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Source: *Strategic Management Journal*, Mar. - Apr., 1988, Vol. 9, No. 2 (Mar. - Apr., 1988), pp. 173-183

Published by: Wiley

Stable URL: <https://www.jstor.org/stable/2486031>

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TOP MANAGEMENT TURNOVER FOLLOWING MERGERS AND ACQUISITIONS

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Little is known about the effects of a merger or an acquisition on an acquired company's management team. This research follows the employment status of target companies' top managers for 5 years from the date of acquisition. Results indicate that turnover rates in acquired top management teams are significantly higher than 'normal' turnover rates, and that visible, very senior executives are likely to turn over sooner than their less-visible colleagues. Variations in top management turnover rates, however, are not accounted for by type of acquisition (i.e. related or unrelated).

Between 1965 and 1985 there were 62,246 merger and acquisition transactions involving at least \$500,000 (Ellwood, 1987). Notwithstanding the prevalence of such activity, our understanding of the organizational implications of mergers and acquisitions is limited (Jemison and Sitkin, 1986). The primary research focus to date has been the study of financial returns from both an accounting perspective (Mueller, 1977) and a finance perspective (Halpern, 1983; Jensen and Ruback, 1983). The study of strategic fit has also been prominent in the literature (Rappaport, 1979; Rumelt, 1974; Salter and Weinhold, 1979). We have very little systematic evidence, however, that would suggest how a merger or an acquisition affects the management of an acquired company. The little research that does exist has been criticized for its flawed methodologies (Marks, 1982). The intent of the present research then is to begin to build a foundation of organizational research on mergers and acquisitions by investigating the employment status of target companies' managers following mergers and acquisitions.

The turnover of top management following a

merger or an acquisition has received attention from both managers and academicians. A recent *Wall Street Journal* article by Bennett (1986: 19) proclaimed (without evidence) that 'mergers and acquisitions are removing scores of CEOs from their jobs'. The article went on to chronicle the personal toll of such a job loss. Potential target managers reading *Newsweek* two months later ('Confessions of a raider', 1986: 52) could not have been heartened by the reported interview with Carl Icahn. When discussing his acquisition of TWA, he said:

At TWA—to make it simple, we basically replaced all the top management. That's one of the steps we took in the first few months. We really replaced the whole 42nd floor. There's nobody there on the 42nd floor at 605 Third Avenue who was there before. Possibly there's one but I think he's leaving. And it had to be done.

There is no consensus in the academic community about the extent or desirability of top management turnover following mergers and acquisitions.

One of Drucker's (1981) widely cited five rules for successful acquisitions is that the acquiring parent company must be able to supply top management for the target company within 1 year. Drucker (1981) does not argue that the parent company should dismiss the target company's management; he is just warning the parent company to be prepared for very high turnover among the target company's management team. Parsons and Baumgartner (1970) and Pitts (1976), however, point out that a parent company's intent is often to acquire and successfully integrate a team of skillful managers. Indeed, the acquisition of the target's top management may be a key attraction of the merger. If they are correct there may not be strong pressures on the target's managers to depart; or, if the pressures are there, some acquiring companies may take steps to ensure the retention of the newly acquired management teams.

In fact we do not know what typical turnover rates are among an acquired target's top management team. The only data that have been reported are the results of a cursory study by a management consultant of '200 acquisitions made by a core group of *Fortune 500* companies' (Hayes, 1979: 42). Hayes (1979) reported that only 42 percent of top management stayed with the merged entity for 5 years after the merger. After acknowledging some methodological problems he conjectured that this figure reflected just 'the tip of the iceberg' (p. 42). The intent of the current research is to document the extent of the phenomenon and begin to understand the origins of such turnover.

