

“Critical Pillars for M&A Success” Survey

While Corporate Deal-Makers Are Optimistic,
Recent M&A Results Are Disappointing

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Executive Summary

Despite the economic recovery and improving availability of capital, the failure rate of mergers and acquisitions (M&A) continues to be well-documented. Most reports point to the same, unsurprising conclusion: M&A transactions are fraught with peril and complexities that threaten their effectiveness and financial success.

The Crowe Horwath LLP “Critical Pillars for M&A Success” survey was undertaken to help the M&A profession – corporate deal-makers and consultants alike – approach the risky business of M&A in a way that achieves the intended goals of a company’s critical stakeholders: shareholders, directors, customers, and personnel. Insight gained from deal experts in one-on-one interviews and through a focus group of serial acquirers drove the creation of the survey. Eighty C-suite and corporate development executives provided detailed answers to the survey questions. The study reveals much about not only respondents’ hopes and concerns about their M&A plans but the practice of M&A in general, including how effectively their companies evaluate acquisition risks and execute at different stages of a transaction.

“The concept of M&A ‘failure’ is often misrepresented, as it does not indicate company failure but rather a failure of the deal to meet the intended goals put in place prior to the transaction,” said Marc Shaffer, managing partner of financial advisory services for Crowe. “Different from other M&A studies, which focus

mainly on deal volume, overall market expectations, or a particular component of the deal life cycle, this survey attempts to peel back the onion and explore what’s happening systematically at each level of the M&A value chain.”

M&A confidence grew for the majority of 2013 with highly visible consolidation in the telecommunications, media, and technology industries.¹ Signaling that M&A remains a core piece of companies’ business growth strategy, most executives report they are devoting significant time and resources to deal-making and plan to keep doing so in 2014. Executives say they generally are hopeful about future deals; however, the vast majority of them acknowledge that their companies have not achieved the financial outcomes and operational synergies that were projected at the time of deal consummation.

Regarding M&A as an important driver of growth, the majority of respondents have actively pursued at least three transactions in the past two years, and many respondents believe they have clearly defined plans for – and adequate resources to handle – their M&A activity. This suggests that they feel well prepared and well equipped to complete successful deals.

Despite the increasing efforts devoted to vetting and pursuing acquisitions, the survey results reveal a sizable disconnect between

executives’ confidence and their measurable achievements. Few say they are achieving the efficiencies and synergies they expected, in part because companies are having trouble maintaining focus to truly confirm that deals match the strategic plan intended throughout the transaction process. Regardless of what executives believe initially, it appears they might underestimate the resources needed to succeed at M&A – and they might not even recognize the capacity and skill sets that their deal teams lack.

“Based on the feedback we’ve received from this survey,” Shaffer said, “there are clear yet avoidable obstacles that are preventing M&A success, ranging from poor strategic fit to failure to execute during the M&A life cycle. Fortunately, when situations are less than perfect, there is opportunity for improvement.”

Highlights of the Crowe “Critical Pillars for M&A Success” survey include:

- Almost two-thirds (63 percent) of respondents have pursued three or more deals in the past two years, while more than a quarter (27 percent) of respondents have pursued one or two deals at least through the due diligence stage.
- Despite the large number of companies pursuing M&A, only 45 percent of respondents believe they do a “very good job” managing their deal pipeline.

- Almost a third of respondents do not believe that their companies are performing well when it comes to clearly defining a strategic plan to identify M&A opportunities.
- Only 37 percent of respondents feel that their company has proper governance to avoid the C-suite unduly influencing whether to consummate a transaction.
- Although 62 percent of respondents rate their company’s performance as “good” or “excellent” when it comes to setting a clear strategy/hypothesis at the beginning of a deal, that number drops to 47 percent when it comes to maintaining clarity and focus throughout the process.
- Only 12 percent of respondents say they are “very efficient” at executing M&A deals, and only 9 percent of them say they are “very effective” at capturing synergies targeted at the start of the transaction process, with the leading challenge being an underestimation of time and resources needed to achieve (68 percent).
- Nearly a quarter (23 percent) of respondents say they do a “poor” or “very poor” job of communicating about and achieving alignment with the structure of a combined organization.
- More than half (51 percent) of respondents admit falling “somewhat” or “significantly” short of their desired rate of return on completed transactions.

With considerable amounts of money at stake and often short windows in which to complete sophisticated M&A transactions, there is tremendous pressure to make decisions with imperfect information and close deals regardless of the level of preparedness. We find that companies are doing a better job of asking for professional help with due diligence. However, this survey shows that there is still significant room for improvement in a number of controllable areas, which, when addressed and executed properly, would improve the likelihood of transactions meeting financial and operational expectations. The areas are:

1. *Structure, governance, and accountability*
2. *Strategic clarity*
3. *Execution efficiency (process management)*
4. *Operation continuity*
5. *Synergy capture*
6. *People and culture management*
7. *Scalable resources*

– Chris Nemeth, leader of M&A integration services at Crowe

¹ “Mergermarket M&A Trend Report: 2013,” Jan. 3, 2014, <http://www.mergermarket.com/pdf/Mergermarket.2013.FinancialAdvisorM&ATrendReport.pdf>

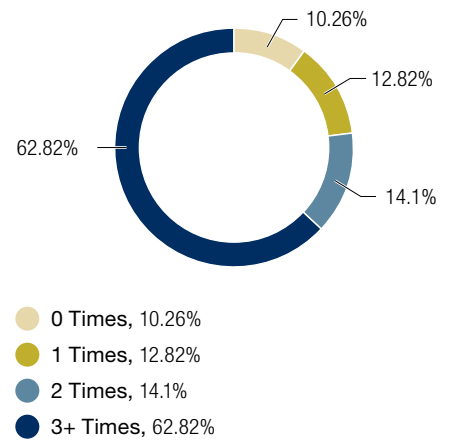


Preparation Counts

Structure, Governance, and Accountability

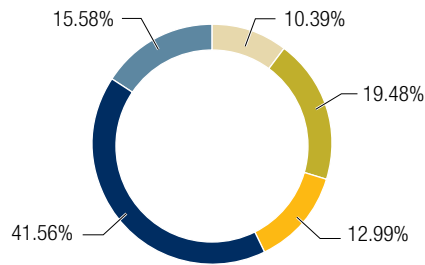
Q: How many transactions has your company actively pursued (at least to the due diligence stage) in the past two years? (Note: Include prior company experience if you have not been at your current company for two years.)

Almost two-thirds of respondents report having actively pursued three or more deals in the past two years – a period when deal activity has been muted. The results suggest that because most companies treat M&A as a core growth activity, its execution needs to be clearly understood, properly resourced, and effectively managed.



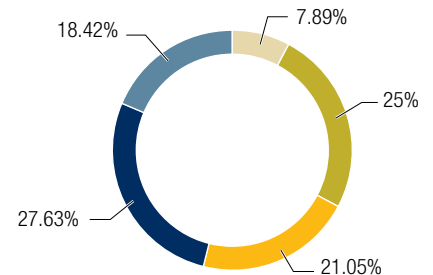
Q: Please rate your level of agreement with the following statements about your company.

