. That means delivering the right communication at the right time to the right employee audiences.

When brought into the deal, there will be many factors that are not within a communication leader's control. With M&A communication, it's all about putting in place, ahead of time, the tools needed to be proactive to help manage the change that both the organization and the employees will experience.

Using a case study, this article provides guidance on practical, proactive steps to help control communication efforts in often chaotic M&A situations. One of the first steps is recognizing that the fundamentals of good communication practice always matter.

What great looks like

Great M&A communication enables leaders to lead through change, acknowledges employees' concerns, keeps employees focused on doing their day-to-day job well, and can help surface issues and concerns – all of which can contribute to keeping your company focused on ensuring a successful business transaction.

M&A communication defined

For purposes of this article, M&A communication refers to the material and messaging that a company develops to communicate with all of its employees to help them manage through the changes they are experiencing as a result of the corporate transaction. This article does not address individual employee communication governed by legal and regulatory bodies, such as communication related to the acceptance process, unions and works councils, employee transfer notifications, and consultation requirements. These have been addressed briefly in “Breaking-up is Hard to Do—People Aspects in Divestitures” on apac.aonhewitt.com under Resources/M&A Leverage.

Employ the fundamentals

Regardless of the topic, communication campaigns succeed when the communication team partners with key stakeholders to:

- Identify team members' roles and responsibilities.
- Gain buy-in and support for strategy and key messages.
- Establish objectives and a measurement approach.
- Identify key audiences, what they need to know and do, the information and tools they need, and how to best reach them.
- Meet all timing expectations.

In M&A situations, these fundamentals still matter – as much if not more – given how critical the communication can be to the success of the deal.

Case study

Here's how one company successfully approached a time-crunched M&A situation and stayed true to the fundamentals of communication success.

Global consumer products company



The situation

Approximately four weeks before their CEO was set to announce publicly the company's intent to divest a large international division, the company's centralized HR communication team was charged with developing a robust employee communication strategy and plan for the announcement. Common for most organizations, their plan had to take these factors into account:

- The needs of numerous audiences – corporate, regional and country leaders; HR business partners; people managers; external-facing employees; and general employee audiences.
- Local communication requirements and practices, including translation needs.
- The final announcement date was a moving target for most of the time leading up to when the announcement would actually happen.



The approach

Aon partnered with the organization's internal communication team to develop an announcement strategy backed by a detailed communication plan (day-by-day, hour-by-hour, minute-by-minute) leading up to the public announcement. The communication included a CEO video and email, presentation decks, talking points for leaders and managers, Q&As and templated letters for each key stakeholder audience (e.g., customers, vendors) that could be customized at the business and local levels. They coordinated closely with legal and regulatory functions, as well as their media and investor relations leaders to ensure the messaging was in alignment with all public messaging.

In addition to creating a suite of announcement communications, the team also developed subsequent communication to keep employees informed as the deal divestiture progressed.



The verdict

The announcement communication campaign ensured that each audience received clear and consistent messages in a timely manner. Leaders had the necessary tools and resources to communicate with employees and other constituents. Through the transaction, employees remained focused on what the company needed them to do and knew how to get answers to their questions. In turn, employee input helped inform ongoing communication.

Keys to success

The HR communication team was able to achieve a “great” outcome by being proactive when they could, while focusing on the most critical fundamentals. Here's how they did it:

1. Activated internal network

To deploy communication campaigns during the year, the HR communication team had an already established network in their key locations across the globe. This network was comprised of regional heads, business leaders, HR business partners, as well as legal and regulatory experts. The team activated this network during the M&A initiative to help guide strategy and provide insights into local communication needs and resources. For example, the network provided inputs on who should review the content, whether the material needed to be translated, and if so, into which languages, and which communications channels were to be used by local leaders. The resulting strategy had the buy-in and support of the entire network, as local leaders felt they had a voice in its development and the flexibility in execution to adapt key portions to suit their local needs.

2. Created a detailed stakeholder map (Fig 1)

The HR communication team had a disciplined focus on the unique needs of each audience – e.g., leaders, HR business partners, people managers, customer-facing employees, general employee audiences. With guidance from Aon, they then created a stakeholder map to account for key considerations and messages for each audience specific to this transaction. This map helped them develop communication quickly and maintain a disciplined focus on each audience's change and communication needs.

Learning #1

Build your network

Build a network and connect with them in quieter, business-as-usual times, which can be activated when you are called upon to lead an M&A communication initiative.

Learning #2

Know your stakeholders

Create and maintain a stakeholder map year-round to ensure you know your employee groups, their needs and challenges, and how best to reach them.

Fig 1

Creating a stakeholder map



Audiences

- Which audiences are impacted by the change (internal and external)?
- Which audiences are key to ensuring the success of the change and how best to engage them?



Impact of change

- What's the impact of the change (positive and negative) on each audience?
- What's the degree of impact (high, medium, low)?
- What do we need each audience to know and do?



Information needs

- How do we expect them to react to the change?
- What questions do we anticipate from them?
- What information do they need to get through the change?



Barriers

- What are potential barriers to a successful change?
- What's the risk if individuals don't change or take action?

