ACA in an M&A Environment:

How Changes Will Impact Your Employee Benefits

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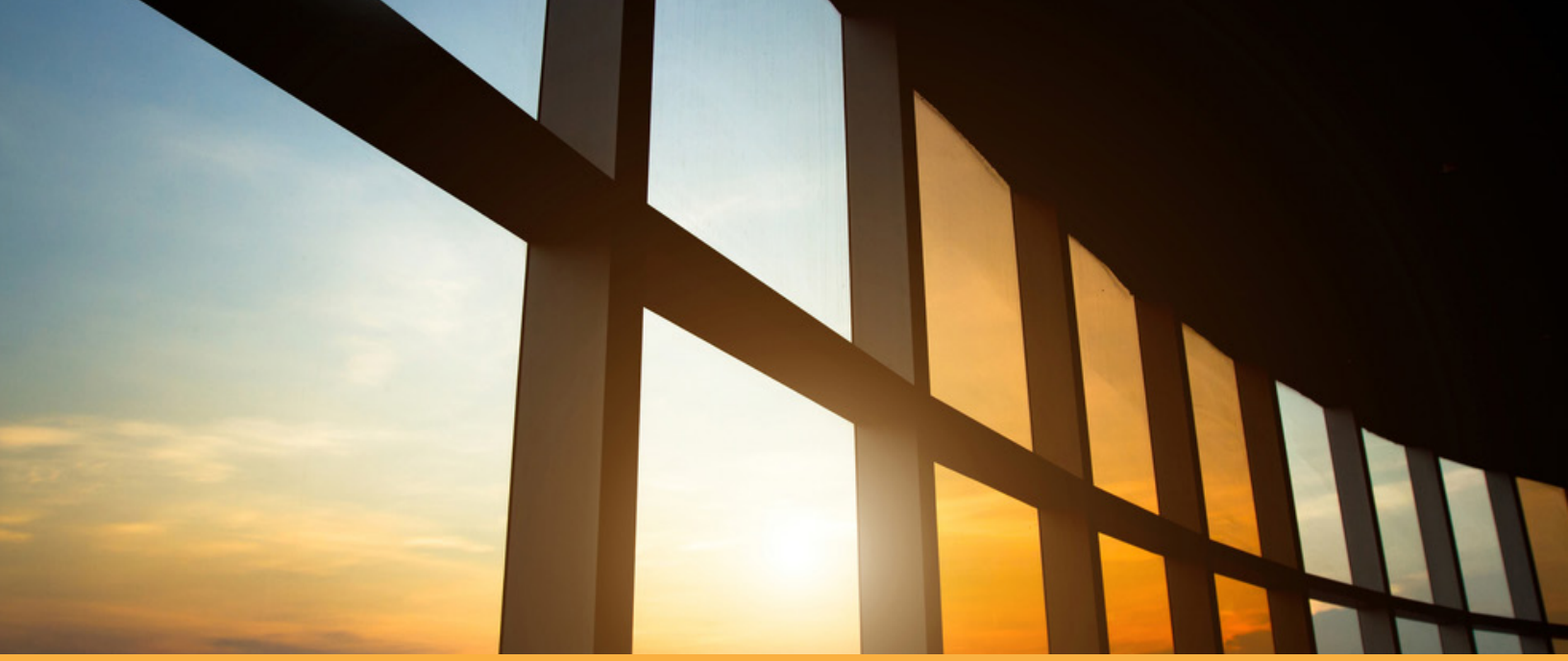

PREFACE

With the recent elections and changes in Congress, the future of the Affordable Care Act has been a contentious subject. The content in this lite paper is current as of this edition, and we will update it if warranted. As of this publishing, the ACA is in place and the information in this document regarding compliance requirements is still valid. If you have questions about how the current requirements may affect your business or potential merger and acquisition, contact your Clark Schaefer Hackett advisor.

"The broad goal of the ACA was to offer affordable healthcare to every American."