Has a clearly defined strategic plan identifying growth through M&A



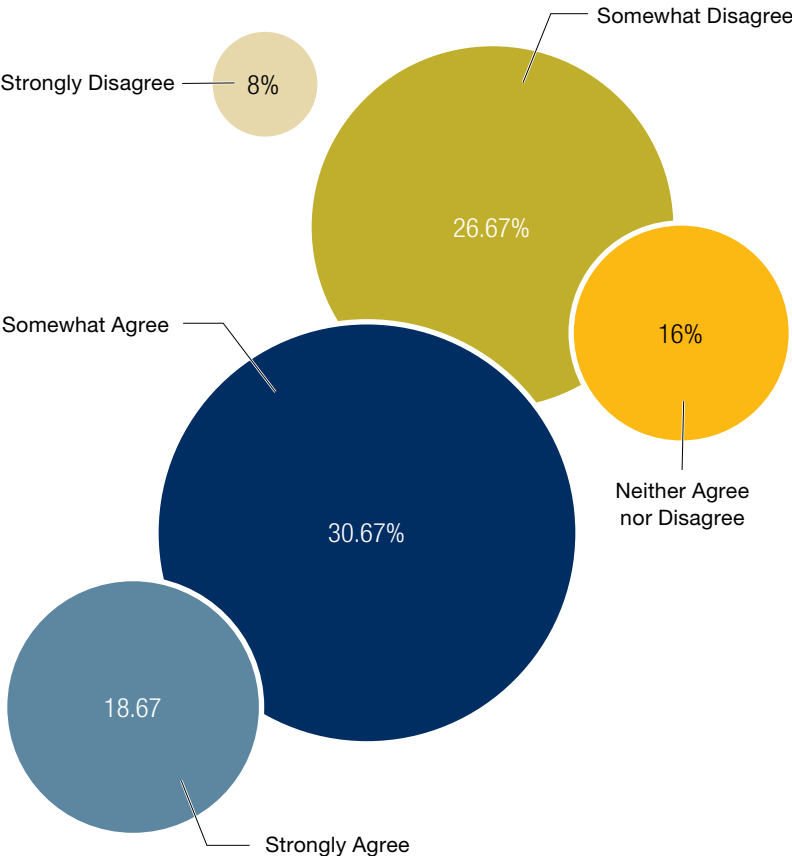
- Strongly Disagree, 10.39%
- Somewhat Disagree, 19.48%
- Neither Agree nor Disagree, 12.99%
- Somewhat Agree, 41.56%
- Strongly Agree, 15.58%

Consistently sets clear expectations or has a framework for approaching M&A deals

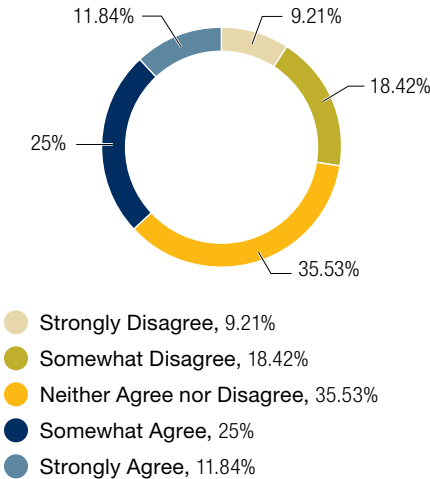


- Strongly Disagree, 7.89%
- Somewhat Disagree, 25%
- Neither Agree nor Disagree, 21.05%
- Somewhat Agree, 27.63%
- Strongly Agree, 18.42%

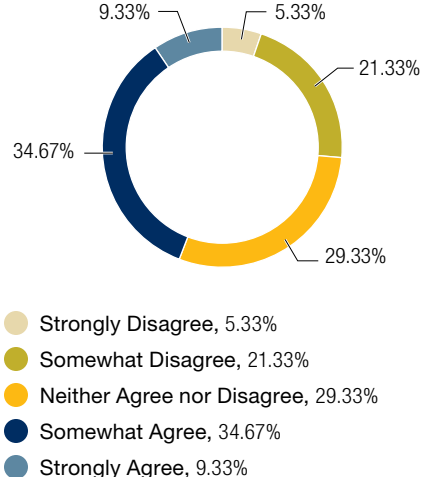
Has a process to assess whether a deal continues to match the strategic plan intent over the course of the transaction



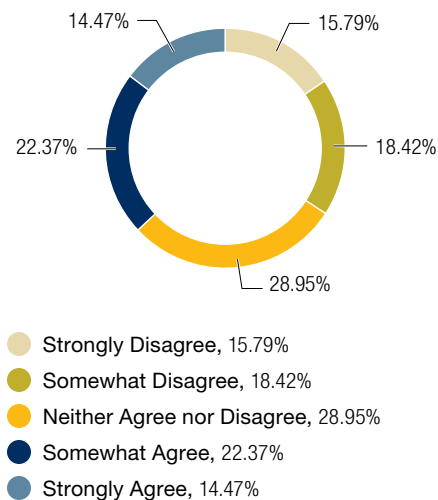
Holds individuals accountable for their clearly defined roles in the transaction



Consistently executes deals at the right price/structure to meet strategic needs



Has proper governance to avoid C-suite unduly influencing whether to consummate a transaction

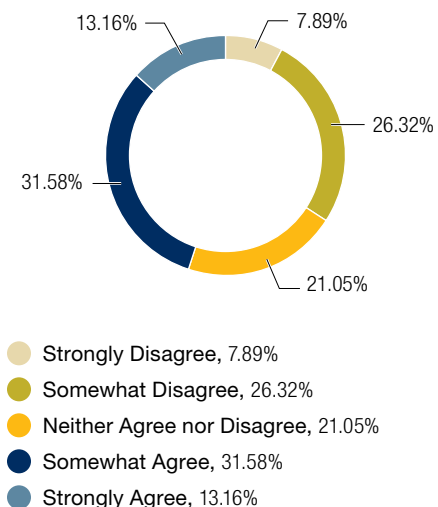


Most respondents believe they are prepared and equipped to handle deal flow. More agree than disagree with statements that positively summarize their abilities, and 57 percent report having a clearly defined plan.

But despite the confidence on display, the responses to the questions that delve deeper indicate a general lack of preparedness. Less than half of respondents say their companies take steps that are vital to a successful deal. Those steps include:

- *Having a process in place to assess whether a progressing deal continues to match the strategic plan*
- *Setting clear expectations or having a framework for approaching M&A deals*
- *Doing a very good job managing a deal pipeline*
- *Consistently executing deals at the right price/structure to meet strategic needs*
- *Holding individuals accountable for their clearly defined roles in the transaction*
- *Having proper governance to avoid members of the C-suite unduly influencing whether to consummate a transaction*

Overall, does a very good job managing its deal pipeline



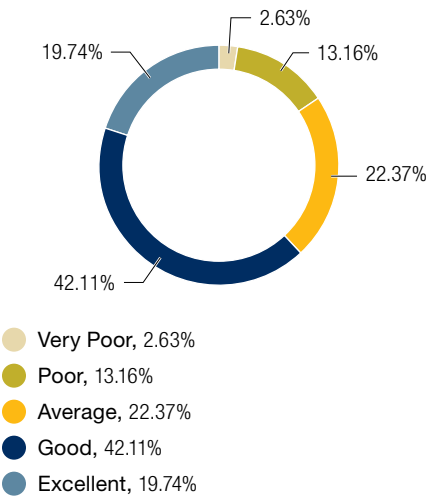
This analysis suggests that despite the stated answers, companies engaged in M&A have a widespread lack of preparedness. Given the high stakes, the issue can create a ripple effect of challenges that undermine deal value. This theme continues to run through many of the following responses.

Stay on Course With Strategy

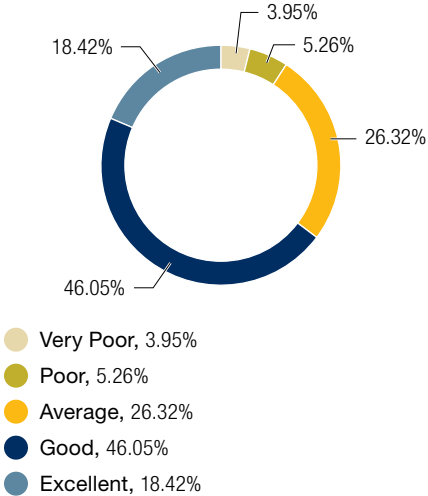
Strategic Clarity

Q: How would you rate your company's performance in the following areas?

