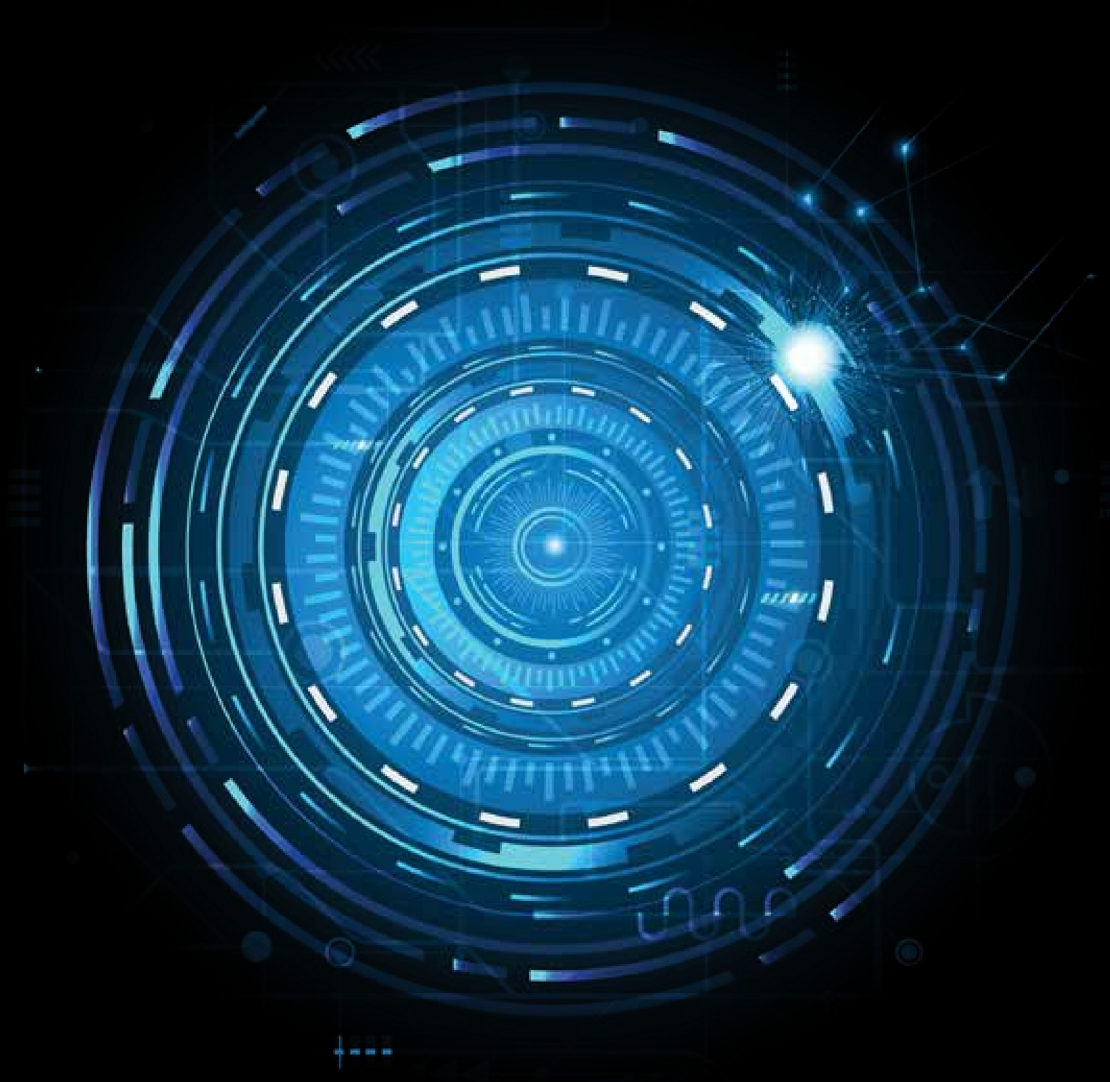

Health care mergers and acquisitions
The IT factor

What's at stake?

