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Session 54PD
Session Title: Building a Winning Culture

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Panelists: DAVID S. DUNCAN
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Summary: Between leadership changes, market shifts and restructurings, what does it take to really succeed in today's environment? Will your company even be in business tomorrow? Are you positioned for success regardless of inevitable changes, or are you barely surviving today? Successful enterprises have one thing in common: winning cultures! Building a winning culture is no longer an option but a requirement to prevail in today's increasingly complex, high-velocity economy.

MR. DAVID MILLER: I'm a business and sales coach. I help consultants and sales professionals attract more clients. I also work with executives to help them become better leaders and achieve more success in their careers. I was thinking about this session, and it reminded me of a story of a boy named Johnny whose grandmother made great pickles. He was curious because he knew the pickle came from the cucumber, but his grandmother made both sweet and sour pickles. He said, "Grandmother, you start out with a cucumber, but the pickles come out so different. How do you do it?" She replied, "It's easy. When I want to make a sweet pickle, I put it in a pot with sweet juice and let it sit in that pot for hours. I have a sweet pickle when it's done. When I want a sour pickle, I put it in a pot filled with sour juice, and it takes on the characteristics of its environment and becomes a sour pickle." Likewise, working with clients' environments is important. You can achieve success in spite of your environment, but it's so much easier when you have a supportive environment.

In his 25 years as a consultant executive in the insurance industry, Dave Duncan has striven to add value to organizations as a financial and organizational turnaround expert. He focuses on achieving a strong financial return on a company's greatest investment — people. Dave believes that the needs and results of an organization are achieved when he focuses on building a winning culture that first meets the needs of its people. As an absolute believer in effective communication, he strives to create open atmospheres of interaction, trust and rapport and focuses on developing a fast-paced and results-oriented environment that rewards and encourages people to grow personally and professionally.

MR. DAVE DUNCAN: An article I picked up stated six out of 10 CEOs said, "Limited internal skills or leadership was inhibiting their companies' ability to change with the market." One CEO said the quality and dedication for people is the only factor that makes a real difference in the path to growth. With the economy recovering, growth has sprung to the top of the corporate agenda, replacing cost control as the primary interest. Detecting customers' needs and then reacting quickly and effectively are the new critical competencies. The biggest barriers to the sweeping changes most CEOs desire are limited internal capabilities and leadership resources.

Technical skills are not everything. It's not just what you could do technically and your own personal talent that will help with your own personal effectiveness, but it's also leveraging people around you. Many times that has to do with culture.

There are a lot of soft issues, such as image, relevance, culture and communication, that are buried in the work that we do. I think that, as a group, if we grasp how important the building of a winning culture is, then it's something that you can influence and shape. If we're influencing your shaping things, then we are also adding value. When we're adding value, I think we're relevant. I think we are looking for more and more relevance. We're saying we need to be chief risk officers in all sorts of industries. We're trying to become more relevant. The way we become more relevant is to create more value. This is one thing that's not done. There is a lack in every industry, particularly our own, and if there's something that you can grasp and go with I think it's a way for you to leverage your own personal success. I know that it works.

I just left a company that did not grow over a four-year period, but I tried to do a lot of unique and different things in the area of building a winning culture. When I joined the company I was in charge of profitability. We went from having a financial plan of $11 million that made $1 million in 1999 to a financial plan of around $42 million that made $53 million in 2002. That's a pretty highly leverage result. It was not necessarily because of things I was doing as an actuary because they don't count that much. It was building a culture in a place where I could leverage things that were happening on the bottom line. You can't create things on the bottom line.

You do everything above the line, and then it flows to the bottom. I don't have all the answers. In my current company, our expenses are down 8 percent from last year, and our sales were up 70 percent. Our financials have gone from negative $500 thousand dollars in the first quarter of this year to positive $500 thousand dollars in the last quarter. A lot of this is attributable to spending time on culture rather than pricing and other things that are a requisite for the work that we do.

What is culture? It's the vision, the values, the process, the relationships and the commitment. The vision is the what, the where and the when. Values are who. The process is how we do things. Merriam-Webster's Dictionary defines culture a little bit differently, but in some ways similarly. It defines culture as attitudes, values, goals and practices. Every organization has a culture. It's a deep set of attitudes, values, goals and practices of how it gets things done.

What are different kinds of cultures? Starbucks is a good example of an interesting and successful culture. Starbucks and Howard Schultz, the CEO, said, "During our 32-year history we worked hard to build relationships with our people and our customers. We have also created a true community gathering place where people come together. Our goal was to build a company that took care of its people and left no one behind. We believe that if we build a company culture around relationships, built on gaining the trust and confidence of our people, they would in turn bring this culture to the retail stores and gain the trust and confidence of our customers."