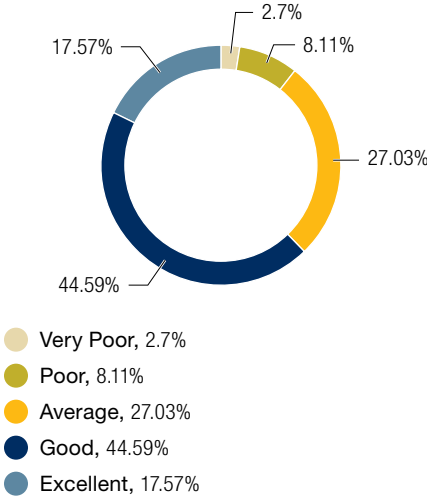
Setting a clear strategy/hypothesis at the beginning of a deal



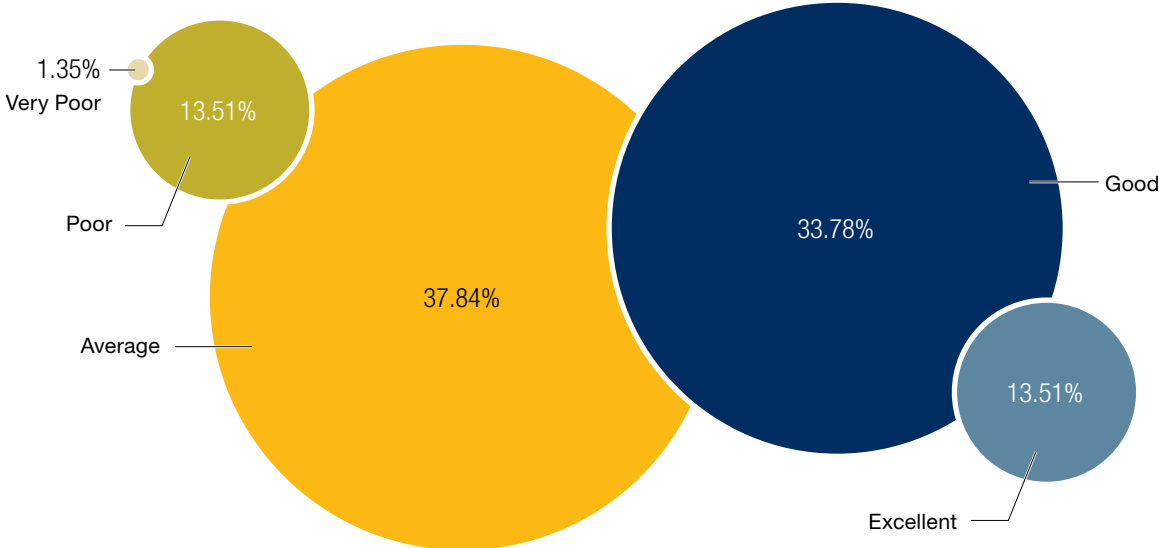
Clearly defining the deal's objectives



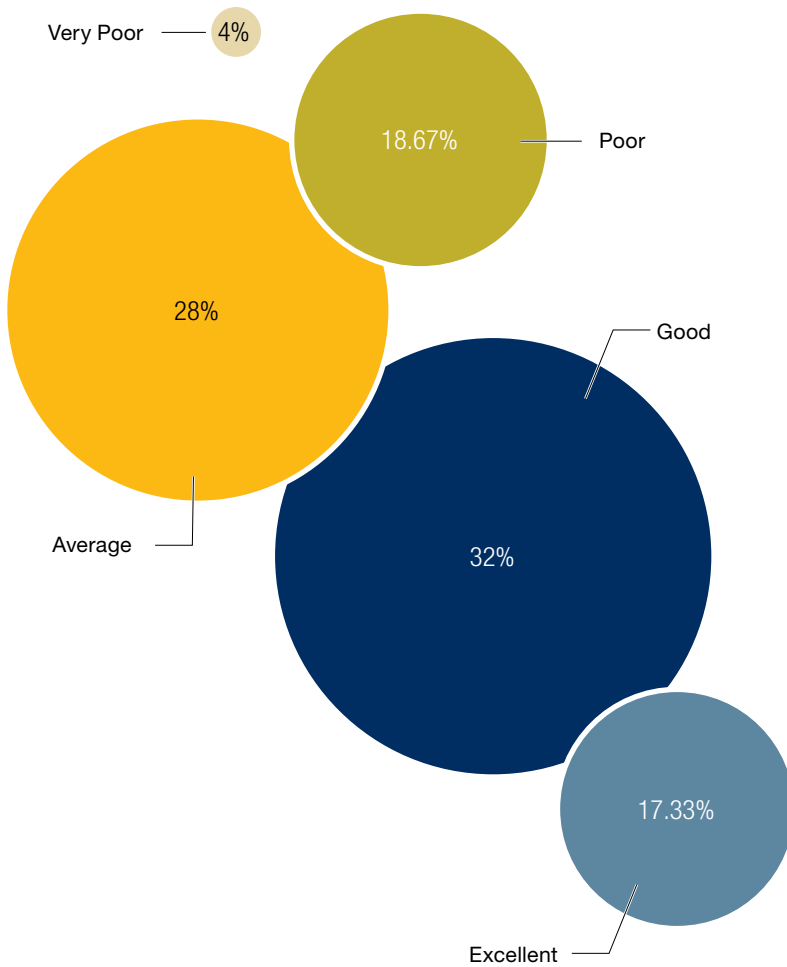
Clearly defining the deal's value drivers



Maintaining clarity and focus throughout the deal process



Clearly defining the deal’s potential risks



Once again, executives display a generally high opinion of their teams and performance. Most respondents say they are doing a “good” or “excellent” job of clearly defining a deal’s objectives, setting a clear strategy or hypothesis at the start, and clearly defining a deal’s value drivers.

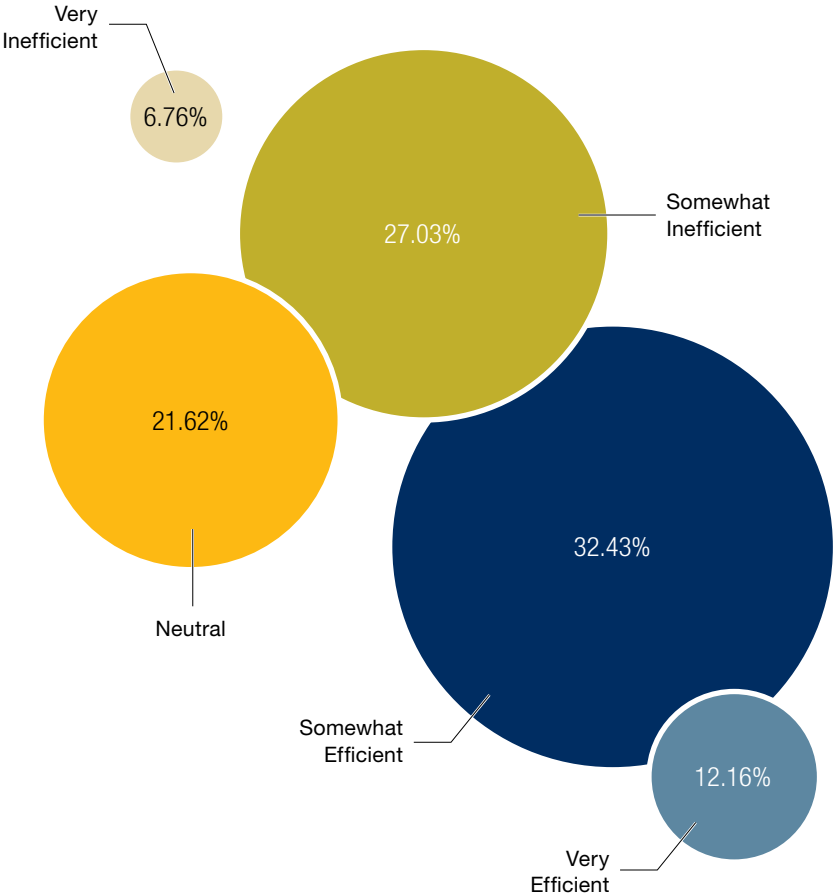
But less than half (49 percent) of respondents say they are doing a “good” or “excellent” job at clearly defining the potential risks that could cause a transaction to stumble or sink, and more than half report having a tough time maintaining clarity and focus as a deal progresses, which makes it difficult to remain on track and progress efficiently.