3. Simplified channels

The HR communication team recognized the need to prioritize speed, easy access, and global consistency (while allowing for local customization) into their communication strategy. The majority of communications were created for electronic distribution, and presentation decks were formatted with minimal graphic design. The team relied primarily on emails directly to employees or their leaders who cascaded the messages. They created a new Transition Resource Center (TRC) section on the company intranet site that served as the central repository for all transaction-related communication, including a new mailbox where employees could submit questions. The mailbox was monitored regularly and answers to the submitted questions were posted to the TRC for all employees to see. Every communication promoted and referenced the TRC to ensure employees would use it as the main resource for transaction-related news and information. The simplicity of the format and channels allowed the HR communication team to work nimbly and swiftly to add content as new information was confirmed or as timing changed.

4. Developed content to meet the needs of both the organization and employees (Fig 2)

Critical to the success of the transaction was ensuring that employees stayed focused on continuing to do their jobs well. However, the HR communication team knew employees would be distracted from their jobs if their most pressing issues were not addressed in conjunction with the announcement. These are quite universal issues and included: how will my job, pay and benefits be impacted; what does this mean to my day-to-day work and interactions; and what opportunities will I have with my company in the future. Though some answers were unknown on announcement day, employees still needed reassurance. The HR communication team worked through this ambiguity by communicating what they could through a steady cadence of messages. At the same time, they acknowledged the questions they could not answer, committing to address them when more was known. Action-oriented educational material developed with Aon for in-person and online sessions enabled managers to help employees through the transition.

Learning #3

Simplify your communication

There is little time to design graphically, print or mail material so focus on the quickest, most efficient and most effective ways to reach your employees.

Learning #4

Prioritize your messages

Employees need to understand how they will be impacted by the news before they can focus on what needs to be done.

Fig 2
Corporate transaction communication: priorities and overlaps



Summary

Given how common it is for organizations to pursue deals involving acquisitions, mergers and/or divestitures, HR communication leaders need to be ready at any moment to implement the M&A communication in support of the transaction. By having fundamentals in place and operating smoothly, the communication leader is able to draw on skills and resources needed to develop and implement a successful change and communication campaign. Success is achieved when the needs of both the organization and its employees are identified, understood and addressed throughout the transition.

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Managing M&A from an HR Perspective

Spotlighting a holistic approach on people and risk

Organizations may face many types of transactions, including traditional mergers and acquisitions to joint ventures or spin-offs. The overarching requirement through all of these situations is ultimately securing the value in the deal (Fig 3).

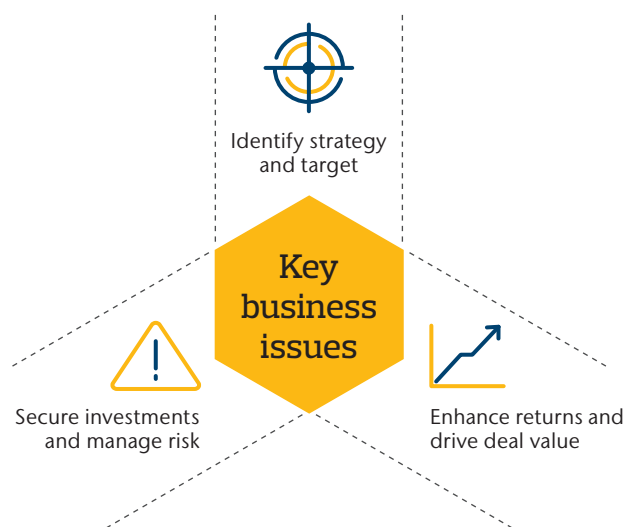
To ensure deal objectives are met, the business will need to consider adopting a holistic approach to truly assess all relative risks involved in the transaction, including the crucial human capital aspects of the deal.

Fig 3

Aon supports inorganic growth holistically

Aon provides significant value for M&A transactions:

- Qualify targets through insights on areas such as risk and insurance, cyber, intellectual property and human capital.
- Secure the investment by managing risk, including downside risk.
- Enhance returns by tapping into insurance as a source of alternative capital.



Organizations that fully assess potential risks early in the M&A process will realize the full value of the deal at closing.

Capture the value of a deal

One way to mitigate the many risks posed by a transaction is to transfer it to the insurance space, where numerous solutions are available to relieve the business of pressures faced by risk in M&A scenarios (Fig 4). Many of these solutions are being driven by private equity companies, with demand from corporate strategic buyers increasing steadily.

Most of the recognized risks within M&A deals are transferrable to the insurance industry for a premium. Anywhere cash and collateral are being tied up for a period of time, strategic buyers are encouraged to look to the insurance market for potential risk mitigation. Aon has vast experience in this space and is actively engaging in discussions with strategic buyers, who wish to leverage our capabilities and expertise.

Fig 4 Enhancing returns: transaction solutions

Liability & Contingent Risk

Warranty & Indemnity Insurance (W&I)

- Provides broad warranties and standard warranty periods to help seller close the deal.
- Enhances the buyer's potential for recovery rather than simply replacing the typical seller's indemnity.

Prospectus Liability Insurance

- Protects against claims alleging a breach of securities law in connection with defective disclosure documents – e.g., an IPO prospectus.
- Claims may allege the related documents contain errors, omissions, untrue or misleading statements or that wrongful acts were committed as part of the sale/offering.
- Typically a policy will pay damages, settlements and defense costs for claims against the company and its directors and officers for claims made against them.

Tax Liability Insurance

- Reduces or eliminates a contingent tax exposure arising from a transaction, investment or other tax position where the underlying legal conclusions may be subject to future challenges by the tax authorities.
- Provides greater purchase price certainty for a buyer in the M&A context by ring-fencing an identified tax exposure.
- Enables a clean exit for sellers by eliminating a long-tail contingent exposure.