Their thing is employees first and customers indirectly second, and then the business would also be successful behind that. How successful is Starbucks at this point? Eleven years after its initial public offering (IPO), it has 7,400 stores. McDonald's, by the way, had 4,200 after its first 11 years as an IPO. Of course, McDonald's has over 30,000 stores today, so Starbucks is well on the way to being a successful enterprise and culture.

How important is a winning culture? The process we're going to be talking about is how to build a winning culture. It's important to win in the process. If culture was not important magazines wouldn't publish the Fortune 100 best companies to work for every year. Somebody out there believes that some cultures are better than others, and some companies are better to work for than others.

There's an interesting investor business article that came out which said, "Six key factors drive business success." We are trying to increase not just our own personal success, but our business success as well. The six factors are talent, climate, relationships, coaching, effectiveness and recognition. The No. 1 thing is the talent. I think as actuaries we get locked in on just the talent piece.. If we can latch on to some of these other things as well, I think it would be good.

The issue of winning, I think, is important in a winning culture. People whom you want to work with and with whom you do work and even you, too, want to be part of an absolutely winning culture.

What do you have when you do have a winning culture? I'm going to discuss the importance of a winning culture. First of all, there's a world of talent going on. One of the reasons you need a winning culture is to make sure that you're attracting the right kind of talent. You're having a war of talent right now. If you're in a culture that doesn't work for you, you may look for some place else to work. If you have good people who work for you, and they're not part of a winning culture, they will go elsewhere as well.

Why is it important? Business success, personal success and a set of rewards go along with that as well.

We're going to talk about mergers and acquisitions (M&A). I am interested in this. The merger and acquisition activity is at a rapid pace.

What companies? I can think of a couple, such as St. Paul, Travelers, Equitable, Hancock, ManuLife, Great West, Guaranteed Life, Conseco, Prudential and Southern United Healthcare, just to name a couple. It's happening. If you haven't been a part of the significant culture change, you will be.

Strange studies have shown that corporate mergers have even higher failure than liaisons of Hollywood stars, according to *The Economist.* Not all M&A are successful. Why? *Marsh Risk Alert* came out and said there are two causes. One is the lack of adequate due diligence. The second one is the lack of attention to the people side of the transaction. The people side of this is important as well.

Aon Consulting has a nice thing out called "The Work Force Commitment Report". It has some good stuff in there. I found a couple of interesting quotes. The first one states, "Successful organizations will be those who adopt a new way of thinking that treats employees with the same care and sense of urgency applied to investors and customers." The second one states, "Successful leaders will restore employee trust, create spirit and pride and build employee commitment by creating and energizing work environment that nurtures, involves and develops employees."

There are eight major elements to what I believe are winning cultures.

The major elements begin and end with other people first. We're a part of a free agency economy. If any one of us wants to go out and find another job tomorrow, we can do it. There's not as much stigma attached to it as in the good old days. It's not just a change in companies, but also a change in careers that is commonplace today. Understanding that no one is captive and that anybody can leave at any time and go any place is important. It's important therefore to put other people first in a winning culture. That includes all of your staff. You cannot have unhappy employees and also have happy customers. Employees are almost the first thing to focus on without worrying about the customers. If you focus on the employees and make them happy, there's a good chance that your customers will be happy, too.

The customer comes second. It's important to understand that by starting with other people first, you'll be on the serious track of building a winning culture. The second major element is the serious business of winning. To have a winning culture, I think we have to be serious about winning and making winning a part of that winning culture as well.

I worked for Conseco in the early '90s during the heyday. It was so exciting. I got 640 stock options when I first joined the company. I heard that the stock was up a quarter one day. It was up an eighth the next day. Then it was down an eighth. The next day it was up one. Then it was down a half, then up three-quarters, then down three-eighths. I thought to myself, "Is this exciting or what? We're growing. I'm putting money in my pocket. We're hiring, spending money, acquiring companies and consolidating things. Is this fun or what?" It was that way because it was dynamic, and it was part of a winning strategy.

The serious business of winning is serious within a winning culture as well. Energy, speed and passion are important. When we are interviewing for jobs we always wonder what to look for. We're all smart people. It's hard to distinguish on things like that. I wouldn't necessarily recommend this, but I personally use three criteria. I want to know how well applicants handle their checkbooks. I always ask them, "How do you handle your checkbook? How often do you balance it? How close is close enough for you?" I want to know how they take care of their personal business. If they do that pretty well, then they might take care of my business. If they don't balance their checkbook often enough, they don't get hired.

Second, how big their heart is. How energetic are they? Getting some feel for their heart and their passion is important to me. Finally, I like people to move faster than slower. I don't want them to look like they're in a coal mine dragging their feet behind them. I want them to move faster than slower.

I'm embarrassed by this, but I used how fast people walked as a hiring criterion. If they walked slowly, they were in serious trouble. If they walked quickly, they got a nod.