Balance Speed and Direction

Execution Efficiency

Q: Overall, how would you rate your company's efficiency in executing M&A deals?

Less than 50 percent of respondents believe that their company is efficient at executing deals.



Q: How would you rank your company's proficiency in the following elements that impact deal execution efficiency? (1 = most proficient; 5 = least proficient)

- 1 Consistently utilizing sufficient expertise on the deal team
- 2 Sustaining focus/momentum over the course of the deal
- 3 Balancing adequate diligence with speed
- 4 Maintaining and following a good playbook
- 5 Avoiding overanalysis

The results indicate that more attention is being paid early in the deal process, as executives believe they use the right expertise on their assembled deal teams and some follow a good playbook. However, though companies are equipped with functional and operational expertise, M&A execution expertise is entirely another specialty. Such expertise might not be well managed – or the playbook is not closely followed – given that respondents indicate their companies are weakest at avoiding overanalysis.

Q. In your experience, what factor(s) commonly causes the execution of an M&A deal to lose speed and momentum?



“Seller’s preparation along with execution on deal requirements.”

*“**Maintaining focus** of the seller.”*

“Disorganized data preparation. Overanalysis and approval process both internally and externally. Seller’s unwillingness to share past information and future projections.”

*“**Lack of focus**; failure to adhere to critical path milestones; inexperience identifying potential risks.”*

“Lack of understanding of the role of operations due diligence or understanding of how to conduct an effective operations due diligence.”

*“**Not staying focused** on the desired result. Constantly changing the goals for the acquisition.”*

*“**Lack of focus** by management.”*

“Lack of executive leadership support/involvement/guidance/approvals.”

*“**Lack of focus** by C-suite.”*

“Overanalysis of noncritical factors.”



The common thread through these comments about deals losing momentum is the lack of focus on the deal by stakeholders of both sides of the transaction. If the stakeholders are not engaged, how can they expect the rest of their teams to deliver a positive transaction?



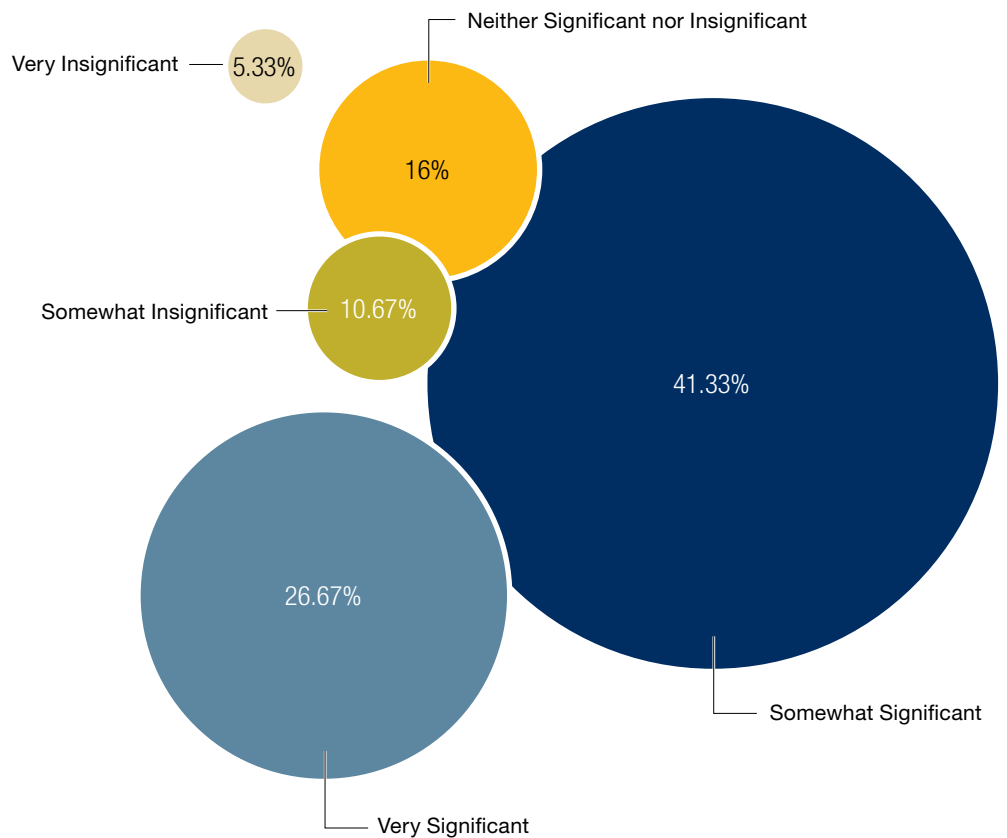
Maintain Business as Usual

Operation Continuity

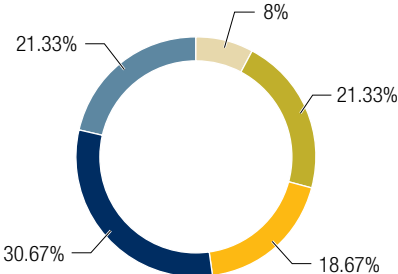
Q: Based on your experience, how significant have the following challenges been to maintaining operating continuity within your company and that of the acquired company?

Maintaining top-line performance at the acquired company is tough, according to respondents. Slightly more than two-thirds (68 percent) say maintaining this has been a “somewhat” or “very significant” challenge.

Maintaining top-line performance within the acquired company

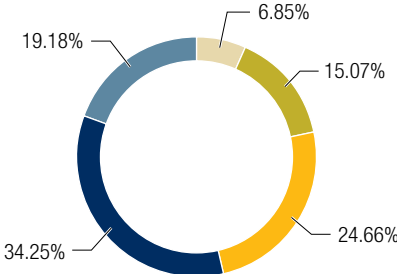


Maintaining top-line performance within our company



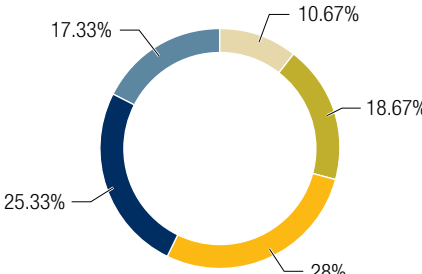
- Very Insignificant, 8%
- Somewhat Insignificant, 21.33%
- Neither Significant nor Insignificant, 18.67%
- Somewhat Significant, 30.67%
- Very Significant, 21.33%

Minimizing loss of key employees



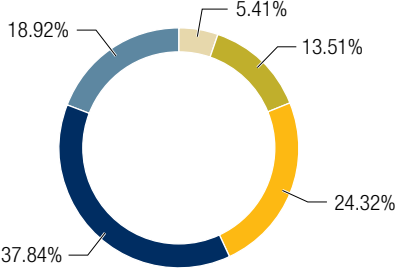
- Very Insignificant, 6.85%
- Somewhat Insignificant, 15.07%
- Neither Significant nor Insignificant, 24.66%
- Somewhat Significant, 34.25%
- Very Significant, 19.18%