Litigation Buy-Out Insurance

- Litigation Buy-Out Insurance enables a client to ring-fence liabilities that may arise from any current or anticipated litigation, arbitration or other dispute.
- Particularly useful in the context of a sale of a business where unresolved disputes would otherwise prevent the sale proceeding or would have a significant impact on the price to be paid.
- Insurance takes this uncertain liability out of the negotiations, allowing the parties to concentrate on the business itself.

Bonding & Surety

Pension Bonds

- Regular actuarial valuations determine the level of (additional) capital that any given company must commit to the scheme.
- A potential solution would be the pledging of surety bonds to the pension scheme trustees. The product is a contingent liability and so sits on the balance sheet. Surety bonds can then be used in a number of ways for deferring and restructuring payment plans, which could free up capital to be used elsewhere in the business, subject to the strength of the corporation.

Deferred Consideration Bonds

- Deferred Consideration is a portion of the purchase price payable by the buyer in the future after closing.
- Purchase price is negotiated on the basis of a fair market value of the target firm.
- Bonds provide a credit solution that mitigate the risk of non-payment by the purchaser.
- Single-risks insurance contracts cover the seller against non-payment of contractual amounts owed under the Sales and Purchase Agreement.

Cash Confirmation Bonds

- Back-stops bidders' obligation to pay target public company shareholders under the terms of the takeover.
- AA-rated surety providers approve bonds in a matter of days.
- Provides comfort to responsible bank and is a key factor in providing the required cash confirmation statement at announcement of a deal.
- Bidder avoids cost of drawing down early under its revolving facility by entering into an escrow agreement/having to ring-fence funds.

Decommissioning Bonds

- Applicable where planning permission or landowner requires provision for reinstatement at the end of the lease term, usually through a Reinstatement/Decommissioning Bond or escrow.
- Surety policy avoids cost associated with these traditional structures and indemnifies the landowner.
- In the event of a breach, non-compliance or contravention of reinstatement requirement by the tenant, the policy is triggered and will pay for the reinstatement of the site.

Achieve huge ROI on risk and capital due diligence

Due diligence is often seen as a cost to the business, but the ability to obtain qualitative and quantitative insights over a broad range of factors is invaluable. Fig 5 describes potential areas of due diligence, especially in critical areas

around cyber and intellectual property. Aon has additional capabilities in these areas through strategic acquisitions with a wealth of expertise available to Aon clients.

Fig 5

Value-added due diligence

Securing investments: M&A solutions

Intellectual Property (IP) due diligence

- Review the relative value of the target company's IP.
- Identify opportunities to maximize value from target companies' IP and patent portfolios.
- Develop strategies to maximize IP value on exit.

Cyber due diligence

- Cyber reconnaissance – a “no-touch, no-knowledge” survey of target's public cyber profile, done on a discreet and confidential basis.
- Pre-transaction assessment – review of controls, procedures, policies and network documentation, done in conjunction with the target in order to get a fuller view of existing risk.
- Transaction assessment – a comprehensive assessment which incorporates technical testing in combination with documentation review.

Risk and insurance due diligence

- Evaluation of past, current and future exposures and other potential issues impacting the M&A deal, including:
 - Risk management.
 - Risk transfer and financing costs.
 - Claims experience.
 - Allocation of responsibilities and liabilities within the Special Purchase Agreement (SPA).

Human capital due diligence

- Analysis and evaluation of retirement and benefit plan design, high-level compliance and market competitiveness.
- Quantification of annual financial impact (including on a pro-forma basis) of retirement and benefit plans, including international benefits plans.
- Executive compensation competitiveness review and design.

In many cases, the people (human capital) risk is seen as a small add-on to many other more traditional areas of due diligence, such as market and financial assessments. The benefit of human capital due diligence is the ability to anticipate integration processes in HR programs before deal close. This is only possible if the due diligence is conducted by a provider, such as Aon, that has the market data internally (data such as current benefit plans, retirement plans and compensation programs) and actively gathers data throughout the deal process, which can be utilized during the preparation phases of the integration process, before close. In addition to data, having the design and operational

execution experience allows us to assess the value capture in advance of the close.

In many cases, data for HR integration purposes is only collected post-close, which means unnecessary and costly delays are incurred. In most situations, synergies are then harder to achieve as a result, directly impacting the deal value and overall process, post-close.

In applying this approach, our experience shows that the ROI for human capital due diligence can be as high as 250 percent on purchase price adjustments.

Securing synergies early in the deal

In addition to data, establishing critical processes early in the deal process enables a swifter start and smoother integration.

Here are some selected scenarios where this is possible:

▶ **Top leadership selection**

Selection process for the top leadership teams can in some instances start before the deal closing, allowing the organization and its team to have a clear organizational structure and leadership accountability from the very outset of the integration process. A well-designed process promotes a positive cultural impact and stability within the teams.

▶ **Culture assessments**

Culture assessments should begin during the early phases of the deal, where information gathering is already conducted during due diligence. The full assessment of differences between the organizations' cultures allows leadership teams to gain transparency around the potential roadblocks for integration and determine which differences are not critical for achieving business results. This transparency allows the teams to have a common language and quickly become a functioning team.

