Best Practice Approaches To Mergers & Acquisitions: A How To Guide

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Joseph P. Naughton-Travers, Senior Associate, OPEN MINDS
I. Developing A Merger & Acquisition Plan

II. The Monarch M&A Case Study
   • Peggy Terhune, Ph.D., Chief Executive Officer, Monarch
   • Mike McCrann, Lawyer & Board Member, Monarch
   • Rev. Ben Marsh, Board Member, Monarch & Friends of Club Horizon

III. Questions & Discussion
Developing A Merger & Acquisition Plan
Mergers & Acquisitions On The Rise!

- Health care M&A activity exploded in 2015
  - 14% growth in total health care activity – from 935 transactions in 2014, to 1,498 in 2015
  - 58% growth in behavioral health care – from 24 in 2014, to 38 in 2015
  - 104% in managed care – from 22 in 2014, to 45 in 2015

Consolidation has been seen by many CEOs as a strategy necessary for long-term survival given the changing environment in health and human services – including more value-based reimbursement, more managed care, and decreased funding.
Economies Of Scale

- The phenomenon that production becomes more efficient as the number of goods being produced increases.

- Larger organizations have the ability to lower their cost per unit – thanks to the ability to spread their overhead expenses over a larger number of units.

- Size doesn’t matter without strategy - there are many models that can achieve economies of scale, but your path to collaboration needs to be part of an overall long-term sustainability strategy.

“There is nothing so useless as doing efficiently that which should not be done at all.”

– Peter Drucker
Market Drivers Of Consolidation

What's driving the push for economies of scale?

- Preference for delivery models that focus on the coordination of services for complex consumers
  - ACOs and medical homes – “new carve-out” is by consumer type
  - Challenge for specialists and acute care facilities
- Reimbursement models focused on value-based payment methodologies
  - Pay-for-performance and risk-based contracting
  - New infrastructure needed
  - Increased financial risk requires finance reserves
  - Ability to cover more consumer services and wider geographic area
- Use of competitive bidding and selective contracting
  - The cost of competition
  - “Narrow networks”
- Consolidation among health plans and health care systems creates new competitive pressures in the rest of the health and human services market
Consolidation As A Strategic Issue

Doing more of a service that is losing money won’t necessarily make it profitable.

- Being big in this instance is only useful if it’s part of a strategy to reduce service cost or gain market clout to raise pricing. If the size doesn’t come with enough economies of scale to reduce the effective cost of service, the strategy won’t work.

Adding services and programs unrelated to your mission could result in more problems for marketing and management.

- Being big can’t only be about a number. Some organizations in the field are big but not sustainable because they are diversifying without a strategic plan.

Increasing size may negatively impact the ability to innovate or adapt.

- Being big has a disadvantage – big is rarely nimble. Larger organizations can be slow to change course, and in a market filled with policy changes, technology innovations, and shifting payment and service delivery models – the ability to adapt is a necessity.
Size Alone Is Not A Solution

Larger organizations can spread the “overhead costs” for technology, financing expenses, compliance, marketing, legal counsel, and other core competencies over a larger revenue base – which in many cases gives them a lower unit cost.

However, not all of the “large” organizations that are a result of these mergers and acquisitions are doing well – either from a service delivery perspective or a financial perspective.
Being Big Isn’t A Strategy

- In maintaining competitive advantage in a changing market, size and scale are just part of the equation.

- A large organization that is unwilling or unable to adapt to a changing marketplace is just as susceptible to failure as a small organization.
Benefits Of A Merger

- Increase financial strength
- Continuation and/or expansion of programs and services
- Integration of services
- Reduced operational costs
- Reduced donor fatigue with fewer organizations asking for money
- The opportunity to rebrand
- Expansion of geographic/demographic reach
- Elimination of a competitor for funding
- Elimination of perceived duplication of services
- Address delivery weaknesses
- Open the door to new ideas and innovation
Risks Of A Merger

1. Negotiations may ultimately fail
2. Merged organizations may prove incompatible, never achieve a successful integration
3. Cost savings may never actually materialize
4. Tensions between leadership and personnel may never subside and eventually will interfere with operations
5. The public, constituents, and donors may have a negative reaction

Top 4 Reasons Why Mergers Fail:

1. A lack of knowledge about how to approach, plan, and implement mergers
2. A lack of funding for due diligence and post-merger integration
3. A failure to find the right partner to merge
4. A tendency to look at mergers reactively, as a way out of financial or leadership problems – instead of proactively, as a growth and positioning strategy
A Formal Acquisition Search Process

1. Review strategic objectives for the provider acquisition.

2. Set required and desired parameters for the provider acquisition (size, profitability, markets, competency, contracts, etc.)