Minimizing disruption to supply chain and other external partners



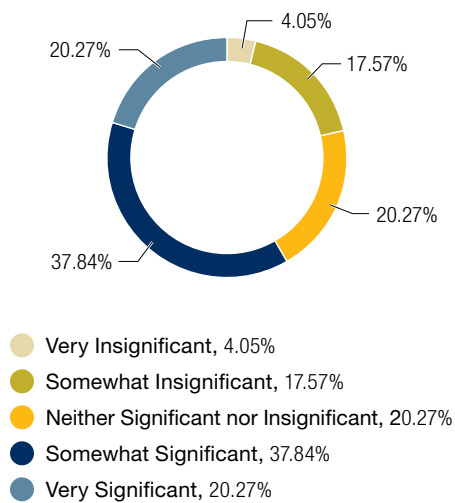
- Very Insignificant, 10.67%
- Somewhat Insignificant, 18.67%
- Neither Significant nor Insignificant, 28%
- Somewhat Significant, 25.33%
- Very Significant, 17.33%

Integrating back-office operations



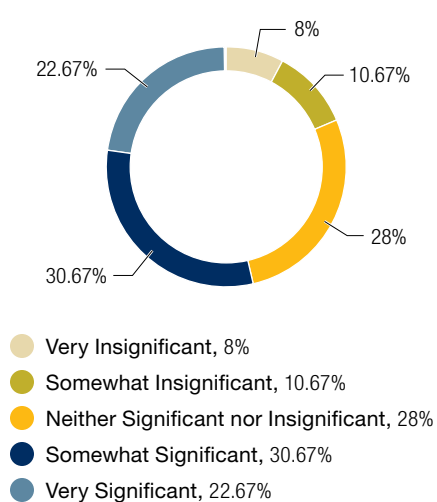
- Very Insignificant, 5.41%
- Somewhat Insignificant, 13.51%
- Neither Significant nor Insignificant, 24.32%
- Somewhat Significant, 37.84%
- Very Significant, 18.92%

Ensuring cultural assimilation



The executives report being challenged by a number of other factors as well. These include ensuring cultural assimilation (58 percent of executives say this is “somewhat” or “very significant”); integrating back-office operations (57 percent); minimizing loss of key employees (53 percent); avoiding lack of bandwidth, leading to employee burnout or items falling through the cracks (53 percent); and maintaining top-line performance within the acquiring company (52 percent). Minimizing disruption to the supply chain and other external partners (43 percent) was the only question in which less than half the respondents indicated that the queried factor was a challenge most of the time.

Avoiding lack of bandwidth, leading to employee burnout or items falling through the cracks

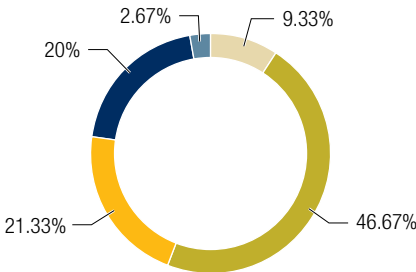


Cultural assimilation is blamed frequently for the M&A failure, and the results support that cultural issues are often a contributing factor. But certainly nailing only the cultural assimilation will not lead to a good transaction in most situations.

Avoid Underestimating Time and Resources

Synergy Capture

Q: Overall, how effective has your company been at capturing synergies that were targeted at the beginning of a transaction(s)?



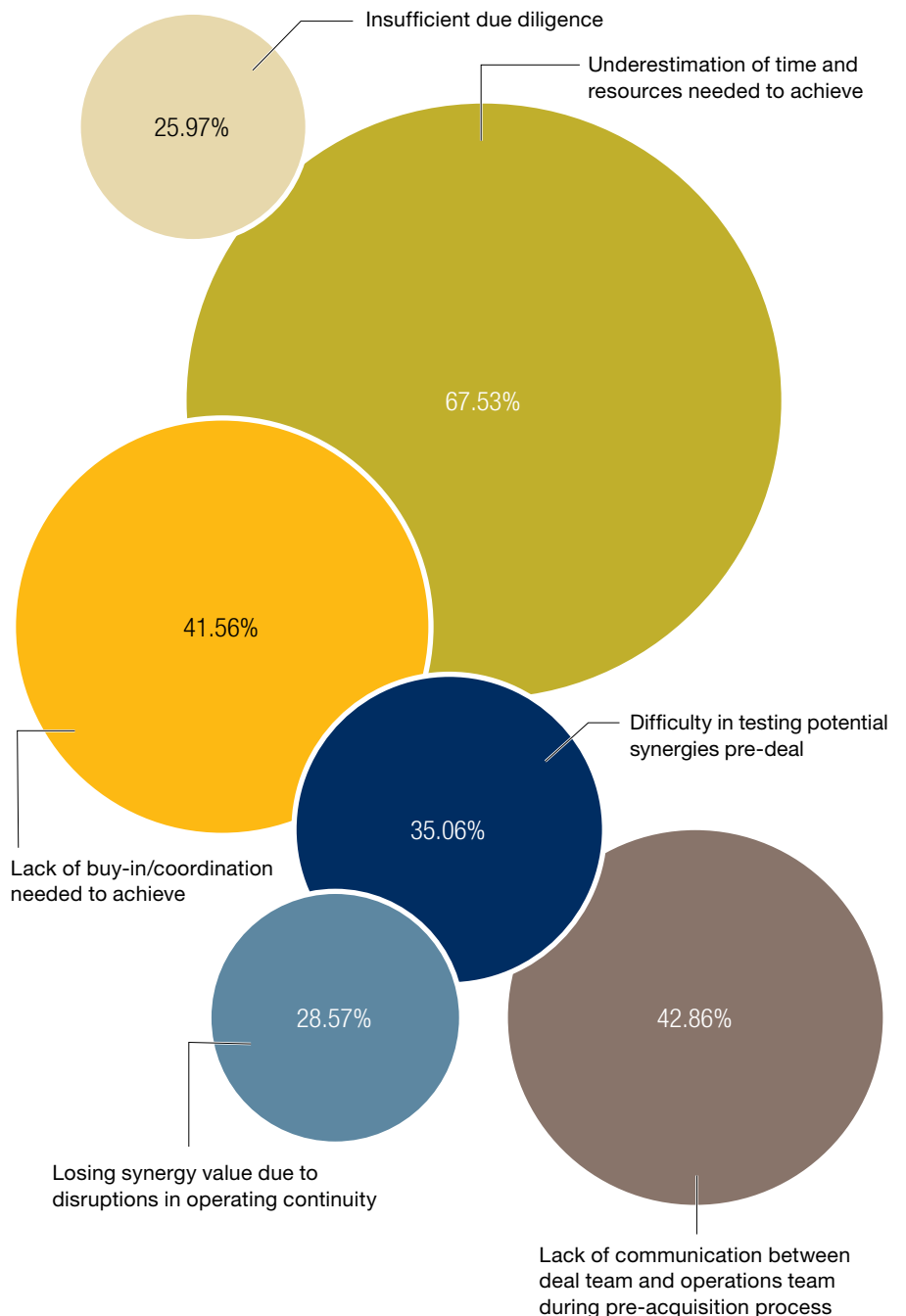
- Very Effective, 9.33%
- Somewhat Effective, 46.67%
- Neutral, 21.33%
- Somewhat Ineffective, 20%
- Very Ineffective, 2.67%

Only 9 percent of respondents say they are “very effective” and nearly half say they are “somewhat effective” at capturing synergies. Considering that synergies often drive deals – many of which are done specifically to capitalize on available cost savings and performance overlaps – it is promising that more than 50 percent of the respondents think their companies are “very effective” or “somewhat effective” at capturing synergies. On the other hand, as synergies frequently drive the deals to succeed or fail, it is surprising that less than 10 percent of companies have developed true strength in this area. This is a glaring point of opportunity to improve the deal success scoreboard.