A number of theoretical perspectives inform our understanding of top management turnover following a merger or an acquisition. At least three forces would seem to contribute to such turnover. First, mergers and acquisitions breed uncertainty among top managers (Simmons, 1984). Given that uncertainty and a lack of valued information has been related to turnover intent (Walsh, Ashford and Hill, 1985), we would expect to see higher than normal top management turnover rates following a merger or acquisition. Managers who either cannot tolerate or reduce uncertainty are likely to withdraw from the firm. Second, all organizations have their own unique cultures (Smircich, 1983). Buono, Bowditch and Lewis's (1985) detailed analysis of a bank merger

revealed that the merging of two distinct cultures can produce 'feelings of hostility' and 'significant discomfort'. They referred to these kinds of post-merger experiences as 'culture shock'. Managers who are either unwilling or unable to adapt to a possibly profound culture shock are likely to leave their organization. Third, mergers and acquisitions have been argued to reflect a market for corporate control, wherein companies compete for the right to determine the management of a target company's resources (Fama and Jensen, 1983). If such competition produces clear winners and losers, we would again expect to see higher than normal top management turnover rates in a target company following a merger or an acquisition. Accordingly:

H₁: A target company's top management turnover rate following a merger or acquisition is likely to be higher than the normal rate for an equivalent non-merged company.

Drucker's (1981) prediction of high top management turnover might not be completely at odds with the prediction of low turnover derived from Parsons and Baumgartner (1970) and Pitts (1976). The extent of top management turnover may depend upon the type of merger or acquisition. It is important to note that different kinds of synergies might be expected from any particular acquisition. Chatterjee (1986), for example, noted three kinds of expected synergies: collusive, operational and financial; Lubatkin (1983) also noted three kinds of synergies: technical, pecuniary and diversification; while Rumelt (1974) noted two: financial and operating. The retention of top management, therefore, might be differentially important across various types of acquisitions.

The Federal Trade Commission (FTC) has created a five-fold category system for classifying mergers and acquisitions. This system is based on the primary economic relationships established between the parent firm and the target firm. The five categories are thought to be mutually exclusive:

1. *Horizontal*. An acquisition is horizontal when the companies involved produce one or more of the same, or closely related, products in the same geographic market.

2. *Vertical*. An acquisition is vertical when the two companies involved had a potential buyer-seller relationship prior to the merger.
3. *Product extension*. An acquisition is considered to be product extension in type when the acquiring and acquired companies are functionally related in production and/or distribution but sell products that do not compete directly with one another. An example of a product extension merger would be a soap manufacturer acquiring a bleach manufacturer.
4. *Market extension*. An acquisition is considered to be market extension in type when the acquiring and acquired companies manufacture the same products, but sell them in different geographic markets. An example of a market extension merger would be a fluid milk processor in Washington acquiring a fluid milk processor in Chicago.
5. *Unrelated*. This category involves the consolidation of two essentially unrelated firms. An example would be a shipbuilding company buying an ice cream manufacturer. *Statistical Report on Mergers and Acquisitions, 1978* (1980: 108–109).

Drucker's (1981) predictions of widespread top management turnover may be more relevant to related acquisitions than unrelated acquisitions. While it is difficult to predict the relative turnover rates among all five types of acquisitions it is likely that top management retention would be less important to the acquirer in the four types of related acquisitions. That is, the parent company's management is already familiar with the target company's business, and can perhaps afford to lose members of the target's management team. Indeed, the parent company may feel that they can add value to the target company by replacing the target's management team with their own skilled managers. In Parsons's (1960) terms, the institutional functions provided by the target company's top management become redundant with the parent's top management duties. The parent is likely to replace the institutionally oriented management team with a 'managerial' team to act as a liaison between their own institutional leadership and the technical leadership in the acquired target. Pitts (1976), however, argued that the retention of top management is crucial for a company that chooses

to diversify by acquisition, because the acquiring firm cannot afford to lose the product and market experience of the target company's management. This should be especially true in unrelated acquisitions, when the acquiring company's management is unfamiliar with the target company's business. It is likely that they would take steps to retain the target's top management in such cases. Following Parsons (1960), the parent company would still need the institutional leadership provided by the target's top managers. These managers are familiar with their organization's environment and provide legitimacy in that environment. Accordingly:

H₂: A target company's top management turnover rate is likely to be higher following a related merger or acquisition than following an unrelated merger or acquisition.