3. Identify acquisition candidates.
A Formal Acquisition Search Process

4. Review provider profiles and select candidates for the due diligence process.

5. Conduct meetings to vet acquisition candidates and make final selection.

6. Conduct due diligence (due diligence checklist, combined market positioning, combined P&L, necessary structural changes, etc.)

7. Implement acquisition and plan on-going combined operations (governance, strategic plan, organizational structure, executive team, financial reporting, operations planning, & marketing planning)
Have You Asked The Important Questions?

- Is your organization looking to acquire or be acquired?
- Does the potential partner organization fit with/support our mission?
- Do I have a strategic reason for this merger or are we growing for growth’s sake?
- Have we addressed the “hot topics” that often prevent a merger from happening?
  - Leadership: Who will be the CEO and key leaders of the merged organization?
  - Name: What organizational names will survive the merger?
  - Board: What will be the composition of the new board(s)?
More Questions

- Have we done our homework on the other organization?
- What will we gain toward the accomplishment of our immediate and long-term goals?
- How will a merger be perceived by the public, our financial supporters, payers, and consumers?
- Can we afford the acquisition or merger? How will it be funded?
- Will the combined organizations have the resources to address the needs of both organizations?
- Is my board fully bought into this and willing to actively participate?
The Monarch Merger & Acquisition Case Study

Peggy Terhune, Ph.D., Chief Executive Officer, Monarch
Mike McCrann, Lawyer & Board Member, Monarch
Rev. Ben Marsh, Board Member, Monarch & Friends of Club Horizon
Mergers and Acquisitions

Peggy Terhune, Ph.D., President and CEO
Michael McCrann, Lawyer and Board member
Rev. Ben Marsh, Pastor and Board member
Monarch fast facts today

- Corporate offices located in Albemarle, NC
- Not for profit
- Provide services state wide
- 1800+ staff
- Budget of $85+ million
- Contract with
  - seven managed care companies
  - Various insurance companies
  - State and local governments
What else?

- Provide services statewide.
- Served over 32,000 people last year who have intellectual/developmental disabilities, mental illness, and substance abuse issues.
- Serve children and adults
- CQL Accredited
- Working on Joint Commission Accreditation
Monarch Mental Health Service Locations

Monarch Service Locator Map
Mental Health

- Mental Health Homes: Anson, Beaufort, Cabarrus, Craven, Lee, Pitt, Richmond, Rutherford, Stanly, Union
- Mental Health Apartments: Beaufort, Carteret, Mecklenburg, Rutherford
- Outpatient Clinics: Cleveland, Columbus, Davidson, Gaston, Guilford, Lincoln, Mecklenburg, Nash, Robeson, Rowan, Scotland, Stanly, Wake, Wilson
- Open Access Clinics: Cleveland, Columbus, Davidson, Gaston, Guilford, Lincoln, Mecklenburg, Nash, Robeson, Scotland, Stanly, Wake, Wilson
- Intensive In-Home Services (IIHS): Cabarrus, Cleveland, Davidson, Gaston, Guilford, Lincoln, Mecklenburg, Moore, Rowan, Stanly, Union
- Community Support Team (CST): Cabarrus, Cleveland, Davidson, Gaston, Guilford, Lincoln, Mecklenburg, Moore, Rowan, Stanly, Union
- Assertive Community Treatment Team (ACTT): Cabarrus, Cleveland, Davidson, Gaston, Guilford, Lincoln, Mecklenburg, Rowan, Stanly, Union
- Mobile Crisis Units: Cabarrus, Cleveland, Davidson, Gaston, Guilford, Lincoln, Mecklenburg, Rowan, Stanly, Union
- Administrative Office/Regional Office: Cabarrus, Forsyth, Pitt, Richmond, Stanly

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Map showing the locations of Monarch Mental Health service sites across North Carolina, with specific locations marked for each category of service.
Behavioral Health Services

Assertive Community Treatment Team (ACTT) (Adults only)
Open Access for First Assessment
Outpatient Therapy (Individual Support and Counseling)
Hospital Discharge & Transition Services / Assertive Engagement
Group Counseling
Parenting Classes/Services for any person
Family Counseling
Substance Abuse Assessment, Treatment, and Counseling
Psychiatric/Medication Evaluation and Management (Telemedicine)
DVI Services
Community Support Team (Adults only)
Transitional Care Team (Guilford County)
Peer Support (Adults only)

