

What's Your Post-Merger Financial Outlook? Why a Pre-Merger Gut Check Is Critical

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One of the most important considerations in finalizing a healthcare merger is how well the consolidated entity will perform, financially, after the deal is complete.

Many times, leaders get so caught up in the blocking-and-tackling of due diligence—a time-consuming exercise that protects their organization from material risk—that their ability to see past the point of deal signing becomes limited. Certainly, due diligence is crucial: When executed effectively, due diligence protects the transacting parties from material risk and can even optimize post-transaction benefits.

But developing a robust understanding of the financial implications of the merger on the newly consolidated entity can, to an extent, be even more important than due diligence. Indeed, for boards, it is their fiduciary duty to understand the comprehensive impact of a transaction before they move forward with a deal.

Sometimes, the pressure to complete the deal can interfere with the need to make sure the relationship is being pursued for the right reasons.

Ideally, at least a high-level pro forma is developed before entering into a letter of intent or undertaking more robust due diligence, so that leadership and board members understand the potential impact of a transaction or investment before going too far down the road toward execution. For many— but not all—organizations, the point at which such projections are calculated varies. There are even instances where a hospital or health system board has filed a merger application with the state without requesting this type of analysis.

While leaders cannot legally analyze all elements of the potential impact of a merger, such as the impact commercial reimbursement rates, they can engage with a third party to assist, including conducting a *"black box" analysis of potential reimbursement impact*. Such an analysis can assist boards and leaders in projecting—in a legally appropriate way—this potential revenue impact of the transaction. Similar analyses can be conducted around key expense areas, including benefits costs and vendor contracts.



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While it's critical to have a high-level understanding of the financial impact of the transaction before entering into a letter of intent or exclusivity agreement and initiating robust diligence, an ideal time for further, more nuanced post-transaction financial planning is during due diligence. This enables teams to incorporate due diligence findings and other strategic and operational considerations into prospective estimates. For leaders, four key actions during this process stand out:

- **Quantify risks identified during due diligence—and understand the future implications.** Will key deal terms need to be revisited given the prospective financial picture?
- **Test the impact of capital commitments.** Here, a *fairness opinion*—which assesses the reasonableness of the price for both parties and the terms of the transaction, including capital commitments—is essential. It will help, even force, leaders to determine: Are the areas of proposed investment appropriate, or should they be revisited?
- **Work with counterparts to identify post-transaction areas of opportunity.** This linear evaluation sets the foundation for realistic, tangible opportunities to be included in the prospective financials. While most synergies are not realized in the first year, there should be a list of low-hanging fruit opportunities that can be implemented in the first three to six months after the deal closes.
- **Pressure-test your assumptions.** This information will prepare the organization to manage risk and uncertainty more effectively.

By conducting a pre-merger financial gut check, leaders can enter the merger with realistic expectations and more effectively plan for the future of the new entity.●