Not all management turnover following a merger may be voluntary. Pfeffer (1981), in fact, discussed the symbolic value of managerial succession. He argued that the replacement of only a few key executives 'provides symbolic ratification of the intention to change organizational operations, and presumably, the effectiveness of those operations' (Pfeffer, 1981: 39). Given that acquired companies are sometimes thought to be burdened with ineffective management teams (Manne, 1965), we would expect to see visible, very senior executives turn over more quickly than their colleagues of somewhat lesser status, regardless of merger type. Accordingly:

H₃: A target company's very senior top managers are likely to turn over more quickly than their colleagues of somewhat lesser rank.

In sum, these hypotheses will be tested using data that track the employment status of acquired target companies' top management teams for 5 years from the date of the acquisitions. This research provides the first systematic evidence of top management turnover following a merger. Hypotheses regarding the relative magnitude of these rates for merged and non-merged companies, and among the different types of acquisitions, will be examined. Predictions about the relative timing of turnover among members of the top management teams also will be investigated.

METHODS

Sample

The research sample comprised an experimental group of acquired companies and a control group of a matched sample of companies not involved in merger and acquisition activity during the observation period. Each will be described in turn.

A sample of acquired companies was drawn from the *Statistical Report on Mergers and Acquisitions, 1979* (1981). This report was published each year by the FTC, ending with the publication of the 1979 data in 1981. The report lists all manufacturing and mining companies with assets of at least \$10 million that were acquired by publicly held U.S. companies. Table 1 displays the number of acquisitions by type per year sampled.

All of the companies involved in the vertical and market extension acquisitions, and a random sample of 30 companies contacted from each of the remaining three categories, were asked to participate in this study. The years 1975 to 1979 were chosen to study to avoid the unique merger waves of both the 1960s and early 1970s, and the most recent merger wave of the 1980s (Scherer, 1986).

A total of 130 surveys were sent to the parent companies represented in this sample. 75 surveys were returned. However, 20 of the 75 responses indicated that they could not provide us with any information either because the data were unavailable or because the acquired company was subsequently divested. As such, data are available for 55 acquisitions that occurred between the years 1975 and 1979. The overall response rate was 58 per cent, while the useful response rate was 42 percent. It should be noted, though, that five of the 55 countries sent us incomplete data. Accordingly we have data on individual

managers representing 55 acquisitions, but complete management team data on 50 acquisitions. The response rate at the company level of analysis then is 39 percent. Nevertheless, these response rates were much higher than the 20 percent mailed survey response rate predicted by Gaedeke and Tootelian (1976). The final sample comprised 11 horizontal mergers, 11 vertical mergers, 11 product extension mergers, five market extension mergers, and 17 unrelated mergers. The mean target company asset size in this sample was \$77.87 million with a standard deviation of \$127.52 million.

A control group of 30 companies not involved in a merger during this same time period was drawn from the *Standard and Poor's Stock Guide*. The 30 companies were distributed over the New York and American Stock Exchanges and were of comparable asset size. Six had assets of between \$30 and \$60 million; 18 had assets between \$60 and \$90 million; and six had assets between \$90 and \$130 million at the time of initial observation. The average ages of the managers in each sample were not significantly different (merged companies, $\bar{x} = 50.3$ years; non-merged companies, $\bar{x} = 49.0$ years). The year of initial observation was controlled to be evenly distributed over the years 1975-79 inclusive.