▶ **Human capital benchmarking**

Conducting a pre-assessment of companies from the corporate deal team's potential targets, based on human capital benchmarks and data, allows for a more transparent understanding of human capital issues and impacts.

Two of the biggest challenges within transactions are managing the complex project and tracking the results of the transactions. Based on Aon's experience within the most complex deals, a comprehensive technology-based platform enables the effective management of corporate transactions within the deal process. The platform, TransAction Manager™, kick starts the project management process, from a one-dashboard view, freeing up time otherwise consumed by process and resource allocation in the early, crucial stages of any deal.

Adopting an integrated HR approach (Fig 6)

All too often within the HR workstream, optimization is conducted on an area-by-area basis, e.g., benefits programs are assessed and implemented independent of other compensation elements. Adopting this siloed approach typically increases cost, owing to missing potential trade-off opportunities between HR elements.

For instance, adopting a total rewards perspective allows for more effective negotiations, where "win" and "lose" scenarios are assessed and "trade-off" solutions are developed in advance.

Fig 6
Holistic approach brings better results and higher effectiveness

Looking at each component in isolation may drive wrong decisions.

Competency	ABC Corp.	XYZ Corp.	Considerations
Base	-7% Below market	0% At market	Market position by component vs total rewards
Total cash base plans annual bonus	-12% Below market	8% Above market	Extent of savings in one area can fund other areas
Benefits (employer-paid value)	1% Below market	20% Above market	Willingness to increase one organization’s benefits while reducing the other organization’s benefits

Integration Complexity

Overall	HR Operations	Total Rewards
Division D	\$X Cost Increase	
Division E	Cost Neutral	Cost increase
Division F	Potential Cost Increase	Cost increase

Total Rewards (Buyer/Acquired Value)

Total Cash	Total Direct Comp.	Retire.	Health and Welfare	Vacation /PTO	Sever.	Perks	Other
105%	100%	89%	70%	99%	85%	95%	100%
115%	100%	120%	130%	95%	80%	70%	100%
90%	115%	100%	95%	140%	130%	100%	86%

Based on Aon’s survey done on total rewards in M&A, leading companies focus integration of reward programs on a single platform over a six-month period immediately following the

announcement, and the most successful approach is to adopt a country-by-country process, with priority assigned to countries with the biggest cost/synergy impact.

Summary

Successful integration can only be fully realized if the focus is placed on influencing factors early enough in the deal. Ultimately, companies need to build and strengthen their corporate transaction capabilities in advance of any potential transaction. For the deal to realize its full value, processes, tools and technical up-skilling need to be enhanced. Also encompassed within this process of readiness is the need to design a governance structure to maximize the organization’s effectiveness and to capitalize on the value of any potential, future or impending transaction.

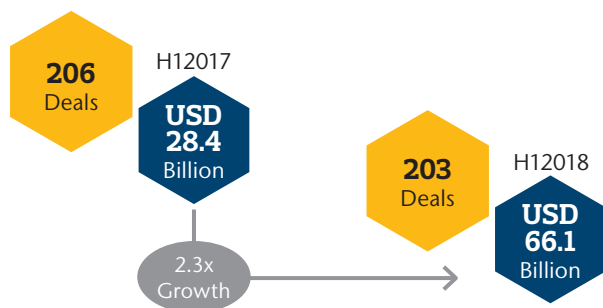
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Impact of Indian Labor & Employment Laws in M&A Transactions

India has seen unprecedented M&A activity in the first half (H1) 2018 (Fig 7). These domestic and cross-border transactions were largely driven by a relatively stable economy, the liberalization of government policies and a continued interest from both domestic and strategic investors.

Fig 7



Global investors with aggressive expansion plans often invest in cross-border acquisitions that fit in with their strategic ambitions. Among the array of strategic, financial and people-related issues faced by investing companies, one of the major pain areas is labor and employment laws in India governing employee rights. Labor laws contain restrictions on transfer of employees, redeployment, redesigning employee roles and responsibilities, recalibrating headcount numbers and employee costs.

Most of the employment practices in India are built on the foundation of pro-labor and outdated employment and labor laws. While the intent during their initiation was to protect labor discrimination, the failure to amend them according to the nation's changing economic and business environment has resulted in multiple hurdles for employers. However, recent years have witnessed attempts to alter a few clauses and relax a few restrictions with a view toward promoting business investments.

In M&A situations, the key labor/employee-related statutory implications usually arise in the areas of:

- Employee Provident Fund contributions.
- Employee state insurance contributions.
- Payment of bonus as per the Bonus Act.
- Pending employee litigations.
- Formation and structure of employee trade unions.
- Pending union settlements.
- Structure of contractual workforce.

A strong diligence on the above matters is key to identifying the depth of impact that each would have on the deal scenario. While some could be identified through verification of available documentation, others might be situational and require a detailed understanding of existing and past operational practices. For instance, circumstances causing labor strikes and lockouts will not have any supporting documentation. Similarly, long pending employee-related litigations could have a history of citations which have not been resolved. Such observations could have material financial and strategic impact on a deal and also provide a view of the existing operational discrepancies. This allows buyers to align themselves strategically and plan for a successful integration or to decide whether to abandon the investment altogether, given the possible negative synergies.

Indian labor laws and the current labor situation are two areas of concern for buyers in cross-border transactions – e.g., acquisitions of Indian operations and multinational companies setup operations in India. Apart from the long list of regulatory approvals, the existing labor environment is of key concern to foreign investors looking for absolute clarity.