Q: Based on your experience, which of the following challenges have the greatest negative impact on synergy capture in your company’s transactions? (Select all that apply.)

Companies are failing to capture synergies in large part because of underestimating the time and resources needed to achieve synergies. Many companies might not consider that the cost of the resources to achieve the synergy is a one-time cost and the synergies captured are likely to have a multiyear effect. Time and resource allocation is a far bigger issue than the next two challenges reported: the lack of communication between the deal team and operations team during the pre-acquisition process and the lack of buy-in/coordination. The communication issue between teams is surprising in that 43 percent of respondents indicate this as a reason for lost synergy despite the fact that this appears to be a contained-environment situation not influenced by third parties.

A logical progression is displayed in the survey results: When deal-making drags on, the attention paid to diligence is compromised due to unclear strategy, value drivers, and risks, and the subsequent synergies become harder to achieve. Much of this outcome also can be attributed to a reluctance to use external advisers and an overall lack of accountability for execution and results.



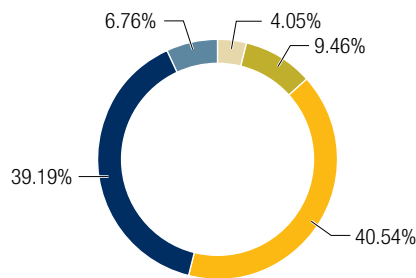


Joining Forces

People and Culture Management

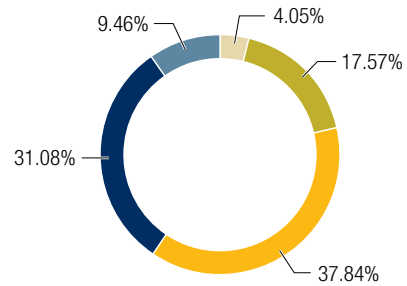
Q: How would you rate your company’s handling of the following people/cultural issues in prior transactions?

Identify people/cultural risks



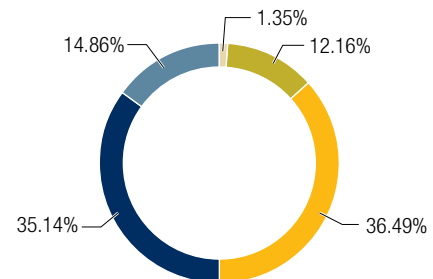
- Very Poor, 4.05%
- Poor, 9.46%
- Average, 40.54%
- Good, 39.19%
- Excellent, 6.76%

Winning the hearts and minds of the acquired company workforce



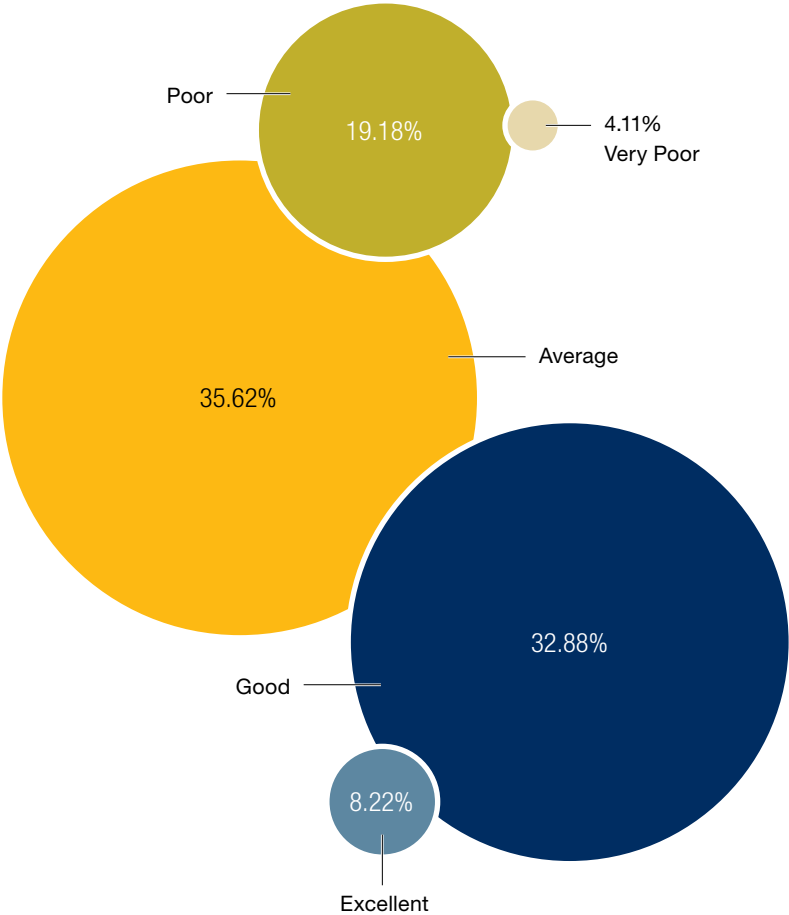
- Very Poor, 4.05%
- Poor, 17.57%
- Average, 37.84%
- Good, 31.08%
- Excellent, 9.46%

Executing human resources transition such as compensation or benefits changes



- Very Poor, 1.35%
- Poor, 12.16%
- Average, 36.49%
- Good, 35.14%
- Excellent, 14.86%

Alignment and communication of combined organization structure

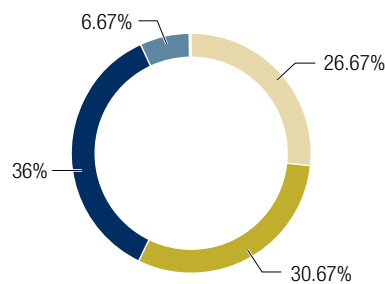


It appears to be particularly challenging for some executives to align and communicate about the structure of a combined organization. Almost a quarter of respondents say they do a “poor” (19 percent) or “very poor” (4 percent) job of that. Meanwhile 33 percent say they do a “good” job, and 8 percent say they do an “excellent” job.

Respondents seem most confident about their ability to execute human resource transitions such as compensation or benefits changes. Half say they do a “good” (35 percent) or “excellent” (15 percent) job of that, and only 1 percent report doing a “very poor” job.

However, the general confidence shown in these responses is not aligned with those to an earlier question about the challenges faced in maintaining operating continuity within the acquirer and the acquired company. Fifty-eight percent of respondents say that cultural assimilation is a “somewhat” or “very significant” challenge. It is possible that respondents who think their companies are only “average” at handling people/cultural issues are causing assimilation issues.

Q: Which of the following best describes how you feel about the impact people/cultural issues have on M&A deal failure?



- People/cultural issues are often the main reason for failure, 26.67%
- People/cultural issues are often blamed as the main reason for failure but can be used to mask issues that had a larger impact, 30.67%
- People/cultural issues are relatively equal to all the other issues that can impact deal failure, 36%
- People/cultural issues are never the reason for deal failure, 6.67%

As only 7 percent of respondents feel that cultural issues are never the cause of a deal failure, the results suggest that issues pertaining to people and culture can be significant hurdles for deal-makers. More than a third of respondents (36 percent) say that these issues can affect failure, and more than a quarter (27 percent) say that these issues are often the primary reason a deal fails.

However, nearly 31 percent of respondents say that blaming cultural issues often masks other issues. This answer is consistent with the results to an earlier question about maintaining continuity at the acquiring and acquired company. The results indicated several other areas that are more or almost as equally challenging to manage.