Procedure and operationalizations

The first task was to identify each member of the 130 target companies' top management teams at the time of the merger or acquisition. This information was found in each company's 10-K or proxy statement. After identifying each executive by name, age, and position, a survey was prepared. A call to each parent company identified a human resources officer to whom we could mail the survey. The survey identified each

Table 1. Total number of acquisitions by FTC category

Merger category	1975	1976	1977	1978	1979	Total
Horizontal	4	12	26	22	5	69
Vertical	3	4	4	13	5	29
Product extension	25	26	38	37	41	167
Market extension	1	8	0	0	2	11
Unrelated	26	27	32	39	44	168
Total	59	77	100	111	97	444

member of the target's top management team at the time of the merger. The average size of the top management team was 8.93 managers with a standard deviation of 3.11. It asked the human resources officer in the parent company to examine their personnel records and report the subsequent career histories for each executive. The parent company representative was asked to identify whether or not each executive was still employed by what was the target company. If the executive had left the target company the representative was asked to provide the date of departure.

To create a comparison referent, the names of each executive in the 30 companies that comprised the control group were identified in each company's 10-K or proxy statement. Their employment status was then tracked in the 10-Ks or proxy statements for 5 years from the point of initial observation.

RESULTS

The percentage of turnover among the top management teams was computed at each of 5 years following the date of the merger in

the experimental group, or the time of initial observation in the control group. Figure 1 profiles the top management turnover rates in the two groups.

T-tests were performed to test the hypothesis that the top management turnover rate would be higher in the merged companies than the non-merged companies. As Table 2 indicates, this hypothesis was supported for each year. The percentage of the top management team that turned over in the merged companies was significantly higher than the turnover rates in the non-merged companies at the end of each of the 5 years assessed (at the 0.001 level of significance). The turnover rate in the target companies steadily increased from 25 percent in the first year after the merger, to 59 per cent (inclusive) in the fifth year. The turnover rate in the control group of non-merged companies also increased steadily through time, but at a lower rate. The turnover rate ranged from 2 percent to 33 percent.

It is interesting to observe that while the turnover rate in the first year was significantly different between the two groups, the rate of increase from these different baselines is almost equivalent. Only the rate of increase between the fourth and fifth year was significantly differ-

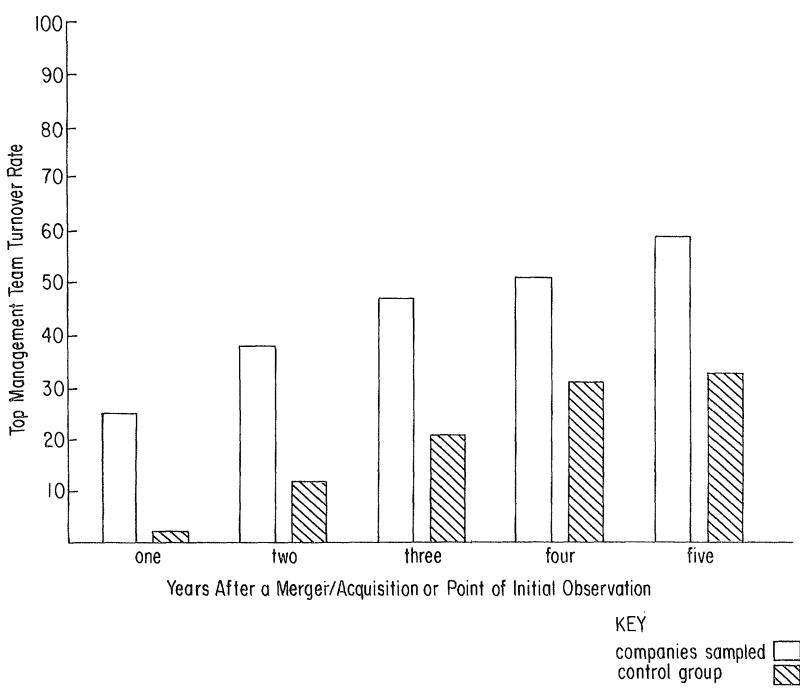


Figure 1. Top management turnover following mergers and acquisitions

Table 2. *T*-tests: top management team turnover rates in merged and non-merged companies