Intensive In Home (Children only)
Psychosocial Rehabilitation (PSR - Adults only)
Clubhouse International Model (Monarch’s Club Horizon - PSR)
Crisis Assessment Services
Facility-Based Crisis / Non-Hospital Medical Detox (Adults only)
Mobile Crisis Services (Children and Adults)
Psychological Evaluation and Treatment
Play Therapy
Employment and Day Services (MH and I/DD)

- Compensatory education
- Day Supports
- Developmental Therapy
- ADVP (Adult Day Vocational Program)
- Supported Employment
- Waiver Innovations Vocational Supports
- Waiver Innovations community supports
- Personal Assistance
- Community Transition
- Vocational Evaluation (community and site based)
- Community Based Assessments
- Situational Assessments
- Vocational Training
- Supported Employment
- Long-term vocational supports
- Waiver supports (CAP/Innovations)
- Work adjustment
- Micro-enterprise
- Mobile Work Crews
- Enclaves
Residential and Community Services (MH and I/DD)

- ICF (Intermediate Care Facilities) for children and adults
- Supported Living
- Supervised living
- Group Homes
- Apartment Complexes
- Respite
- Supports for people who live in their own homes
- AFL (Alternative Family Living)
- Services in the Community

- Services in Your Home
- Community Inclusion
- Family Support
- Crisis Services and Counseling
- Volunteer Opportunities
- Community Support
- Family Support
- Advocacy
- Information and Referral
- Self advocacy groups
- Family/Caregiver Training
Services provided 1995

- Group homes (5)
- Intermediate Care Facilities (4)
- Developmental Day Program
- Sheltered Workshop
What Happened?

Area Authorities → Local Management Entities
• Three different proposals
  – Rutherford/Polk Counties
    • 4 I/DD homes, 1 I/DD Apartment
    • 2 MH homes, 1 MH apartment
  – Rockingham Board
    • 1 ICF, 3 I/DD Group Homes
  – Winston Salem
    • 3 Sheltered workshops, 2 ICFs, 3 Family Care Homes
The process

- Tour properties
- Submit response to RFP (5 copies in paper, each 4 inches thick).
- Respond to questions
- Come for interview with funder
- Interview with families
- Choice made
- Date to start services
What we offered to staff

• Everyone to be hired unless
  – Criminal background check
  – Drug test
  – Unable to verify education
• Seniority based on current employment
• Same salary or better
• No wait for health insurance
• Retirement based on seniority with current company
• Keep the senior managers
What we offered to families

- Legal, ethical, and transparent
- Answered ALL questions
- Family involvement in many ways
- Clear communication channels (handed out my business card!)
- Open to alternative ways of thinking about things
- Best (or evidence based) practice
- Try to keep their existing staff
Managed Care

- LME ➔ MCO
- Quality drove the system
- Companies started to fail
- Do we want to help?
Group Homes/Voc programs

- Rutherford/Polk (6 res)
- CenterPoint (3 day, 3 res)
- Community Based Alternatives (3 res)
- Sandhills (9 sites)
- Mainstream (1 res)
- PBH sites (3)
- Davidson closing two companies (12)
- Neuse/Onslow Carteret/ECBH
- Beacon Center (5 res)
- Smokey/private company (2)
- Southeastern Regional (4 day)
- Albemarle (5 day)

Behavioral Health

- Caring Support
- Dare (1 day)
- MHA
- Private Group Home Company (6)
- Mecklenburg Open Door
- Tru Behavioral
- Johnston county agency
- Guardianship agency
- Johnston County Apartments
- People helping people
- Club Horizon
- Pinetree

Who did we acquire?
Challenges and Lessons Learned

• Due Diligence and the decision
  – Lack of information for due diligence
  – Values
  – Does the board have to be involved?
  – Should there be a contract, and if so, what should it say?
  – How do we ensure no liability for paybacks or staff claims?
  – What about the company’s assets, especially if the company is a for profit?
  – What about the other company’s governance and leadership?
• Created a checklist with Formalities, finances, marketing, operations, personnel, technology, physical plant, clinical and licensure
• Met with leadership to complete checklist
  – How do we integrate board members?
  – How fast can we do this?
  – What can we really promise?
  – Transferring EHR data?
  – Keeping our promises while becoming fiscally sound
### Checklist Example: Formalities