Executive summary

Mergers and acquisitions (M&A) continue to be relevant strategies in the toolboxes of health care provider organizations. The number of hospital and health system mergers and acquisitions continued an upward trend in 2017. This trend is fueled by a number of factors including:

- Demand for more comprehensive care
- Financial pressures to reduce costs and improve margins
- Competition for expanded markets

M&A activity is viewed as a key enabler for responding to changes in reimbursement models from transaction/volume to value-based care, and outcomes are often highly dependent on the degree of IT enablement in the merged organization. Failure to realize planned synergies or overruns on planned cost can jeopardize an organization's viability. While the executive team knows that IT will play a role in bringing the two organizations together, it is a frequently made mistake to not engage IT early enough in the transaction. In fact, due diligence may even be too late in the process to bring IT considerations to the forefront – IT should be a primary consideration from the very beginning, including defining the IT strategy in supporting the M&A and defining the expected benefits.

Why is IT so critical in the early stages?

If IT is not baked into the earliest stages of M&A, carefully considered in due diligence, planned for in integration strategies, and supported in execution by a robust project plan and governance, provider organizations can find themselves in the situation of a merger with spiraling IT costs and mounting frustration for lack of efficiencies gained, putting the future in serious doubt.

Upwards of seventy percent of expected synergies in M&A transactions are interdependent on IT capabilities. If not well planned and managed, IT costs can be significantly under estimated and spiral out of control. This can have significant impact on the long-term financial and operational benefits of the merged organization. Failing to include IT in the early stages of planning can result in misaligned expectations once a deal is struck. Determining the right IT strategy in the context of M&A includes carefully evaluating instances and systems consolidation to gain economies and reduce costs, investing in strategic market differentiating IT capability, and determining a strategy for outsourcing non-core functions.

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Our take

Industry activity and the role of IT

The health care sector is striving to deliver more effective care at a lower price amidst a dramatic shift in business, clinical, and operating models. This dramatic shift is the consequence of a number of factors including an aging population, an intensified focus on quality and value of care, ever-evolving regulatory requirements, and innovative treatments and technologies.[1] These factors often lead to increasing costs to patients and increased spending by providers on care, infrastructure, and technology. Health care systems will likely continue to pursue strategies to decrease costs while maintaining a high standard of care.

One recent trend in this regard is the movement toward a larger footprint, control of all points of access to care, and the ability to offer services in all phases of patient care. This has primarily been achieved through M&A as smaller hospitals and independent physician groups fuse into larger health care systems to realize economies of scale. M&A will likely continue to be a defining and impactful activity in the provider marketplace.

Common drivers of the surge in M&A activity include:

- Demand for more comprehensive and integrated care
- Ability to respond to change in reimbursement models from transaction/volume to value-based care
- Financial and operational pressures to reduce costs and improve margins
- Competition for expanded markets and services that increase populations served and referral channels while diversifying risk

Role of IT in M&A in early stages

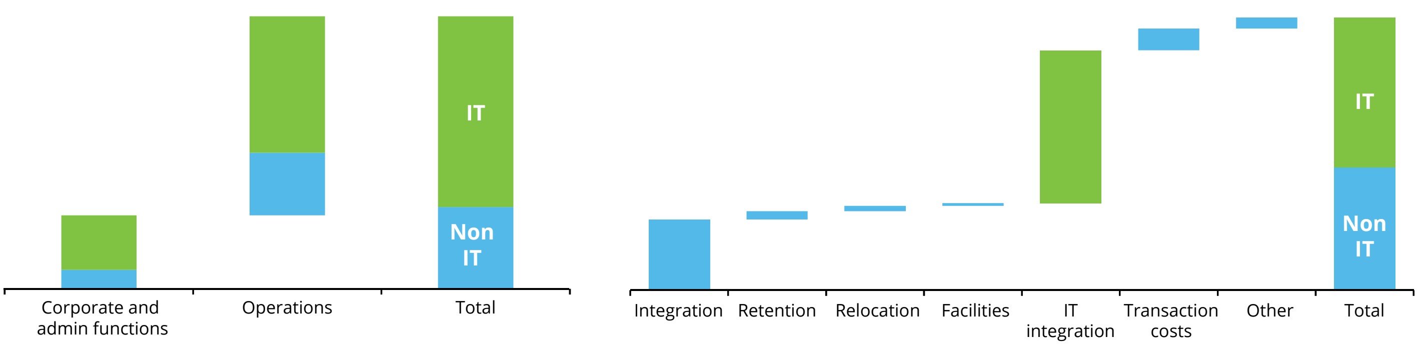
As M&A activity continues to define the health care industry, many stakeholders from across organizations come together to determine a health care system's path during the planning stages of a merger or acquisition. For many, IT considerations can be an afterthought. However, if IT integration is not a major emphasis before planning begins, it may already be too late, and the integration of health care systems can be at risk of not meeting its full expected potential. For example, if two organizations expect to interface their systems rather than consolidate, consideration needs to be given to the timeline, complexity, and data mapping challenges that will need to be addressed. Analysis of prior mergers demonstrates that failed IT integration can result in lower than expected synergies and higher costs.[2]