Variable	Number of cases	Mean	Standard deviation	<i>T</i> value	2-tail probability
One-year turnover rate merged companies	50	0.25	0.28	4.35	0.000
non-merged companies	30	0.02	0.06		
Two-year turnover rate merged companies	50	0.37	0.29	4.33	0.000
non-merged companies	30	0.13	0.14		
Three-year turnover rate merged companies	50	0.46	0.29	4.29	0.000
non-merged companies	30	0.21	0.16		
Four-year turnover rate merged companies	50	0.52	0.28	3.48	0.001
non-merged companies	30	0.31	0.24		
Five-year turnover rate merged companies	50	0.59	0.25	4.61	0.000
non-merged companies	30	0.33	0.24		

ent. The turnover increased 7 percent in the merged companies and only 2 percent in the non-merged companies during that period, $t(1,78)=2.33$, $p<0.05$. There were no significant differences between the two groups of companies in the rate of turnover increase between the first and second, second and third, and third and fourth years.

T-tests were performed to test the second hypothesis that the top management turnover rate would be higher following a related acquisition than an unrelated acquisition. While the mean 'related' turnover rate was higher than the 'unrelated' mean in each year, none of the differences reached statistical significance. Moreover, a series of ANOVAs were performed to test for mean differences in top management turnover rates among the five types of acquisitions at each of the 5 years of observation. All of the ANOVAs were non-significant. As such,

hypothesis 2 was not supported with these data. Table 3 reports the descriptive statistics for top management turnover by the type of acquisition.

While top management turnover rates are not related to the type of merger that took place, it is possible that the rate of top management turnover could be related to the size difference between the two companies. That is, a very large company is likely to have a supply of skilled managers on hand to replace the managers in a small acquired company. In such circumstances we might expect to see high management turnover rates in the acquired companies. An exploratory analysis will examine this possibility. To test this alternative hypothesis the logarithms (base 10) of both the parents' and targets' assets were computed. Logarithms were employed because of the sizeable variance in the assets. Pearson product-moment correlations were then computed between the turnover rates at each of the

Table 3. Descriptive statistics: top management turnover rates by type of merger or acquisition (mean, with standard deviations in parentheses)

Type of merger or acquisition	Years after a merger or acquisition				
	One	Two	Three	Four	Five
Horizontal	24.91 (23.36)	41.27 (23.92)	43.09 (26.14)	51.55 (29.27)	61.27 (20.73)
Vertical	28.36 (30.80)	34.91 (30.30)	45.18 (30.47)	49.91 (30.14)	59.73 (29.24)
Product extension	24.00 (29.51)	35.10 (29.93)	50.40 (32.40)	54.60 (28.90)	59.10 (28.60)
Market extension	37.25 (30.90)	43.50 (41.72)	46.50 (39.15)	52.50 (33.68)	64.00 (24.17)
Unrelated	20.43 (31.15)	36.00 (31.10)	44.21 (27.15)	51.14 (27.49)	55.21 (25.63)

Note: All statistics are expressed as percentages.

5 years, and the difference between the logarithm of the parents' assets and the logarithm of the targets' assets at the time of the merger. A significant positive correlation between these two variables would support this alternative hypothesis. As Table 3 indicates, none of these correlations reached statistical significance. In fact the relationship between the asset size difference and top management turnover was negative in the first year after the merger, suggesting a slight tendency for such parent companies to retain top managers in the first year following a merger.