Here's how buyers and investors can mitigate the risks

▶ **Employee trade unions**

Many manufacturing setups in India have employee trade unions. These can basically be of two types – internally registered unions with no affiliation to external bodies or unions affiliated to politically proclaimed national union bodies. While the preamble of both is to protect labor rights and interests, in the case of the latter, involvement of external stakeholders in decision-making during collective bargaining adds additional complexities.

Though history is replete with examples of hostile environments created by unions, significant changes have been undertaken with the inflow of a skilled workforce and professionally trained HR personnel.

During M&A scenarios, the key focal point is to understand the union structure, its history of formation, past issues/concerns and associated repercussions. In addition, it's important to understand existing operational practices and how they might need to be altered to cater to the go-forward business strategy.

▶ **Collective Bargaining Agreements (CBA)**

In India, CBAs or “Long Term Settlements,” are usually signed for three years. Like every CBA, it lists out the details of an organization's expectations from its labor workforce, compensation, benefits and related additions or alterations. However, there are instances where the CBAs are delayed due to differences between management and unions. This delay usually leads to operational disruptions which affect productivity, employee engagement and on-going disputes.

In such scenarios, the buyer needs to understand the seller's reasons for such delays and whether these delays can be overcome prior to deal closure. However, the buyer does have the authority to influence the seller on compensation and benefits, as the impact of these decisions will have a cascading financial effect on the future operations of the buyer. The best practice here is to provide Representations and Warranties Insurance in the purchase agreement.

▶ **Employee litigations**

Given the pro-labor nature of the Indian labor laws and the everlasting judicial battles, employee-related litigations are the key areas of concern during M&A. Employee-related litigations may include disciplinary actions, undue termination from services and violation of code of conduct. Judgements toward such cases are usually issued by the Indian Labor Court, which tends to involve an unpredictable amount of time. These types of litigation decisions usually revolve around employee reinstatement and compensation, which may have an unprecedented financial impact.

Therefore, during M&A scenarios, the status of litigations – both past and present – need to be thoroughly verified. While these are critical areas of concern, they are definitely not deal breakers. The immediate resolution that buyers may adopt to protect themselves is to provide for Representations and Warranties Insurance in the purchase agreement, and require the seller to deal with them as and when the judgement comes in. However, in instances requiring reinstatement of a considerable number of the workforce – who may be redundant for the buyer's future operations – identification of such observations during the due diligence process will help in substantiating the go-forward decision of the deal.

▶ **Contractual workforce**

In India, it is a common practice to deploy a third party or contractual workforce in operational areas which are secondary or unskilled in nature. This provides employers the flexibility to conduct such operations without the responsibility of fulfilling regulatory requirements.

The provisions of employing such workforces are clearly laid out under the Contract Labor Regulation & Abolition Act. The act provides for statutorily identified operational activities where a contractual workforce can be deployed, with the onus on the employer to ensure that their regulatory benefits are being provided for by the respective contract manpower provider. However, due to lack of awareness, many organizations tend to be non-compliant. Apart from the financial impact of penalties arising from such non-compliance, the other major concern is the possibility of a judgement reinstating such contractual workforce as permanent employees. Therefore, during M&A due diligence activity, it becomes imperative to understand the contract labor structure and their regulatory compliance. It is also important to review the status of compliance on benefits being provided by the contractor, as implications of any non-compliance would fall directly on the principal employer.

Statutory benefits and social security system (Fig 8)

Provident Fund and Employee State Insurance (ESI) are defined contributions to social security schemes that provide post-retirement benefits and health and welfare benefits, respectively, to employees. Both employers and employees contribute to these funds as per statutorily regulated rates. It is the responsibility of the employer to file monthly returns by a specified date. Any non-compliance attracts penalties, and continuous non-compliance may result in drastic legal implications. During M&A scenarios, associated documentation needs to be verified to ensure the seller complies. Reasons for irregularities in such payments need to be understood and should be described in the purchase considerations.

With respect to statutory bonuses, employees within a certain salary threshold are required to be paid at statutorily regulated rates. Employers are also required to file returns with associated bodies. While the act provides the range for minimum and maximum bonuses to be paid, the rate of bonus is derived based on the organization's financial performance. Non-compliance to such regulations

may attract penalties with associated legal implications even amounting to imprisonment. In M&A scenarios, it is imperative to verify the rate of bonus payouts in alignment to the organization's performance, and issues of irregularities need to be accounted for in the purchase agreement, ensuring all future implications of such irregularities will be the seller's responsibility.

Gratuity is a benefit to be paid at the time of an employee's retirement, provided that the employee has completed continuous service of five years, irrespective of the nature of employment. However, as per the Gratuity Act and the Indian Generally Accepted Accounting Practices (GAAP), employers are required to actuarially value their gratuity annually through a certified actuary, and provide for this in the accounting books. In M&A scenarios, the buyer must validate the valuation to ensure that it has not been undervalued, as this may lead to future financial implications. The mitigation strategy here would be to re-evaluate the gratuity and make the necessary adjustments to the purchase considerations.

Fig 8

Acts governing employee benefits and social security system in India



Summary

The complexity of the landscape described above is undoubtedly daunting. However, this does not mean that the laws and employment environment in India prohibit restructuring of businesses or optimum arrangements.