Experience Matters

Scalable Resources

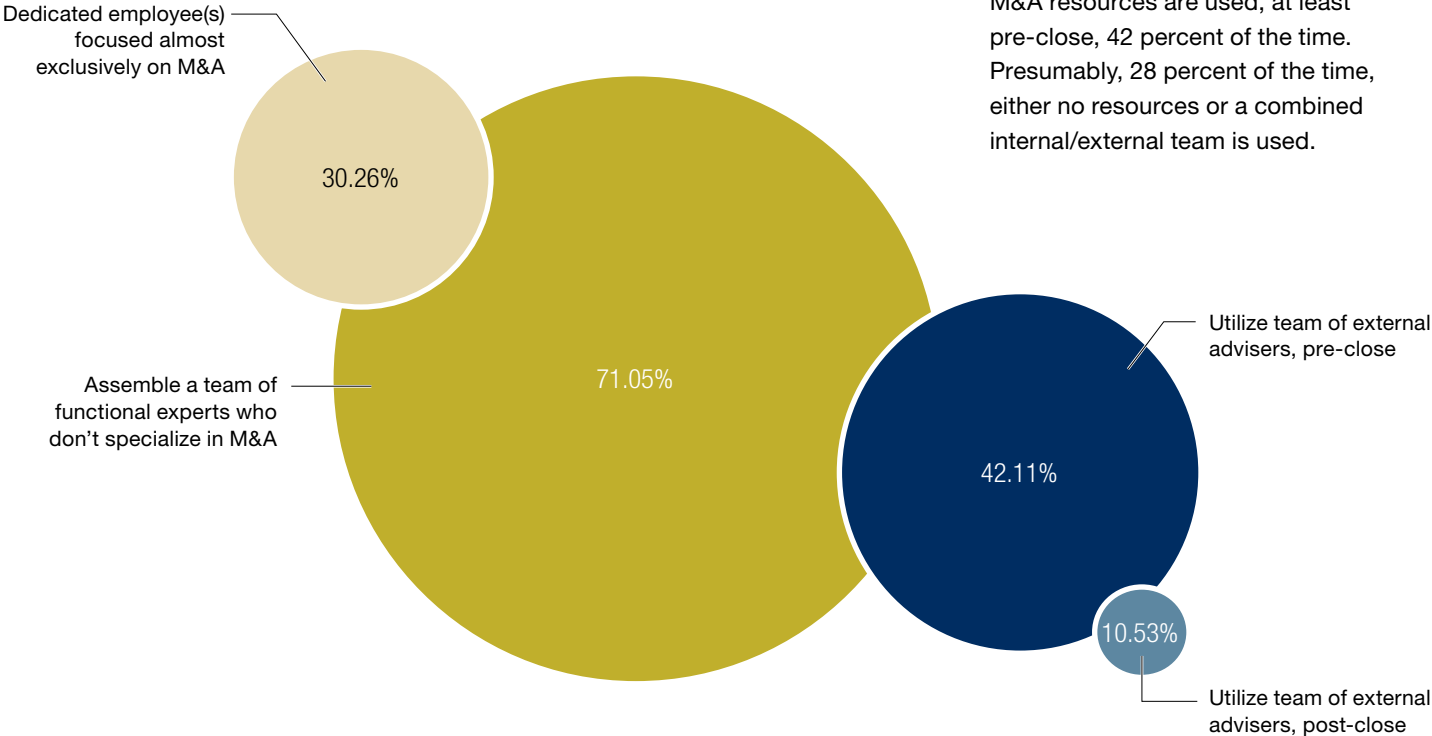
Q: How does your company typically manage resources with regard to conducting M&A deals? (Select all that apply.)

Many respondents indicate they tend to underestimate the time needed to complete a transaction. And the biggest challenge many face is maintaining clarity and focus. Yet somewhat surprisingly, relatively few appear to bring in outsiders with expertise in deal-making.

Moreover, companies might lack the help they need to make sure a deal is successfully implemented. According to the results, 42 percent of companies use external advisers before the deal closes, but only 11 percent use advisers after a close despite that the time commitment for integration is frequently much more than the pre-deal investigation and negotiation phase. This situation might contribute to the low number of respondents who report achieving all hoped-for efficiencies and synergies.

A full 71 percent say they assemble a team of experts who do not specialize in M&A. This fact suggests that most companies lack critical assistance, traits, and skills needed to close a deal.

Dedicated M&A employees are used 30 percent of the time, and external M&A resources are used, at least pre-close, 42 percent of the time. Presumably, 28 percent of the time, either no resources or a combined internal/external team is used.



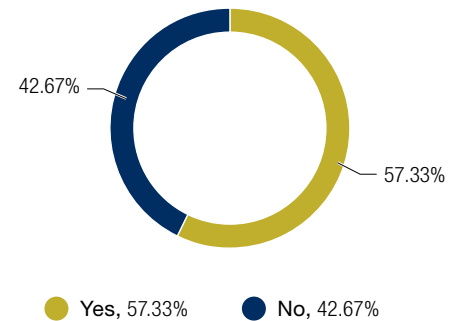
Q: How would you rank your company’s effectiveness at managing resources in the following ways? (1 = most effective; 6 = least effective)

- 1 Consistent involvement of internal resources throughout the pre-close deal process
- 2 Securing help, when needed, from external advisers, pre-close
- 3 Scaling internal resources to meet deal needs
- 4 Consistent involvement of internal resources throughout the post-close process
- 5 Securing help, when needed, from external advisers, post-close
- 6 Transitioning “handoffs” between teams through the course of the transaction

Respondents say their companies are best at consistently involving internal resources while the pre-close phase of the deal progresses and at securing help from external advisers when needed, again more often for pre- than post-close. Yet despite involving internal resources, respondents report they are worst at making the handoffs between teams while a transaction is on course. Given the lesser focus on post-deal activities, this might be when handoffs are dropped.

This issue should lead an executive to question whether his or her internal resources and the external advisers mentioned on the opposite page are fully equipped to complete successful handoffs needed to seal the deal. It is possible the deal teams are experienced at operating only in their pre- or post-transaction silo instead of having expertise in completing all phases of the M&A deal life cycle from strategy through execution.

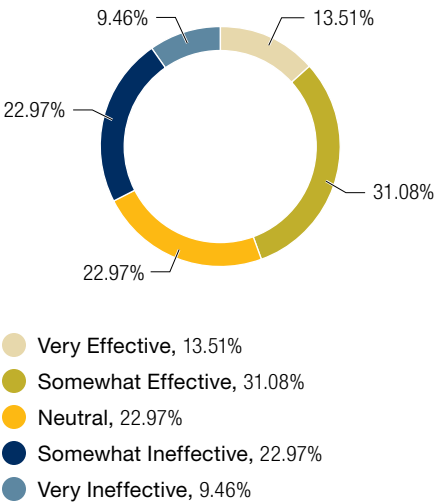
Q: Overall, given the mission critical and time-sensitive nature of M&A deals, do you feel your company has adequate resources (both internal business units and aligned external consultants) to address the current and expected deal flow?



More than half of respondents say their companies are equipped with the resources they need to handle M&A deals. Yet a low number of respondents report achieving maximum efficiencies and synergies from deals. Despite executives’ confidence in their resources, they might lack the proper resources to execute both the front and back end of a deal.

Measuring Success

Q: Overall, how would you rate your company's effectiveness at measuring/tracking rate of returns on closed transactions?