The sample of 761 managers was then divided into two groups to test the hypothesis, derived from Pfeffer (1981), that more senior-level executives in the target companies would turn over more quickly than their colleagues of lesser rank. The first group was comprised of 55 of the 142 presidents, CEOs, or chairmen of the board that departed within 5 years of the acquisition date. The second group was comprised of 168 of the 619 vice-presidents, senior and executive vice-presidents, controllers, secretaries, and treasurers that turned over within 5 years of the merger. A *t*-test revealed support for the third hypothesis. The group of presidents left their company in an average time of 17 months, while the vice-presidents left, on average, in 23 months $t(1,221)=2.07$, $p<0.05$. It is also interesting to observe that a total of 39 percent of the

Table 4. Pearson product-moment correlations between top management turnover and parent-target asset size difference

	Top management turnover (years)				
	One	Two	Three	Four	Five
Asset size difference	-0.06	0.18	0.11	0.06	0.05

'presidential group' left their companies within 5 years, while only 27 percent of the 'vice-presidential group' departed within 5 years.

Finally, it should be noted that in an exploratory ANOVA the interaction effect between management level and type of acquisition was non-significant for the time-to-departure variable. Moreover, this same interaction did not significantly explain top management turnover in any of the years following a merger or acquisition.

DISCUSSION

The results of this research provide the first systematic evidence of the employment status of senior executives following a merger or an acquisition. Hypothesis 1 was supported with these data. Top management turnover rates

following a merger or acquisition are significantly higher than 'normal' top management turnover rates. These rates are generally consistent with Hayes's (1979) earlier results. Recall that 58 percent of his *sample* of managers had turned over within 5 years of a merger. The current results indicate that 59 percent of each *company's* top management team departs within 5 years of a merger.

The descriptive portrait alone provides a basis to discuss Drucker's (1981) 'rule' that the parent company must prepare to replace the acquired company's top management team within the first year of the acquisition. These results indicate that the parent company should be ready for management turnover occurring at more than 12 times the normal rate, but that only one-quarter of the target's management team is likely to turn over within the year. Paine and Power (1984) questioned Drucker's (1981) assumption that the target's managers would naturally leave their company after an acquisition. They argued that the parent company could work to retain the target's management, and not just quietly accept the fact that they will leave. The results of this investigation indicate that, independent of what the parent company might do, the magnitude of the turnover 'problem' may not be as great as Drucker (1981) or Paine and Power (1984) feared. Nevertheless, Drucker's (1981) specific concern with turnover in the first year after an acquisition would seem to be appropriate, given that the rate of increase in the turnover rate between merged and non-merged companies is nearly equivalent beyond this first year.

It was hypothesized that the extent of top management turnover would vary as a function of the type of acquisition. Drucker's (1981) prediction of high turnover rates was hypothesized to be most relevant to related acquisitions, while Pitts's (1976) vision of low turnover rates was predicted to characterize unrelated acquisitions. These results indicate that there is some variance in top management turnover rates following an acquisition, but that the type of merger, or even the size difference between the acquiring and acquired companies, does not account for this variance.

The support for the third hypothesis that very senior executives are the first to turn over following an acquisition is noteworthy. Although it is impossible to tell from these data whether this turnover was voluntary or involuntary, it

does provide some evidence in support of Pfeffer's (1981) theory of the symbolic value of managerial succession.

FUTURE RESEARCH NEEDS

The present research has documented the extent of top management turnover following mergers and acquisitions, and examined possible origins of such turnover. Although we have positioned this investigation in the mergers and acquisitions literature it is also a part of a broader stream of research on executive turnover and succession. Turnover and succession studies have been conducted in private firms (Dalton and Kesner, 1985; Helmich and Brown, 1972; Johnson *et al.*, 1985; Reinganum, 1985; Worrell *et al.*, 1986); government (Bunce, 1980; Brunk and Minehart, 1984); professional sports teams (Allen, Panion and Lotz, 1979; Brown, 1982; Pfeffer and Davis-Blake, 1986); and even churches (Smith, Carson and Alexander, 1984). This research has generally focused on understanding the level of performance that predicts executive turnover. Once this turnover has occurred, it has also examined the nature of executive succession and its effects on subsequent performance. Building upon the logic of this research tradition, we need to know much more about the origins and consequences of top management turnover following mergers and acquisitions.