The third major element of a winning culture is energy, speed and passion. What kind of a heart do people have? How engaged are they in the business? Those are the people who are going to drive the winning culture and are the kind of people whom you want to build your business around.

The fourth major element is execution/delivery. Do you bring it home? Do you finish the things that you're supposed to be finishing to get them done on time? Are they comprehensive? Are your employees doing that as well? Are you insisting on that with the people who work for you? Execution/delivery is a major element of a winning culture.

Another thing on the major element list is genuine protection and care for each other. I think this is important. It's important for you to know people on your staff and what goes on in their lives. The only way that you could possibly meet the needs of your business again, I believe, is if you meet the needs of your staff. Genuine protection and genuine caring for people are very important.
The Gallup Organization has 12 key questions. One of them is whether you have a best friend at work. How much do you care about the people on your staff and their well-being? If you care about them, they will care about you. If you care about how they're doing in their business, their growth and their success, they will care about yours. If you don't, they won't.

Differentiation and reward comprise the sixth major element of a winning culture on my list. I am adamant about rewarding people based on performance. You have to find ways of rewarding your key performers to keep them. The key performers are typically your top 10 to 25 percent of employees. It's easy to cater to the other 70 or 80 percent. You don't want people mad at you. But what you do is drive away the other 20 percent. It's the last thing you want. In a winning culture, find ways of rewarding your top performers.

The next major elements of a winning culture are growth and continual improvement. In a winning culture people are continually growing and learning. Tony Robbins would say, "If you're green, you grow; if you're ripe, you rot." The only time you stop growing and stop changing is when you're dead. Something is changing continually. We are changing, and the plants outside are changing. If something is not growing, it is dying. In a winning culture and in a winning environment, it's important for there to be continual growth.

Finally, communication is the eighth major element of a winning culture. Frequent talk and frequent chatter are important. You should be constantly talking to each other, constantly boosting each other and pumping each other up. In a winning culture there's constant and frequent communication. Whether it's weekly meetings, e-mails, notes to somebody or a card for somebody, it is important. How many times have you given somebody a card or some little note somewhere and you go back later and look in the cubicle and the thing is hanging on the wall? Winning culture is finding a way of frequent communication.

There are also some other elements of a winning culture besides the eight I just listed. One of them is diversity of talent. Other ones are youthful exuberance, balance, ideas from everywhere, mastery of fundamentals, the ability to improvise and a lack of egotism, which is an interesting thing as well. If you have somebody who knows everything, it's the most ridiculous thing in the world. We do not know everything. A culture that has a lack of egotism, that is humble in spirit and that welcomes ideas from everywhere is part of a winning culture.

Physical, mental and spiritual attentiveness is also an element of a winning culture. I put people on bonuses for losing weight. I told them being fat is not a good thing, and if you can lose weight, I will pay you bonuses. My predecessor had a bonus plan for people who stopped smoking. People who are physically fit are going to be more able to do the job. Finding some kind of a balance in life is part of a winning culture as well. Attentiveness to all the elements of the people who work for you and also to yourself is important for employee satisfaction and for winning culture.

Customer orientation is also an element of a winning culture, as are fun and the happy factor. Somebody asked me, "Are you having fun?" The answer is "Yes, I'm having fun." If I'm not having fun, I quit. It's that simple. We spend too much time doing so many important things that if we're not having fun in the process, then we should find something else to do. Creating an environment and a culture that are fun results in happy people. Happy people are productive people. How many people are unproductive on your staff that are also unhappy? How many times have you been productive if you'd been unhappy or fearful? Happy employees make for better employees. Better employees make for happy customers, and happy customers make for better top-line growth, retention of clients, growth in your business and profitable business. Again, it's a focus on the people first.

I'm going to go back to this article one more time in concluding here. Six out of 10 CEOs said, "Limited internal skills or leadership was inhibiting their companies' ability to change with the market." This is according to a recent IBM business consulting study. The quality and dedication of the people are the only factors that make a real difference in finding the path to growth. It could be the growth of the actual profession, it could be personal growth or it could be the business growth and success of your company. But when the economy is recovering, growth has sprung to the top of the corporate agenda, replacing cost control as a primary interest.

Responsiveness in detecting customers' needs and reacting effectively and fast are the new critical competences. The biggest barriers to sweeping changes most CEOs desire are limited internal capabilities and leadership resources.

Going back to the Investor's Business Daily article that said there are six key business drivers, talent was the first one. We all have it, and our staff members have some talent as well. What do we do with that? Climate is the second one. Every work environment should offer continuous learning, a sense of community and fun. If it isn't enjoyable to work, then productivity nosedives. Relationships and relationship building were the third. Coaching was the fourth one. Effectiveness was the fifth one. Recognition was the last key business driver.