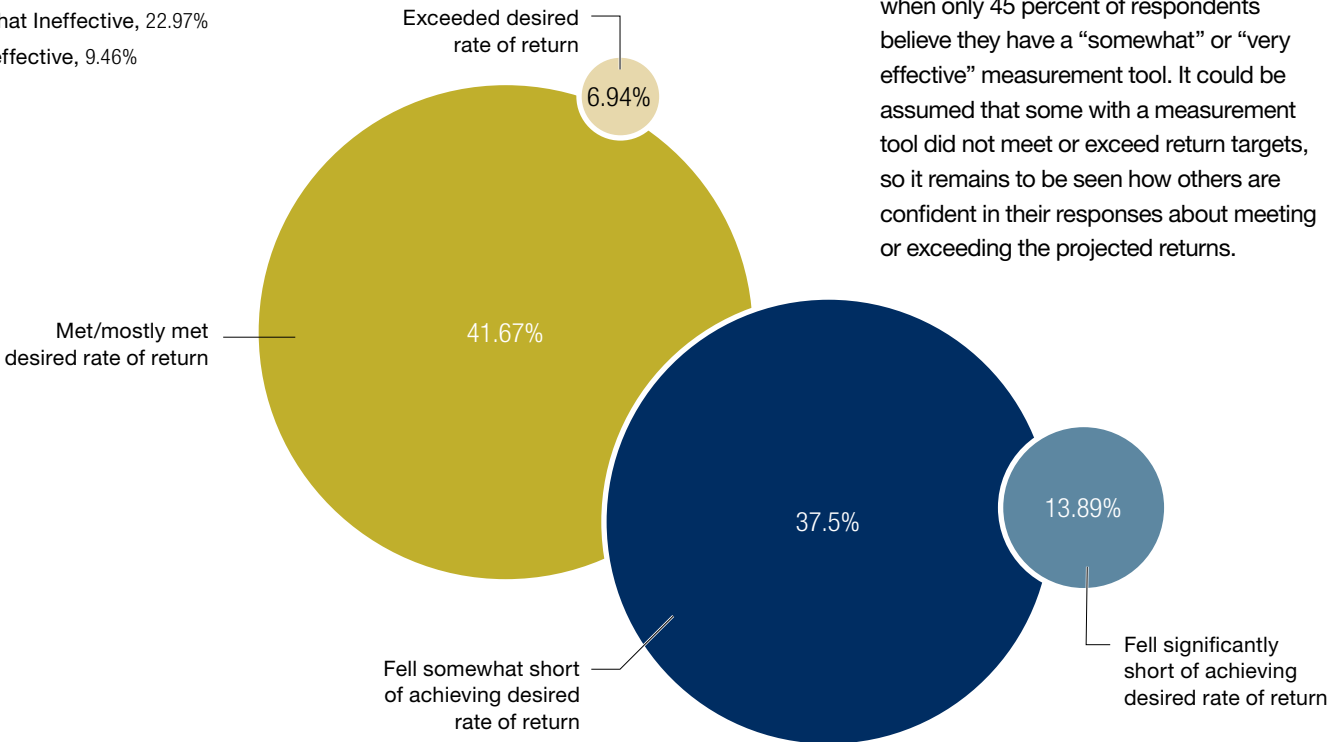
Q: Which of the following best describes your company's success in achieving the desired rate of return on closed transactions?

Given the level of capital required for most transactions, it is telling that only 14 percent of companies have an effective tool to measure returns on the capital deployed and only 45 percent of companies appear to have a tool that even somewhat tracks performance.

Almost half of respondents believe they are "somewhat" or "very effective" at tracking a transaction's rate of return, but nearly one-third must be disappointed to learn they are falling somewhat or significantly short of their goals.

Once again, this reinforces a theme: There is a gap between executives' confidence in their deal-making abilities and the outcomes of those deals. Many executives have a great deal of confidence in their teams and resources and claim to be equipped for deal-making. Executives who believe they are prepared would presumably expect high performance, yet many are not achieving the results they want.

Also revealing is that 49 percent of respondents believe that their companies meet or exceed the desired rate of return, when only 45 percent of respondents believe they have a "somewhat" or "very effective" measurement tool. It could be assumed that some with a measurement tool did not meet or exceed return targets, so it remains to be seen how others are confident in their responses about meeting or exceeding the projected returns.



Q. If you could improve one aspect of your company's deal execution, from pre-deal planning through post-close execution, what would it be?



"Better and more robust playbook, well executed at several levels of the organization."

"Having a dedicated M&A team from pre- and post-closing to monitor exact progress throughout the deal."

"Better upfront evaluation in front of the letter of intent and early due diligence review/involvement from a broader base of the company's functions."

"Pre-transaction estimate of post-merger implementation timeline: quality over speed."

"Improving the resources needed to do proper acquisitions."

"Post-closing integration plan."



The respondents appear to be dissatisfied with the level of involvement of experienced M&A professionals, particularly with post-transaction management.

Q. Based on your experience and other economic factors, how are deals being structured and completed differently than they were 12 months ago?

“

“More demanding in [terms of] faster time to process and complete.”

“Increased awareness of the future consequences of regulatory impact.”

“They are getting more detailed. More pre-diligence work is done with mathematical modeling.”

“More earn-outs in deal structure.”

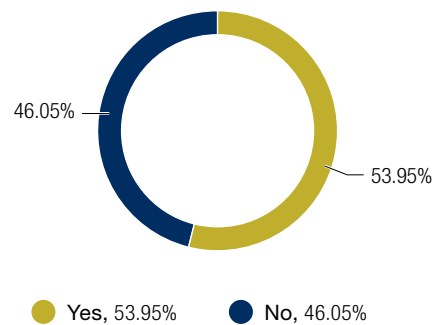
“Follow-up is starting to become important and is beginning to be measured/looked at.”

”

A takeaway from this list is increasing complexity, which necessitates that experienced deal professionals to be more involved in the pre-deal process.

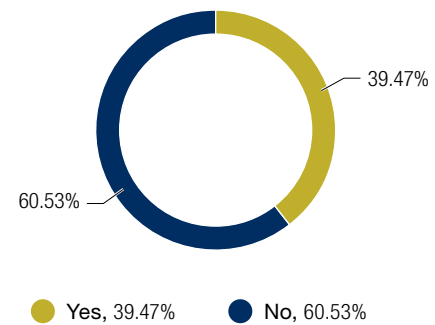
Looking Ahead

Q: Do you expect your company and its corporate development team to increase its sourcing and execution of M&A deals in the next 12 months?



Despite the fact that many M&A deals are producing less-than-ideal outcomes, respondents indicate that M&A will remain a priority in the coming year. This suggests that companies both recognize that deal-making is necessary and believe they can produce successful outcomes regardless of past experiences. With the level of capital available today in the forms of cash on balance sheets, strong stock valuations, and low-cost debt, it is surprising that more companies do not expect M&A to grow.

Q: Is your company actively pursuing or anticipating participating in cross-border transactions?



The majority of companies are not looking across borders to make deals. Considering the increasingly global nature of most businesses, this suggests that significant opportunities exist for the firms that seek out and seal cross-border deals.





Method

In November 2013, Crowe distributed its “Critical Pillars for M&A Success” survey via various digital channels and via hard copies to a group of senior executives. Representing companies of various sizes and industries, respondents identified themselves as CEOs, CFOs, corporate/business development officers, consultants, and other finance and M&A-focused titles.

Represented industries included manufacturing (30 percent), finance and insurance (17 percent), and professional, scientific, and technical services (9 percent). The companies also represented a variety of sizes in terms of annual revenue:

- Less than \$25 million (16 percent)
- \$25 million to \$49.9 million (11 percent)
- \$50 million to \$99.9 million (9 percent)
- \$100 million to \$199.9 million (11 percent)
- \$200 million to \$499.9 million (16 percent)
- \$500 million to \$999.9 million (9 percent)
- \$1 billion to \$4.9 billion (15 percent)
- \$5 billion to \$9.9 billion (5 percent)
- \$10 billion or more (7 percent)

Due to rounding, percentages used in all questions might not total 100 percent. Percentages in certain questions exceed 100 because respondents were asked to check all answers that applied. Also, a few minor edits were made to verbatim responses to correct spelling, punctuation, and verb tense.



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