MERGERS AND ACQUISTIONS:

Integrating Total Rewards Strategies to Drive Value

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INTRODUCTION

As health care continues to evolve at a rapid pace, many organizations are exploring opportunities to expand and scale their operations to support long-term growth. One of these strategies includes pursuing mergers and acquisitions (M&A) - a practice that began to gain momentum again near the end of 2022 following a two-year slowdown in the wake of the COVID-19 pandemic. According to Kaufman Hall's Hospital and Health System M&A in Review report, this momentum continued through 2023 with 65 announced transactions - a 10% increase from 2022. Sixteen of the 65 transactions were reported near the end of 2023.

Two primary factors have contributed to this growth in M&A activity. Foremost, there has been an increase in the number of financially distressed organizations seeking partnerships. Transactions involving these circumstances, including smaller hospitals and health care systems, rose from 15% in 2022 to 28% in 2023. Due to financial hardship, many seek to secure partners to help ensure financial sustainability and maintain access to care delivery within their community.

Reorganization in regional markets, with the realignment of both for-profit and not-for-profit health system portfolios, also contributes to the rise in M&A activity. Many organizations consider this is critical to expanding into complementary capabilities and delivering more coordinated care across a broader market.

TOTAL REWARDS: ADDRESSING COMMON INTEGRATION CHALLENGES

An essential key to success while undergoing a merger or acquiring another organization is addressing financial and operational goals and making the transition as smooth as possible for employees.

This includes the alignment of total rewards strategies – which requires critical input and information from the Chief Human Resources Officer and the Human Resources function that may influence critical decisions, timing, milestones, and integration approaches to mitigate human capital risks during implementation.

This article focuses on common total rewards challenges that many health care organizations encounter during an M&A transaction. Recognizing and addressing these opportunities early will help minimize potential risks and deal-breakers, prioritize pre- and post-merger activities, and support a successful implementation process.

- **Inefficient Workforce Structure**
  Assessing your current workforce structure to ensure an efficient mix of management and staff to streamline performance and manage costs is critical for the integration process. The question of centralization vs. decentralization remains the key focus for the M&A process. A recent workforce survey from SullivanCotter showed that, for most support functions, centralization is a more efficient staffing model than either decentralized or hybrid structures.

- **Misalignment of total rewards philosophy**
  Establishing a consistent total rewards philosophy should be the foundational element that governs the new organization's pay strategy. Differing approaches between the two merging organizations on essential program elements such as market pay positioning, targeted market comparators, incentive opportunities, benefits programs, and more will lead to inconsistent rewards and pay practices. While harmonization and consistency are critical, it is also an opportunity for the new organization to reevaluate and differentiate the philosophy where appropriate. Many health care organizations have recently recognized the need to differentiate certain reward programs and practices by their specific workforce segment. As an example, SullivanCotter's 2022 Nursing Compensation Pulse Survey reports that staff nurses are more likely to have their pay philosophy set higher than the market 50th percentile (median) as 32% of organizations target the 60th or 65th percentile and 26% of organizations target the 75th percentile. This is due to unprecedented nursing labor shortages, pressure to remain competitive with the unionized workforce, and the prioritization of recruitment and retention goals.

- **Outdated and/or uncompetitive legacy pay structures**
  M&A often present an opportunity to update the total rewards philosophy. Organizations can streamline pay structures to address internal pay equity issues and ensure market alignment. This is becoming even more critical as organizations continue to source talent outside the traditional health care market.

- **Inconsistent pay practices and program administration**
  While ensuring consistent and equitable pay practices across the new organization is essential, organizations must first identify the most significant differences and determine the level of harmonization required. Programs and practices such as supplemental pay, premium pay, and incentives/bonuses often require the most reconciliation between two merging organizations. The annual compensation planning process – including pay increases and promotions – also tends to vary. Organizations can prepare for post-close integration by conducting program and practice audits before the deal closes.

- **Conflicting and costly benefit offerings**
  During the M&A process, integrating benefit programs and policies is vital to ensuring a cost-effective and seamless transition that will deliver positive outcomes for the organization and its employees. A comprehensive due diligence process followed by a clearly defined integration strategy aligned with the overall goal of the transaction can reduce duplicative costs and create a more attractive total rewards package.

- **Lack of a cohesive and well-defined career architecture**
  Addressing workforce structure, compensation and benefits programs is only half of the battle. As organizations come together, a comprehensive career architecture that optimizes the new organization's structure and helps to identify redundancies will drive the M&A integration process. It will also ensure consistent job titling and leveling, enable better workforce reporting and analysis, and provide leaders with clear guidelines for promotion. High-performing companies continuously examine and restructure the overall career framework to promote talent mobility, enhance learning opportunities, and improve employee engagement and retention.

- **The need for greater transparency**
  M&A is a complex business strategy that requires clear lines of communication and a high level of transparency. Despite the confidential nature of these transactions, effective communication and change management strategies are imperative to help build trust and confidence across merging entities and support employee productivity and morale. Whether combined with an overarching plan or one focused exclusively on total rewards, an ideal communications strategy allows for several 'touchpoints' throughout the process. Leaders, managers, and employees must be earnestly included in the transition and implementation journey to understand how the new organization will positively impact the employee rewards experience.

KEY TAKEAWAYS

It's important to note that only some M&A transactions are successful – many struggle to achieve the strategic goals and operational efficiencies originally envisioned within the timeframe established. While effective integration of an organization's total rewards strategy does not define a transaction's overall success or failure, it is a critical contributing factor. Organizations should look to complete this integration in a timely manner and with as much compassion and transparency as possible.

Although these considerations are relevant during any stage of an actual transaction, they also pose important planning questions for organizations that are contemplating but have yet to pursue any M&A opportunities. Given the current environment – with a strong emphasis on cost containment, operational efficiency, and employee retention and engagement – organizations not currently considering any partnerships can benefit from a more holistic and continuous assessment of these foundational aspects to help ensure consistency and market competitiveness.