INTRODUCTION

As the Patient Protection and Affordable Care Act continues to evolve and integrate itself into today's healthcare landscape, growing businesses could soon find themselves in a complicated situation with regard to employee benefits. If a merger or acquisition is on the horizon for your organization, the final product could alter how you are viewed under the lens of the ACA. Your newly defined venture will now have to reevaluate employee benefits as a whole to ensure coverage is a constant.

This paper will outline the current relationship between the ACA and employee benefits, detailing how a merger could affect your organization and what you can do to balance your combined structure with healthcare insurance requirements.

KEY CHANGES WITH THE ACA

Love it or hate it, the ACA has flipped healthcare in the U.S. on its head. Signed into law in 2010, with some major provisions going into effect at the start of 2014, the broad goal was to create a system that would offer affordable healthcare to every American. Its implementation was rocky, and the rancor experienced in Congress during the debate phase was well documented. Regardless, the bill made it through, and now marketplaces are established with the goal toward an ACA-compliant healthcare plan.

The ACA also carried with it several key changes that affected how employers offered healthcare coverage to their staff members. Depending on the number of employees, you may have a responsibility to notify them of the affordable marketplaces or provide each with an ACA-compliant plan. Naturally, this can create complications should a merger be in the works for you: Combining your firm – with fewer than 50 employees – with another firm that puts you over that threshold will immediately require changes to your employee benefits to ensure healthcare rules and regulations are met.

"For firms with fewer than 50 employees, only 52% offered healthcare coverage."

HEALTH PREMIUMS CONTINUE TO INCREASE

The ACA's implementation got off to a rocky start. Lawmakers, business owners and employees are debating the pros and cons of healthcare reform, but not up for discussion is the fact that organizations across the country have been affected by this change.

One doesn't have to look much farther than the surge in health premiums experienced in 2014. A recent survey conducted by The Henry J. Kaiser Family Foundation reported a 3 percent uptick compared to 2013 for employer-sponsored plans only. Average annual premiums for employee-sponsored family health coverage hit $16,834 this year. Workers contributed slightly less than $5,000 to the yearly cost of family coverage.

Since the number of employees per business is so important under the ACA, the Kaiser survey looked at the impact this reform will have based on size of workforce. For firms with fewer than 50 employees, only 52 percent offered healthcare coverage. Out of all those surveyed, only 26 percent of workers took part in a plan that would be "grandfathered" in under the ACA. The survey also found that costs were the greatest reason why employers skipped healthcare benefits for staff members.

HEALTHCARE BENEFITS REMAIN QUESTION MARK

Offering healthcare benefits is still up in the air for many employers. The 2014 Small Business Healthcare Study, conducted by the National Small Business Association, dove deeper into future plans given the current ACA climate.

Polling a number of employers, findings showed that 30 percent of all employers don't offer healthcare benefits at the moment. A substantial 67 percent don't plan on changing course over the coming year, either, while 22 percent are not sure. That leaves only 11 percent of employers who want to begin offering benefits soon.

"If you have 50 employees or more, you are legally required to provide each person ACA-compliant healthcare coverage."

The reason why those 11 percent are planning on creating an employee benefits plan? Expectations. The survey noted that 33 percent of employers out of this segment believe their workers will expect benefits, while 20 percent feel that the ACA will lead to cost savings.

Overall, the ACA has changed how businesses approach employee benefits, but employers still have questions about the impact healthcare reform will have on their organizations.

WHAT DOES THIS MEAN FOR EMPLOYERS?

One of the main goals for the ACA is to insure every American living in the U.S. Due to the passage of this legislation, more Americans are either insured or have the ability to acquire an insurance policy. Some progress is related to employers reevaluating their employee benefits and providing coverage to their staff members. As these changes continue to integrate into the U.S. healthcare landscape, more developments could be on the horizon for employers.