How much time do we spend recognizing people? It can be a small thing, such as a note, a dollar, an hour off, a handshake or just saying thanks. Those kinds of things make a significant difference in a work place as well. So never minimize the impact of recognition in your work place.

MR. MILLER: Our next speaker is Jim Toole. Jim is managing director of Odell & Associates, a division of MBA Actuaries Incorporated, which is a full-service, independent consulting firm offering a wide range of actuarial management and strategic consulting services. Founder of the SOA Latin America Committee, Jim is a member of the SOA Strategic Planning Committee and International Policy Committee. Jim is a frequent speaker at industry meetings, seminars and universities in the United States and Latin America. His most recent paper, "Actuarial Considerations in Insurance Mergers and Acquisitions: An International Perspective," was published as part of the SOA's Monograph series and is included in the course eight finance exam syllabus. Jim is an experienced M&A practitioner working for both the buy and the sell side of life, health and T&C lines of business. Jim worked for Tillinghast and Milliman USA prior to joining Odell & Associates.

MR. JIM TOOLE: Because we are talking about culture, how many of you are aware that there is a change going on in corporate culture or culture here in the SOA? The Strategic Planning Committee, which I've been on for three years now, is actively involved in attempting to change the way actuaries communicate and are perceived by employers. It struck me only when we were talking about these other issues that I shouldn't be talking about M&A, I should be talking about the culture of the SOA and the great strides we have made in the past three years from the change in leadership from John O'Connor, who was a great leader and led this nonprofit organization for over 20 years, to Sarah Sanford and the work she is gearing to lead us into the next generation and bring up a new generation of actuaries. I am excited to be a part of that process. I learned a lot about change, management and leadership.

M&A is a change process, and it obviously has huge implications on corporate culture. We're going to discuss M&A measurements of success as opposed to winning, why companies do it, an overview of the process and implementation, stakeholder issues and characteristics of successful acquirers. We will also have other discussions of radical gut-wrenching changes that are similar to M&A. I've done the buy side and sell side. I've been through it at companies when I've been a consultant. I've been both the victim and protagonist. I've done it in both Latin America and the United States, and believe me every time is different.

What is corporate culture? Corporate culture encompasses the ways work and authority are organized, the way people are rewarded and controlled and the organizational features such as customs, taboos, company slogans, heroes and social rituals. Before I started this process I thought culture was customs, taboos, slogans, heroes and rituals. I did not recognize that the way you are rewarded, the way you're paid and incentivized and how ideas flow up the leadership chain of command are all part of corporate culture. What you as an employee are allowed to do, or empowered to do, is a direct reflection of your corporate culture. Let's be honest. M&A is going to affect all of that. In fact, it's going to shred it. It's going to take your fabric of culture and tear it apart, which is a scary thing.

What is a successful M&A transaction? It is the creation of shareholder value. That's all it is. That's the only measure. If you don't create value, you failed. Your entire goal in going through the process is to create value for your shareholders. There are a lot of other stakeholders involved that you have to take into account to create this value. But at the end of the day, if your stock goes down, you blew it. The other thing you have to keep aware of is that you have to do better than your peer group. It's not good enough just to do better than you did. If your competitors are doing 10 percent, and you only did 5 percent, you didn't create value. You have to net out the rising tide.

People get excited about M&A. They look at the short-term gain. But it's not just short-term that is important; it's also long-term. You seldom are able to measure the long-term value creation directly. It is hard to do. Few companies will look at the components, net out the expense savings and say, "Did we create value?"

One way of doing it is looking at and listening to the Wall Street chatter. What do the analysts say? If you paid any attention to the AOL-Time Warner merger, it is a classic example of a huge dismal failure from every perspective.

The largest insurance transaction to date is Citibank-Travelers, which was $73 billion in '98. About $38 billion of that was allocated to its property and casualty (P&C) unit. It was a groundbreaking deal. It received a lot of coverage because it was a bank insurance merger. It got a lot of attention. Unfortunately as the deal progressed it got a lot of negative attention. Eventually the companies spun off the P&C unit. What was once worth $38 billion they sold for $16 billion. They destroyed over $20 billion of value. Sandy Weill, who's the president of Citibank, got under a lot of pressure from his institution investors to straighten up or get out. That process is still under way.

Management tends to do better in M&A than shareholders. That's part of the reason why M&A gets done. It is because there's an agency problem, and this gets into corporate finance. Managers are supposed to act as agents for shareholders, but they don't always do a good job. That's why there has been a lot of investment activism in the past year, where the California Public Employees' Retirement System (Calpers) and these other funds are taking a proactive stance against bad management. They're making their voices known. I have some quotes from when MONY went on the market and when AXA started to buy it. They had a shareholders' meeting, and it was one of the most vituperative things I've ever seen in a professional environment.