IT is typically the largest investment cost in the broader integration of health care systems, and it also accounts for roughly seventy percent of all synergies in the process. It is considered the principal driver of M&A benefits and is thus a crucial element of every integration. Therefore, it is imperative that the core IT integration strategy is well-planned and well-executed from the very first day of the proposed merger or acquisition. A merger with such an IT strategy will ultimately position the future organization favorably to battle rising costs and a continuously changing industry landscape.

Figure 1: Importance of IT in M&A deals

IT is the #1 driver of benefits, accounting for roughly 70% of all synergies

IT is typically the largest investment cost to achieve



Source: Deloitte Consulting analysis of over 30 prior merger of equal transactions

Developing the IT strategy

When there is a failure to consider IT in the earliest planning stages of M&A, the result is that once transactions are executed, IT may not be able to deliver on the vision set forth by organizational leadership. Taking on the monumental task of merging two organizations' systems, or integrating multiple operations in another's enterprise, add additional layers of potential hazards in regard to IT complexity. This challenge, sizeable under ordinary conditions, is greatly exacerbated by M&A activity. The anxiety and uncertainty that often occurs can have a detrimental impact on the ability to retain critical IT experts required to efficiently navigate the complexities of merging the two organizations. IT should carefully evaluate people, process, technology, and delivery across both source and target organizations based on the priorities and objectives of the M&A activity.

Health care industry M&A in particular tends to have a number of complex IT systems and interfaces that require significant proactive planning to ensure success and reduce any disruptions in patient care. Therefore, it is critically important to involve IT leadership in the early planning and strategy development of all health care provider M&A deals.

An extensive pre-deal IT due diligence plan is an important first step in starting the conversation with IT and its impact to both entities involved in the deal. Some key initial questions that a leadership team must answer in the early planning stages include:

- What is required from IT to deliver on the overall vision of the deal?
- What IT infrastructure currently exists between organizations and is there potential for synergies?
- How would the necessary IT enablement be delivered and what team will carry it out?

Answering these questions should manifest into a common understanding of strategic vision across key stakeholders, establish an integrated IT team structure and governance model, and begin to develop a communication plan. Aligning on IT strategy and establishing these governance structures during the early planning stages can lead to more efficient IT due diligence execution.

The next critical stage of early planning for IT M&A can be started during due diligence. Conducting a thorough inventory of all systems and functions served for all organizations involved will set the baseline for defining shared services and interdependencies and identify opportunities to improve the value of the M&A deal. From this complete cross-mapping of all systems and functions, the leadership team can strategically focus on assessing certain opportunities for consolidation, documenting infrastructure support needs, and defining integration requirements for all interfaces and systems. Understanding and defining the portfolio of IT services provided will help to build out a thorough timeline of activities and Transition Service Agreements needed to support performance during the M&A transition. After all activities are identified and documented, establishing a strong IT PMO to develop and track transition, consolidation, and activation plans will help monitor value realization throughout the M&A lifecycle. Laying this groundwork in the early planning stages of IT integration into the overall M&A timeline can position the organization to better estimate budget requirements, timeline expectations and succeed in being able to both adequately define and achieve its core goals of the M&A deal.

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For example, specific strategies in M&A execution will vary depending on these defined goals that the organization sets:

If the goals of the organization are to position for the demand for integrated care and preparedness:
The resultant IT strategy might include a focus on a roadmap to achieve a single core EMR platform and related technology portfolio to support the new organization. Enabling patient-centered care empowers patients to take an active role in their health care plan. "Making that transition to patient-centered care requires systematic changes," a group of physicians and researchers wrote in an op-ed for MedCity News. The industry must "redesign its core processes," and in order to do that, hospital systems need to "embrace digital technology that gives patients more access to their health information and easy access to clinicians."[3]

If the goals are to respond to change in the reimbursement model:
A shift to value-based care model would create a new paradigm in which care is delivered by an entire coordinated care community that shares in the responsibility—and risk—of outcomes and costs, touching almost every part of the health care delivery operations. "The ongoing shift to value-based care has widened the gap between the regulatory demands on providers and the existing capabilities of health IT systems. Informatics experts say access to data is the key to closing that chasm. Despite progress in pushing health systems into the digital age, most health IT systems are still not designed to "support a transition to value-based care," according to a new policy paper released by the American Medical Informatics Association.[4] These strategies will require significant capital investment, planning, and a longer timeline to achieve.