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Manage Your Global HR Compliance Risk

HR plays a pivotal, binary role in global HR risk management

Companies have embraced comprehensive, transparent, enterprise-wide compliance and ethics programs for several years now, emanating from regulatory requirements and the desire to reduce corporate litigation exposure. However, HR is still not always adequately represented in the corporate compliance structure.

Multinationals are increasingly centralizing the HR function globally. When HR is not at the table, it may be due to a lack of appreciation from senior management for the nuances of global HR compliance and the pitfalls of non-compliance (financial, reputational, or both). Global HR compliance can be challenging, so it's important to educate the C-Suite on how to navigate international employment and benefits, employee classification, HR policies and handbooks, expatriate programs, payroll, collective bargaining agreements, compensation plans and global equity arrangements. Since people are fundamental to managing risk – and they are a source of risk – HR plays a dual role in global HR risk management.

Set up a global HR compliance review (Fig 9)

Achieving clarity on the existing plans, programs, policies and procedures, as well as extraterritorial rules and regulations is helpful in aligning HR strategy to business strategy. It also facilitates due diligence for the next M&A deal. Establishing a regular practice of HR compliance reviews helps avoid the risks of expensive penalties, fees and costly lawsuits arising from alleged non-compliance.

Fig 9
Reasons for global HR compliance review



A relevant finding from the 2018 American Benefits Council and Aon Study on Global Benefits Governance and Operations is that most companies aim to achieve best practice global governance by 2021.

Best practice in global governance broadly includes:

- Defined strategies and policies to manage important risks.
- Global and local responsibilities for executing strategies.
- Ready access to information to identify misalignments with policies.
- Insights into local costs, risks and opportunities to prioritize actions.
- Regular monitoring of reports of risk and emerging risks to aid decision-making.

A global HR compliance review is a useful tool for ensuring proper training is in place for ethics, bribery and insider trading. Likewise, reviewing the organization's cultural training, orientation, recruiting and performance management helps to ensure that organizational values and beliefs are shared globally to sustain the ongoing success of the business.

Not all global HR compliance reviews look the same

To determine the right scope for the organization, consider:

- Geographical markets.
- Departments and functions within HR, such as benefits, employment and employee classification, labor, HR policies and handbooks, payroll, compensation and training.
- Objectives for the review.

For example, if the objectives for the review relate to a forthcoming spin-off of a multinational division to become a stand-alone company, the approach may entail identifying HR interdependencies, employment and employee transfer issues, existing total rewards programs by region. If the business is in each region of the globe, perhaps a comprehensive review every four to five years makes sense. The scope or timing may need to be adjusted if there is a significant change in the global HR program or a compelling business reason.

Conducting a comprehensive review initially helps to document all HR programs and potentially generates efficiencies for future reviews by focusing solely on changes to:

- The plans and programs.
- The local or extraterritorial laws and regulations affecting such plans and programs.
- The processes for administering the plans and programs.
- Talent who administer such plans and programs.

Case studies

Most employers initially think in terms of their total rewards plans when considering global operational compliance reviews. Below are a few examples of recent projects that represent the diverse scope of global HR compliance reviews. It should be noted that these reviews are generally conducted under confidentiality agreements and attorney-client privilege.



M&A integration

Aon was hired to support the integration of a multi-country, global pharmaceutical company that had been acquired by another multinational global pharmaceutical company. As part of the discovery phase of the project, Aon was tasked with creating an inventory of global HR and payroll policies, processes and delivery infrastructure. After analyzing the data, Aon developed a gap analysis of key processes, along with recommendations and prioritization of action steps to ensure compliance, risk management and business continuity. The analysis was then supported by the North American HR leader with project management and execution of these recommendations leading up to day one. Aon's assistance aided in a seamless integration, by establishing a clear set of guiding principles and expectations for managing the integration across all HR functional areas. The process also established an effective day-one HR and payroll operating model as well as a centralized repository of the company's policies and processes to facilitate ongoing compliance and adherence to the company's code of conduct.



Gender pay equity compliance studies

Aon was engaged by several global companies to conduct reviews of compensation programs in the countries where they operated. The reviews were designed to assess compliance with country-specific discrimination laws, including "adverse treatment discrimination" – known as "direct discrimination" in Europe – and "disparate impact" discrimination – known as "indirect discrimination" in Europe. Since each jurisdiction imposes its own list of protected groups or traits, compliance can be a challenge. Aon was engaged to help a multinational, Asian technology company undertake an equal-pay compliance review in the company's UK operations. The purpose of the review was to determine if there were any underlying equal-pay issues relative to gender and ethnicity. Following the review, strong governance policies were put in place to mitigate the equal-pay risks.

Aon's approach to conducting equal-pay reviews in the UK is grounded in UK legislation that prohibits any less favorable treatment between men and women in terms of pay and conditions of employment, the approach recommended by the Equality and Human Rights Commission as presented in its Equal Pay Statutory Code of Practice. Aon added its proprietary risk-based methodology to the review, resulting in an analysis that enabled the client to be in a strong position to further interrogate the data if required.