I'm going to give you a little bit of background on that. MONY demutualized about five years ago. For those of you who aren't familiar with the process of demutualization, you have to look out for the policyholders' interests. The policyholders become shareholders, and there are certain protections in place to prevent them from getting ripped off. They put in a five-year window, where management could not sell the company. As soon as that five-year period expired, the CEO of MONY, Michael Roth, put together a deal with AXA.

Let me give you some feedback on that deal. This is a quote from David Heller, an advisory researcher. This is all public information, and it's required by the FCC to be posted on the MONY Web site. "I've been in this business a long time, and I've always had a list of the five most egregious transactions that I've looked at. I want to congratulate you because I knocked No. 3 out, and you just qualified for number three. I think this is a disgrace to shareholders. I think it's marvelous for management. All the synergies are terrific, but you're merging the companies you're selling for cash and imposing capital gains on people if they profit. I want to congratulate you. You've qualified for my top five. Thank you." There was no response from management.

This is from Stanley Cates. "We are not on the brokers' list and Bloomberg, but we hold 4.9 percent, so we'd be your largest shareholder. Kind of along the lines of what we've heard from other shareholders despite that very powerful endorsement by the investment banker, we think the price is ridiculously low and will certainly vote against it." The reason why the analysts were so upset is because they had been talking to analysts for five years and painting a rosy picture that value was being created and their share price had gone up to $48, but they offered to sell for $31.

If you've been telling all your stakeholders that you're worth $48, but you accept $31, essentially that means you've been lying the entire time, and that's why everybody is so upset. This is a quote from Curtis Jensen. "Since shareholders are getting their faces ripped off from this transaction and cashed out a disgraceful number, I'm wondering if you'd consider taking AXA stock, which among other things might have enabled us to enjoy some of the wonderful benefits you're talking about and perhaps even get a better premium." This is what can happen if you don't communicate effectively and honestly with your stakeholders.

Also, a lot of activity swirled around the AIG-American General deal. There was a big cloud because certain options were exercised where they were underwater, and the concern was that American General was going to go bankrupt. A Prudential from the U.K. came in and put in a bid, but nobody liked that bid, and Prudential stock went way down. Then AIG came in as a white knight and said, "We'll do a little bit better. We'll treat you right." They took it over in a difficult time when the company was going to go bankrupt. They maintained value, they increased value and you don't hear any negative press. Twenty-three billion dollars is a lot to swallow even for AIG. These are contracts that are easily movable. They are an odium life business and did an excellent job salvaging a difficult situation. The analysts still look at it carefully, and it's reported separately in their annual report. AIG is definitely the example of quality M&A.

Most people agree that only 50 percent of mergers meet the objectives. The No. 1 reason that's cited is incompatible cultures. The inability to manage the target is another reason. A third reason is the inability to implement change, which also is a cultural issue. Tillinghast did a survey that says that insurance does a little bit better from a CEO's perspective and culture is less of a problem, whereas overpaying and not capturing synergy are problems. I think what that says is that the culture of the insurance industry is inbred and is much more alike than different, so incompatibility of cultures is not a problem.
Although most executives agree that over 50 percent of mergers fail to meet objectives, people do it anyway. Why is that? There are drivers other than money for shareholders. For management it's exciting. For people who do M&A it's very exciting. What drives M&A? Why would you want to do an M&A process? There are two main threads. One is financial, which is making money directly. Two is strategic. You want to position your company. On the financial side you calculate the value, which is made up of your book value, the value of your in force and the value of new business. Hopefully, when you put that altogether you come up with an estimate of value. Then you have to look from the business standpoint of what your GAAP ROE is. You also have to determine your accretion/dilution ratio. Is the acquisition going to increase earnings, or is it going to dilute earnings?

Then there is evaluation from the strategic standpoint. Analysts are going to look at both sides. Does it make sense strategically? Is it going to give you access to new markets? Is it going to create economies of scale, or is it going to improve distribution? Wall Street will look at both of these issues.

I'm going to go through the M&A process quickly. First, you either find a target, or it finds you. You get sent some information, and then you're going to go put a preliminary bid. In two weeks you'll look through the information you get. You will go on site and do a due diligence, in which you look for holes and try to find any problems. Hopefully you find some problems so you can bring the price down. You sign a letter of intent if you want to go forward with the process. You come back and do a week-long due diligence where you try to find even more problems or, if you're good, you can find some value that nobody else spotted. It goes both ways. You could find problems and then find value to put in your pocket. There are plenty of instances where that happens.

Finally, after making a definitive agreement, you have to make a presentation to your board of directors. You have to sell it to the board, which has to sign off on it. Then you have to go about presenting the deal to the public. That includes regulators. They have to approve. You have to sell it to the rating agencies. You have to sell it to your shareholders. They have to buy off. That's M&A in 60 seconds. What have we forgotten?

FROM THE FLOOR: Implementing.