We know now that top management turnover in merged and acquired firms is higher than normal, but we do not know why. Future research needs to proceed at both the individual and organizational levels of analyses. At the individual level we need to specifically examine the role that uncertainty, ambiguity, stress, culture shock, and the like play in an executive's decision to turn over. At the organizational level we need to examine the governance implications of such turnover. Fama and Jensen (1983) and Manne (1965) view mergers and acquisitions as a means of replacing inefficient managers with efficient managers. The target companies' performance needs to be assessed prior to the merger or acquisition to determine if a market for corporate control, in fact, is operating. One might predict higher turnover rates among the poorly performing target companies. A similar prediction could be derived from Nystrom and Starbuck's (1984) and Starbuck and Hedberg's (1977) organizational

learning perspective. They view the replacement of top management as the only certain way to ensure that outdated learnings and world-views do not interfere with a company's adaptation to an environmental crisis.

Neither the type of merger and acquisition nor the size difference between parent and target company explained the variance in the turnover rates. The implications of parent-target organizational size differences needs further investigation for at least two reasons. First, we know that organizational size is associated with different patterns of executive succession (Dalton and Kesner, 1983). Smaller firms are more likely to experience outside succession than larger firms. Second, the present investigation suffered from a restriction of range problem. We sampled only among the 444 mergers and acquisitions involving \$10 million or more in the 5 years between 1975 and 1979. Ellwood (1987), however, pointed out that a total of 11,031 mergers and acquisitions involving \$500,000 or more took place during the same time period. Future research should sample these smaller mergers and acquisitions to understand the full impact of organizational size differences on top management turnover.

The acquisition process itself can be crucial to a successful acquisition outcome (Jemison and Sitkin, 1986). The acquisition negotiations themselves may affect subsequent organization fit. Indeed, Hayes (1979) found that 'professional' negotiations were associated with top management retention. By 'professional' he meant that they 'took place on both social and business levels' (p. 42). Research that examines the nature of the acquisition negotiations (i.e. distributive vs. integrative; Walton and McKersie, 1965) and its subsequent effect on top management turnover would be welcomed.

The succession event itself needs additional research. We know that very senior executives depart more quickly than their less senior colleagues. We do not know, however, who takes their place. As noted earlier, Parsons (1960) might predict that more managerially oriented executives might replace the more institutionally oriented executives in a related merger or acquisition.

Finally, the consequences of such top management turnover should be examined at the individual and organizational levels of analysis. At the individual level we need to know what happens to the careers and personal lives of those

executives who lose their jobs. The anecdotal evidence cited by Bennett (1986) would indicate that these executives incur some cost in this transition. At the organizational level future research needs to determine if top management turnover is associated with a subsequent improvement or decrement in company performance. Given that these target companies cease to exist independently upon the completion of the merger or acquisition, however, it will be difficult to obtain the valid performance data needed to examine these relationships.

CONCLUSION

Jemison and Sitkin (1986) recently called attention to the paucity of empirical research on issues of organizational fit following mergers and acquisitions. Notwithstanding our many well-reasoned prescriptions, we really know little about how to integrate an acquired company into a parent company. By giving us some insight into what 'typical' top management turnover rates might be for merged (and indeed, non-merged) companies, this research begins to build the empirical foundation upon which to understand issues of organizational fit. We still do not know, however, how these rates affect subsequent organizational performance. Nor do we fully understand what is responsible for the variance in these turnover rates. Additional research should aim to understand both the origins and consequences of top management turnover following mergers and acquisitions.

ACKNOWLEDGEMENTS

The author would like to thank Susan Ashford, John Ellwood, and the anonymous reviewers for their comments on an earlier version of this paper. Kathy Jardine and Lisa Lehman deserve thanks for their help in collecting and coding these data. The financial support of the Tuck Associates Program is gratefully acknowledged.

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