Compliance studies focused on compliance with a specific issue or particular law

An industrial conglomerate based in Germany with manufacturing, service and sales operations around the globe had subsidiaries in more than two dozen countries with decentralized HR operations. Each such subsidiary sponsored one or more country-specific "retirement savings" plans. Aon was engaged to conduct a broad review of HR operations and over the course of discussions regarding such HR operations, client headquarters staff were surprised to learn of their exposure under a U.S. tax law, the Foreign Account Tax Compliance Act (FATCA). HR had assumed that FATCA might be a concern for the finance and risk operations but not for programs within the HR function. We were engaged to conduct a global compliance project that included aiding the client in understanding the rules, developing an inventory of all of the client's plans organized by country, identifying the characteristics of each plan as relevant to the FATCA exemption(s) available in that country, and facilitating the documentation for exemption status of each. Our expertise enabled us to help communicate effectively with both local HR and local service providers to obtain the information essential to expeditiously and successfully meet the objectives of the compliance project.

Selecting external resources

Hiring a qualified, independent global firm, under attorney-client privilege, protects the findings, increases the review's credibility, employs the right skillset for the review, helps ensure review independence and maximizes efficiencies by minimizing disruption to the global HR team. Further, since global companies may lack expertise in all countries or operate on a decentralized basis, using a firm with the appropriate global experience and local knowledge is critical. Vetting the organization that will conduct the review is crucial, considering what's at stake.

The process is straightforward and includes:

- Gathering data specific to countries covered by the scope and reward plan documents such as broad-based and executive compensation programs (including equity and non-equity incentives), HR policies and handbooks, employment agreements, codes of conduct, expatriate programs, collective agreements, and scripted and other HR communications.
 - Identifying the country-specific HRIS and other HR systems.
 - Reviewing all data to identify risks and gaps with applicable laws, international corporate policies and employment agreements.
 - Conducting interviews with all local HR talent to confirm understanding of the plans and programs as well as processes.
- Identifying areas of non-compliance and inefficient processes.
 - Assessing impact of non-compliance and recommend possible resolution strategies.
 - Meeting with senior global leadership to identify and agree on resolution strategies.
 - Implementing resolution strategies.
 - Establishing a monitoring program for areas of concern.

Benefits of HR compliance reviews

Depending on the scope, the outcomes from global HR compliance reviews can be quite varied. In some cases, significant areas of non-compliance are identified that help the business make corrections and avoid fines prior to government investigations and lawsuits. Direct and indirect benefits of such reviews can also include significant financing and cost reductions through de-risking, harmonization of programs by country, other changes in plan design and – very importantly – reputational protection. In some cases, the results are quantifiable in the form of improved processes that eliminate duplication of efforts. Less quantifiable outcomes such as HR representatives who are better informed about the global business and their role in improving risk management may also result.

Summary

With more companies emphasizing the need for global governance, drafting and implementing a corporate-wide HR compliance review strategy is well timed. Proactive HR risk management solutions are typically far less costly than utilizing a “wait-and-see” approach and may even improve an organization's public image, which is good for the company's equity. Delaying until a compliance concern is discovered by an employee, former employee or a regulator will negatively impact the business. When management and HR mutually appreciate that global compliance reviews are designed to inform, educate and improve processes, rather than redundancy exercises or fault-finding missions, everyone wins. Employees are more engaged, and the company is better positioned to influence change, improve processes and positively address issue resolution.

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Human Capital Considerations in Divestitures

A divestiture is often a strategic decision to support organizational objectives. It may be a step to refocus on core competencies, realize greater value for the business unit or achieve higher long-term financial goals.

The separation of a business is complex and involves a variety of human capital issues and challenges. Factors that impact separation activity include the structure of the transaction, the destination of the divested business and the level of integration among business units prior to separation.

Understanding the deal structure and context

It is critical to establish an early understanding of the structure and context of the divestiture, which will drive the planning and execution of HR separation activity.

1. Identify the destination of the divested business.

Will the business be sold to a strategic buyer, a financial buyer or will it be set up as a standalone entity? If it is sold to a strategic buyer, it will likely be integrated into the buyer's existing operations. The buyer will have its own HR systems, plans and programs in place, and may not have interest in retaining those of the target business. A financial buyer, on the other hand, may not have an HR infrastructure in place, and thus may look to the seller to provide more human capital support for the divesting business, either through replication of HR plans and programs, the provision of transition services or a combination of both. In the case of setting up a standalone entity, it will need to be furnished with a comprehensive HR support structure, including HR plans, programs, IT systems and staff resources.

2. Identify whether the divestiture will be a stock sale or an asset sale.

In a stock sale, a buyer will purchase the full, ongoing business operation, including all of the target's people, HR plans, programs, assets and liabilities. Employees will transfer automatically to the buyer at the time of the share sale. In an asset sale, however, a buyer and seller will negotiate the specific assets, liabilities and people that the buyer will take on. Employees will generally be transferred through an offer/accept process, unless sufficient assets are

transferred to meet local requirements for an automatic transfer of employees. Moreover, in an asset transaction, HR plans, programs and IT systems may not transfer with the business. For example, they might be held at the parent level or the buyer may decline to accept them as part of the assets purchased. In this instance, the buyer will have to provide its own HR plans, programs and systems, and may require some transitional support from the seller until that infrastructure can be put in place. Furthermore, if the buyer will not provide employment to all employees of the target business, severance implications and costs must be identified for those employees who will not transfer to the buyer.

Early planning and execution

HR should be part of the deal team from the onset of transaction planning. Participation by HR ensures an integrated deal strategy that maximizes business valuation while treating employees fairly. This is done by linking HR terms and conditions with documents governing the marketing and sale of the divesting business, including the Offering Memorandum, human capital pro forma financials (including business standalone financial statement adjustments), management presentations, the Purchase and Sale Agreement and the Employee Matters Agreement.