MR. TOOLE: That's right. Everybody thinks it's so exciting to do the deal, and then the implementation is drudgery. It is. It's hard work. That's where the rubber hits the road, and that's where you find out whether or not you can capture all the stuff that you put in your report, which said you can save this much money and can create this much synergy. Are the deal shapers accountable for capturing or creating that value, or in your M&A environment do the deal men walk away? Are incentives aligned with outcomes? Those responsible for structuring in a deal should bear some responsibility for the execution. But in many environments they move on to the next deal and leave implementation to line managers, which frankly is not fair. Line managers have to go through a due diligence again, and they don't even know necessarily what the objectives were when the deal was done.

We're now going to talk briefly about strategic and tactical teams. You have a steering group develop a plan with goals and dates that are important. The group must focus on capturing the drivers of value. You also have to communicate with your stakeholders and deal with uncertainty as quickly as possible. Do not let the process drag on. Bad news is definitely better than no news. To some extent the challenges you face in integration will depend on what the objectives of the deal were. If your objectives were to expand geographically, you will have a different implementation challenge than if you were trying to develop a new product mix.

After you have the strategic view you have to go to the tactical view, where you have the project teams coming in. They could either be corporate specialists or line management. Some companies do it by function, such as claims, IT and finance, and other companies do it by line of business, such as life, health and annuity. But everybody needs to understand the drivers of the deal. If you don't, your shareholders will remember. Your analysts remember what you told them you were trying to do with this deal, and they'll hold you accountable to it. Throughout all this time you have to work in and around both cultures, which makes it hard.

FROM THE FLOOR: What do you do with your regular job while you are doing this? You are expected to still make money and do everything you were already doing in addition to this. That makes it difficult.

MR. TOOLE: Burnout is a big issue. Some companies have transition teams that help facilitate that. Again this is a cultural issue. Other companies hire consulting firms to help get it done. That also leads to problems because then you can blame the consultants. Management is not making the decision. They're just delegating, which is not the way to go. Burnout is a big issue.

Management consultants are saying you can either have a company that's separate or that is absorbed. Very early on in the process of due diligence when you're doing the deal, you have to decide whether you're going to keep in a separate operational structure or if you're going to integrate everything. That's going to drive your choices going forward.

Stakeholder issues are important. I'm going to talk about three main groups: employees, distribution and policyholders. There are other ones, but they are less involved with the cultural issue. Your employees hold the keys to your cost savings and synergies. You have to identify and contact your key talent, and let them know you want them.

FROM THE FLOOR: Does the cost of doing the deal include any bonuses to those people?

MR. TOOLE: It should. If you have a good EB person on your team that will all be taken care of. Can you use the mike and say your name?

FROM THE FLOOR: A major bank acquired another bank. After a year or so an 82-year-old lady who was an account manager had it. She was fed up and wasn't going to deal with it anymore. She called her son at 11 o'clock in the morning and told him not to worry, but that she was walking out the door. At two o'clock she called back and said, "I was just recruited by another bank." A few years later that bank got acquired by the same original acquirer. This time the VP of operations sat down with her to convince her to stay because the first time at 82 years old when she walked out the door, $31 million worth of deposits followed her. The second time, for $31 million worth of deposits, he was going to make a personal appointment to see her and to make sure she was going to be happy.

MR. TOOLE: From banking perspective that's not unlike how you have to deal with your distributors. You have to identify your key distributors. You have to identify your key employees and make sure you have a process for contacting them and making them feel part of the team. From an employee standpoint, they have to feel that the role they are playing in the process is key to the ultimate success.

A key point is that you paid for three pieces of value in your acquisition. First is your book value, which hopefully you identified in due diligence. Second is your existing business, and third is new business. In some situations you don't pay for new business. Distribution is the key to unlocking the value of new business. Distributors also control, to some extent, your existing business because if a distributor walks, you can roll all that as well. Your key distributors have to be stabilized. Your policyholders hold the key to existing value. Your competition, and your competition in this case could be distributors who are leaving, is going to be exploiting this changed situation. Direct communication is always appropriate.

On the Web site how is that going to look and feel? How are you going to communicate that? Even the rollout of a new brand versus confirmation of the old should be examined. How are you going to handle brand management? That's not something that as actuaries we think about all the time, but I think when you're doing it in an M&A process, it has to be incorporated into your value creation proposition. We can put a value on a brand through a modeling process. The answer is communicate and don't drop the ball. Keep communicating. If you tell people you're going to get back to them in a month or a week, or we're going to have monthly meetings, don't let them fade away. Have the meetings or tell people you're going to stop, but don't just drop it.

Communicate often and honestly, and be sure to follow through with promises. Bad news is better than no news. Culture is an issue in the United States, but when you're doing it internationally it's insane because everything is different. There are huge risks.