If the goals of the organization are to respond to financial and operational pressure:
The IT strategy might include a focus on governance and processes around application rationalization. Establishing a structure defining how your organization will align the IT strategy with the business strategy will help your company achieve strategies and goals, as well as implementing leading practices to measure IT's performance. This alignment:

- Drives efficiency and reduction in cost of supporting and connecting systems
- Drives more consistent workflows across the newly formed organization as systems strategies are standardized and variations reduced

This will entail an agile IT department and significant investment in the upfront infrastructure to execute the rationalization.

If the goals of the organization are competition for expanded markets and services:
The IT strategy might include a focus on integration of existing systems with less rationalization. The integration would enable rapid realization of new markets and capabilities with a shorter IT implementation timeline. Confirm IT has processes designed to drive maximum business value from IT, such as developing a process to ensure that certain functions are accelerated when the value proposition is growing, and eliminating functions when the value decreases. Look to manage resources more effectively by organizing your staff more efficiently; categorizing resources by skills instead of by line of business. This will require a large investment in integration between systems – interfaces, extracts, reconciliation processes, etc.

These are just some of the considerations for developing IT strategy based on some of the more common examples of provider M&A goals. Since every organization is different, it is important to tactically tailor IT strategies to better meet the defined M&A objectives and drive towards successful outcomes.

The path forward: Executing on the IT strategy

Execution can reduce IT costs and risk
As previously outlined, during the course of due diligence it is imperative to keep IT strategy on the mind of the transaction teams. IT systems, personnel transition, and facilities consolidation typically account for fifty percent of all integration-related costs. The emphasis on and importance of IT systems should be no different during the execution of any post-merger integration strategy.

Execution focused on outcomes
Key business drivers and value opportunities are usually further defined during the due diligence process. Value drivers and opportunities should be prioritized based on their estimated value and ease of implementation. Value drivers should be translated into distinct, actionable, and measurable opportunities to inform integration planning and establish integration guardrails and guidance.

IT governance is a critical success factor in M&A execution
Building and maintaining an Integration Management Office (IMO) is an ideal way to maintain an IT strategy throughout the M&A cycle. The goal of the IMO is to provide a structure and consistent method for the collection and dissemination of information; establishing program governance, infrastructure and milestones. The IMO will include sponsors from each side of the M&A activity (i.e. acquiring and acquired companies) and be composed of multiple work streams, including IT. Joint ownership of the M&A model and synergy targets across transaction and integration teams will align incentives throughout the deal lifecycle, drive accountability on both sides, and improve end-to-end visibility.

Bottom line

Remaining competitive in an environment of federal regulations, changed payment incentives, increased demands for efficiency and cost effectiveness, and increased competition will continue to see M&A as a strategic option. Prioritizing IT in early strategy discussions and as part of due diligence, conducting thoughtful planning in developing a go-forward IT strategy, and setting up the roadmap and infrastructure to execute on the IT strategy is one of the most important jobs of organizational executives prior to, during, and immediately after a transaction.

Authors

Bryan Sung
Principal
Deloitte Consulting LLP
Strategy & Operations – Provider Clinical
bsung@deloitte.com

Mary Beth Mikols
Managing Director
Deloitte Consulting LLP
Provider Technology Strategy and Transformation
mmikols@deloitte.com

Chris Harris
Specialist Leader
Deloitte Consulting LLP
Strategy & Operations – Provider Clinical
chriharris@deloitte.com

Sam Vos
Manager
Deloitte Consulting LLP
Technology – Systems Integration
svos@deloitte.com

Acknowledgements

We would also like to thank Adam Panfalone, Ted Dwyer, Mike Kramm, and Sam Wittig who contributed to the preparation of this report.

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