HR has a role to play at every step of the deal process. HR transition planning should begin three to six months prior to engaging with potential buyers with an assessment of HR implications of the anticipated transaction. In coordination with the overall deal team, HR should provide inputs and support on the following:

➤ Impact to HR environment

Assess the impact of divestiture on the seller's HR environment (e.g., shared services, HR plans, programs and systems), identify gaps resulting from the proposed sale and devise mitigation strategies.

➤ Leadership incentives and retention

Identify leaders critical to the success of the transaction and implement an incentive and retention strategy aligned with transaction objectives.

▶ **Internal due diligence**

Conduct a thorough examination of the divesting business's human capital environment by country, including an assessment of the employee population, employing legal entities and terms and conditions of employment (e.g., compensation and benefit plans, retirement benefit liabilities, workforce separation risks and obligations, potential curtailment and other charges to a gain/loss sale).

▶ **Offering memo and financial statement**

Include HR terms and conditions in the offering memo and develop pro-forma standalone financial statements reflecting appropriate benefit balance sheet liabilities, expense and cash flow adjustments.

▶ **Due diligence data room**

Collect and populate a data room with documentation on seller's HR plans, programs and systems (executive compensation, compensation and benefits, payroll and HRIS, labor and employment agreements, workforce demographics, HR litigation and compliance matters, along with any business specific and/or country-specific programs as applicable).

▶ **HR input to deal negotiations**

Develop a strategy for negotiating HR terms and conditions as well as related economic terms, review HR provisions of the initial purchase agreement, including Representations and Warranties Insurance, conduct of business between sign and close, and employee matters provisions (e.g., maintenance of terms and conditions, service credit, treatment of accrued benefits, no-hire/non-solicit protections, transition services including potential employee "lease" arrangements).

▶ **HR operations**

Assess the HR operational implications of the proposed divestiture (e.g., HRIS, payroll, HR functional structure), including timing and impact to resources.

▶ **Communications**

Develop announcement strategy and rollout, consider the need for ongoing employee updates, identify country-specific requirements and implement process for addressing employee questions and concerns.

▶ **Transition planning and separation support**

Identify global HR separation issues (e.g., legal entity setup, compensation and benefit plan disentanglement, labor relations/workforce transfers, HR operations), establish separation strategy and provide support for seamless transition of divesting business, with necessary/agreed HR setup and/or HR transition service agreements.

Key HR challenges in divestitures

The divestiture process is lengthy – it can take several months and sometimes years from the onset of divestiture planning, through the sale and close of the divestiture and the post-closure transition period. Managing HR through this timeline poses numerous challenges and requires thoughtful planning and decision-making in order to in order to retain maximum value of the divesting business, and minimize disruption and other negative impact to the seller's operations.

Key HR challenges that may arise:

▶ **Announcement of intent to sell business**

The decision of whether to announce the intention to divest a business publicly typically follows the deal sales strategy (e.g., public auction vs. private negotiation). The benefits of a public announcement include the ability to engage a broader deal team (confidentiality is not an issue), facilitate planning and avoid false deal rumors. The disadvantages include employee and customer uncertainty over a period of months and potential business valuation impairment if the deal does not go forward as announced.

▶ **Regulatory review**

In some instances, a transaction may be subject to anti-trust or other government regulatory review by organizations such as the U.S. Department of Justice, the European Commission and other country-level regulatory authorities. Communication about the deal may be highly restricted during the review process, which can heighten employee and customer concerns in the information vacuum. Uncertainty around status of deal closure may negatively impact business operations, as employees are distracted by concerns about their futures, causing heightened engagement and retention risks.

▶ Labor relations

Employee representative groups, including labor unions, trade unions and works councils, may have transaction-related entitlements, requiring that they be informed and/or consulted with regarding the transaction itself, along with any anticipated transaction-related impacts to employees. In some geographies, employee representatives may have to be consulted prior to any decision being made that impacts employees. The employee representative must have the ability to impact the decision process and outcomes. Moreover, if negative consequences to employees are anticipated (e.g., terminations, disadvantageous changes to terms and conditions or location of employment), employees may have entitlements under acquired rights and similar legal doctrines to be “made whole” or to receive severance and other termination entitlements.

▶ Internal restructuring

Sometimes, sellers may internally separate the divesting business from the remaining business prior to close. This may be done to facilitate a share sale to a buyer or to restructure the business into a standalone organization. If the existing businesses are integrated in common legal entities, disentanglement may require establishing new legal entities to house the divesting business’s assets, liabilities and employee workforce, a process which can take months in some countries, including the setup of tax identification numbers, bank accounts and requisite government registrations. The transfer of employees to the new legal entities may be done via asset transfers, which could require their own employee representative notification and consultation processes, along with offer/accept processes to effectuate employee transfers.

Summary

Divestitures are complex undertakings that require specific HR transaction expertise to execute successfully. Involving HR early in divestiture planning increases the likelihood that employment-related issues will be properly identified and factored into the financial model and governing documents. Close coordination throughout the deal process between HR, legal and finance will help ensure that decisions made will align with employment requirements in all relevant geographies. Thoughtful and proactive focus on how the deal impacts employees, along with a commitment to open and transparent employee communication, will increase the likelihood that employees stay engaged throughout the deal process and will help drive the transaction to success.

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