There are many factors that make for successful acquirers. You have to identify value. You have to know how to identify value and bid appropriately. Know when to say when. Know when to pull out. Don't get caught up in a bidding war. AIG will sit back and wait and see if there are any problems. It'll swoop down at the last minute and just top it out, or wait until everybody else has dropped out, and you got damaged goods.

You protect your investment through due diligence. You must have good due diligence in all aspects of the corporation. You have to get a good team together, and the talent that you don't have internally you must contract externally. There's nothing that says you have to bring all consultants or all internal people. Whatever you're missing you should get. If you don't have expertise in a particular line of business, either take it off the table with a lawyer's pen, or get somebody with that expertise. Then you have to negotiate terms to safeguard your deal. If there's a window of three months to closing, make sure you're protected in that window. If there's intellectual property that you need to keep to make the deal work, make sure that that's protected. There are all sorts of things that good lawyers will handle.

Successful acquirers are proficient at integration. It's something that can be learned. If you get it right the first time, you're a genius. I read that you have to do it six times before it really gets into your genes. It is a good idea to jump-start that process by getting some consultants involved, but don't rely on them too heavily. You want to learn from them and then minimize them if possible.

Remember to pursue the drivers of value. If you said this is what you're going to get out of the deal, focus on that first. Capture it. Then address cultural issues in a timely and forthright manner. I've heard many stories about CEOs who will get up in front of 500 people and say, "We're keeping all the jobs here, and everybody is safe." Three months later they close down the division.

I want to quickly go over some similar situations in which changed management is, to my mind, not unlike M&A. Demutualizations, in which you take a company that had no oversight and little paper performance and bring in a new CEO, have the same challenges as M&A without the bidding. Kearns came into Xerox in the '80s, took a failing company and turned it around based on quality. Another example is Gerstner and IBM. Gerstner wrote a really great book called *Who Says Elephants*

Can't Dance? and he focused the culture around service. They brought a cultural change in response to market conditions.

I have an interesting point here. Both Xerox and IBM were dominant in the industry and in a period of five years were at the brink of bankruptcy. This was because of a change in numerous things, such as environment and technology. They went from a highly bureaucratic, centralized decision making, limited incentive compensation culture where everything is based on seniority, to pushing the decision rights closer to the customer, becoming service oriented, paying for performance and being entrepreneurial. I would say change starts at the top. You have to walk the walk, and people smell hypocrisy. If you're the leader, and you hire a consultant to cut costs, but you're flying around in your small jet, they are going to laugh. You have to accept responsibility. You can't delegate responsibility. You have to be a part of the process.

This is an interesting quote from Petronius Arbiter in 210 B.C. I would have thought it was from yesterday. "It seemed that every time we were beginning to form into teams we would be reorganized. I was to learn later in life that we tend to meet any new situation by reorganizing, and what a wonderful method it can be for creating the illusion of the progress while producing confusion, inefficiency and demoralization." This was before the age of Bill Gates and computers.

By any other name, changed management, restructuring, reengineering, reorganization, benchmarking, total quality management and broad banding are the same things.

When examining changed management, there are resources that can help you. "New Corporate Finance" is one that is on the course eight financing exam. "Five Frogs on a Log" is a good talk in the SOA *Record* on how to avoid common pitfalls of health plan mergers. *Project Management For Dummies* is a good book. There is a book on insurance industry mergers and acquisitions due out fourth quarter '04.

FROM THE FLOOR: That was interesting, it really was. I'm not convinced that insurance companies are as compatible as noninsurance companies, having lived through some M&A activities. One of the interesting things that I heard during the presentation was the due diligence part of it. Due diligence typically includes valuations of blocks of business, looking at the underlying products and so forth. But little due diligence is actually done on cultures and the cultural compatibility. Because 70 percent of all M&A fail, because actuaries are involved in M&A work, and because we hate being failures 70 percent of the time, it begs for us to start spending more time on some of the soft issues and doing more of the cultural due diligence because it's not being done.

Doing these kind of things and being involved in M&A activities, as many of us are or will be, or even being a part of it if we're not actually driving a process, are things that we can do as actuaries. No time is better than now. Helping to change culture is something you can do. Changing a culture, modifying a culture and getting the most out of it add corporate value. Increased corporate value means increased personal value. Increased personal value means to increase personal success. More success means opportunities. More opportunities mean more relevance. It's good for you personally, and it's good for the profession. A lot of the stuff ties together.

MR. DAVID DIXON: I'd like each of you to do one thing. Let's say you're the integration manager for a new merger or you're the new chief actuary in a new situation. You just came into the situation. What are the top three things that you would do to implement or to assess the culture. You've got 30 days. Give me a 30-day plan.