<table>
<thead>
<tr>
<th>TASK TO BE COMPLETED</th>
<th>RESPONSIBLE</th>
<th>TARGET</th>
<th>COMPLETION</th>
<th>COMMENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Identify contact person to mail bills to as they come into LME/agency after transfer date</td>
<td></td>
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<tr>
<td>Identify contact at LME/agency to mail correspondence to</td>
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<tr>
<td>Notify Arc Housing/HUD of changes and identify what needs to be completed for records</td>
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<tr>
<td>directions, staff names, fax #, names of those served, guardians/caregiver names &amp; addresses,</td>
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<tr>
<td>Meet with key LME/agency staff introductions, discuss set up transfer</td>
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<tr>
<td>up transfer, educate about agency, consumer rights, share transition plan, gather feedback and</td>
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<tr>
<td>Meet with staff discuss start up transfer, educate about agency, employment, share transition plan, gather feedback and suggestions</td>
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<tr>
<td>Provide immediate access to P/R manuals</td>
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## Checklist Example: Finances

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<tr>
<th>A</th>
<th>B</th>
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<tbody>
<tr>
<td></td>
<td>TASK TO BE COMPLETED</td>
<td>RESPONSIBLE PERSON</td>
<td>TARGET DATE</td>
<td>COMPLETION DATE</td>
<td>COMMENTS</td>
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<td>4</td>
<td>Inventory all capital supplies in programs and send list of them to Finance (over 500.00)</td>
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<td>5</td>
<td>Make a listing of all purchasing accounts under LME/agency and change to Monarch</td>
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<td>6</td>
<td>Transfer vehicle titles</td>
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<td>7</td>
<td>Notify Arc Housing of changes and identify what needs to be completed for their records</td>
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<tr>
<td>8</td>
<td>Set up account/department numbers in BB/ADP</td>
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<td>9</td>
<td>Assess payroll schedule; determine how first check to be done</td>
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<td>10</td>
<td>Pre-note bank account for direct deposit</td>
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<tr>
<td>11</td>
<td>Determine process and deadlines for timesheet submission</td>
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<td>12</td>
<td>Negotiate contracts w/LME</td>
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<td>13</td>
<td>Train staff in methods of communication with central office, use of forms, etc.</td>
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Once it’s started...

- But you’re a better company!
- Leadership sometimes is the problem
- It’s not fun to fire the previous owner of the company
- Changing perception and values
- Sabotage (Pence and Bellemeaden)
- Changing the culture
- Sheer numbers and paperwork
- Expense of fixing what we found
• Mike’s past experience with Pinetree
• His challenge at the “introduction” meeting with families
• His initial comfort on the board
• Using his questioning to make us better
• The view he has now about Pinetree and Monarch – was it the right thing to do?
• What is the board’s role in these types of situations?
Monarch’s Club Horizon

Merge or Die

Ben Marsh, Monarch Board Member
Club Horizon’s Story

- Single location non-profit Clubhouse est. 2004
- Located in rural suburb of Raleigh, NC (Wake Co.)
- $300-500k budget funded by Medicaid UCR funding
- Only clubhouse/PSR in Wake County, NC

- Mission-driven: To increase community acceptance and improve the quality of life for adults with serious mental illness by facilitating meaningful work, education, housing, and social opportunities
• Ben’s Story…The Old Man said: Merge or Die
Why Monarch

Service Sites
• 18 Outpatient Offices
• 183 Residential and Day Program Sites

Annual Budget
• $100 million

Patients
• Over 32,000

Staff
• over 1,800
Why Monarch

• IDD and MH with broad spectrum service in North Carolina
• Mission-centered:
  – Monarch is committed to supporting, educating, and empowering people with developmental and intellectual disabilities, mental illness, and substance abuse issues to choose and achieve what is important to them.
• Values-driven:
  – Dignity, respect, person-centered, safety, options, accountability, innovation, listen carefully; integrity; willingness to change; all staff committed
Mission Alignment

- Meetings between Monarch staff and Club Horizon Board
- Commitment to Club Horizon regardless of financial viability
- Signed contract to return Club Horizon to independence if needed
- Club Horizon Board re-branded to Friends of Club Horizon, allowed to keep $100K of seed funds for fundraising activities
- Two Club Horizon Board members joined Monarch’s Board
- All staff retained from Club Horizon – significant investment in training and professional growth
Questions & Discussion
Turning market intelligence into business advantage

OPEN MINDS market intelligence and technical assistance helps over 140,000 mental health executives tackle business challenges and maximize organizational profitability.

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