PANELIST: The first thing I'd do is call the employee benefits manager and get his or her assessment. I would talk to the consultant that I hired to assess those benefits. Right off the bat it will tell you a lot about the entrepreneurial future of the culture. Certainly one of the things that I didn't hit on is during the process that we're doing is, you take everything that you learned here and leverage it into your implementation. I wouldn't be starting from scratch. You would know a lot from the network of people whom you sent out looking at every single aspect of the company and reporting back to you. I would have a plan in place on the first day stating these are the day-one issues that have to be addressed, and then these are the plans that need to be done in two weeks, then a month, then three months, and then six months. That's even before it started.

PANELIST: I saw something in that Marsh Risk Alert that I thought was terrific because it described ways of assessing corporate culture. I would do it sooner rather than later, given that it is such a key driver in the potential success of a combined enterprise. They break it down into five or six different components. As for the top three, they would say environment, achievement and sitting down and meeting with as many key people as possible to find out how achievement is recognized. Is it at the individual level? Is it at the team level?

For example, Oracle and people saw two different types of culture in the area of achievement. How were rewards given? How is work assigned? How is credit given? Those kinds of things fall in the area of achievement. The second thing would be to find out what kind of an environment they have. Are things based on results, or is the process more important than the results? I've seen that as something that can be incompatible in M&A work. One company isn't so much driven by the bottom line results, but it's happy with the process itself of getting there. The other one wants the bottom line at any cost.

I would look at the environment of how things are done. They have a couple of other things, but I thought a key one was in the area of power. Is power concentrated in the hands of a few? They give lip service to empowering their people to make the right decisions, but wrong decisions are not tolerated. Is power really focused at the top, or is power equally distributed throughout the organization? There are some key things to look at and some key questions to ask of people. The more people involved in the process, the better.

MR. GERRY FRYER: I just came from a situation where I was with a company that had a winning culture, and we were absorbed by a company that had a culture that could best be described as one that was around about 15 years ago and was Neanderthal by comparison. Winning cultures don't always win in the marketplace, and that's kind of sobering. I wonder if you had any comments on that.

MR. DUNCAN: It is tough because when two companies come together, you have some choices. It can take on the culture of the acquiring company; it can take on the culture of the acquiree, which typically is not the case; there can be some blend in between; or it could be a brand new culture. The brand new culture completely is almost impossible, but at best there may be some blending of those two.

I don't necessarily have a solution. I have made the same kind of observation. But the observation I've also had is that it creates a tremendous opportunity for people, particularly in a company that has been acquired to volunteer to help, because it's something that's not getting attention. If you can be some kind of a leading change agent in that regard for bringing those cultures together or being a thought leader in that regard, it is a way of creating that value in the combined enterprise. However, it's problematic.

MR. JOHN STARK: Culture, it seems, is such a huge risk. Has anybody done anything to try to quantify it? It seems that as actuaries this would be a great place for us. It's an unstructured problem that's kind of soft. A lot of people would love to at least have a sense of a dollar value or probability that what they are proposing would succeed or fail. Even on a scale of one to five it would probably be worthwhile.

UNIDENTIFIED SPEAKER: I recently saw *The Fog of War* about Robert McNamara and would compare M&A to that. There are millions of decisions, and it's difficult at the end of the day, or sometimes or during the middle of the process, to figure out what's going on. On the subject of quantifying culture and probability, sometimes I would suggest that culture is the whipping boy for failure when it was pure execution. People will just say that the cultures were incompatible. I think that's why it always gets those high marks. Nobody wants to say it was his fault. When you are valuing the purchase, the discount rate you use should reflect the execution risk. When you see that that has a higher probability of failure you should obviously get a higher discount rate. That's the best place I can see.

FROM THE FLOOR: It seems like that would probably just get lost in the shuffle. Nobody wants to hear that you may or may not make it.

UNIDENTIFIED SPEAKER: What if the Actuarial Standard of Practice (ASOP) No. 19, which is currently under review, had something that said discount rates should take into account certain intangibles not included in the list of execution risk?

FROM THE FLOOR: Yes, it seems that there's a place for us somewhere in these things that are so risky and that have historically failed.

MR. DUNCAN: I agree with that. I've seen articles that try to quantify the loss of some productivity for employees in the company being acquired. I tried to do my own study one time of my own employees. I took an informal survey. I was in a charge of a big unit in St. Louis, so I knew that these numbers were all low. I went around trying to survey how much lost productivity we had because people are sitting around with fear, spending time doing resumes, talking on the telephone calling headhunters or commiserating with the coworkers. I took 100 samples. The loss of productivity in our company in St. Louis was somewhere between a minimum of 25 percent and a maximum of 65 percent. It was a huge number. I thought that they're probably lying to me because they're afraid to get in trouble because I'm in charge. The actual number was probably higher.

I agree with you. I think that if we can assign a value to how we build into the whole due diligence process, it is a natural place for actuaries to get involved.