This is especially true should a merger or acquisition be in the works for your organization. The ACA comes with that one critical mandate for employers: If you have 50 employees or more, you are legally required to provide each person ACA-compliant healthcare coverage. If you have more than 100 employees with average annual wages over $250,000, then you are required to provide coverage for at least 70 percent of your full-time staff in 2015, with that percentage increasing to 95 percent by 2016.

So think about the scenario where you are a small employer with fewer than 35 full-time employees, merging with a similar-sized firm with 30 employees. You will then have a total of 65 workers – and now you are required to provide coverage to each of them. This could drastically alter how you structure your employee benefits, and as the push for fewer uninsured Americans continues, you will quickly have to address this scenario.

"M&A deal activity has been the strongest in the commercial, technology, and consumer services and retail trade sectors, among others."

ACA GIVES SECOND THOUGHT TO MERGER

In some cases, employers are being proactive about the impact the ACA will have on their upcoming merger or acquisition. So proactive, in fact, that some are drastically changing their approaches, even calling off their deals altogether.

The fact that ACA mandates will require companies to alter how they address employee benefits has caused many to give second thought to the idea of a deal, as evidenced by client feedback noted by Kathi Wright and Monica Kelley, attorneys at Minneapolis-based Gray Plant Mooty. Wright and Kelley told Twin Cities Business magazine that many of their clients are keeping a close eye on healthcare reform.

"We've heard from companies – particularly franchise organizations – that are now much less likely to expand because of the significant increased costs they'd incur becoming a large employer," Kelley told the media outlet.

SLIGHT DECLINE FOR MONTH-OVER-MONTH M&A ACTIVITY

While the ACA has caused some employers to think twice about a merger, overall activity in this market has declined slightly. Based off of information compiled by financial research and investment analytics tools firm FactSet, M&A deal activity has been the strongest in the commercial services, technology services, consumer services and retail trade sectors, among others.

However, in September 2014, the amount of activity in the U.S. dropped 20.3 percent compared to August, FactSet reported. Aggregate spending for M&A activity also decreased during that time period. While there were several hundred deals worth more than $1 billion during the 12 months ended August 31, 2014, the most transactions were completed on the other end of the spectrum.

For example, there were 726 deals finalized during that time worth less than $10 million, the most out of any deal size other than those that didn't disclose a monetary value. While this data illustrates the current popularity of mergers and acquisitions, the overall trend is a downward one. FactSet noted that for these deals, there were 813 in 2013, which is good for a yearly decrease of 10.7 percent.

"Given the current relationship between the M&A environment and the ACA, you must determine the health of each employee benefit plan."

WILL YOU CROSS THE THRESHOLD?

If a merger is in the works for your company, you need to understand how to prepare your business for employee benefit changes after the deal is complete. One of the preliminary questions you should be asking is whether or not the deal will put you over that 50-employee threshold. If the answer is yes, now is the time to address due diligence.

First on your to-do list must be a close inspection of the existing structure of your company. Ask yourself several important questions, including:

- **Who comprises my workforce?** If your employee base is full-time, seasonal or part-time, it will affect the benefits you offer following the deal.
- **What are my existing benefits?** Determine what type of plan you currently have, including whether or not you have staff members that are fully insured, self-insured or uninsured.
- **Who is currently covered?** Once you take note of your existing benefits, you next need to identify who in your company is currently covered. Those who aren't will see their insurance change following your merger.

These are crucial questions to ask of your own company, but remember early on that your own company is but one part of the equation. Your partner in the deal also comes into play, so ask these same questions while analyzing its workforce. Then, repeat while looking at a merged final product. This will ensure comprehensive due diligence during this preliminary stage.

ARE YOUR FINANCES IN ORDER?

Current employees with and without insurance are only one – albeit important – part of due diligence. Another area that you need to analyze prior to merging is financial, both for your company and your partner's firm.

An acquisition is a significant outlay. There will be financial implications along the way, and the earlier you catch problems or errors the better off you'll be. For instance, given the current relationship between the M&A environment and the ACA, you must determine the health of each employee benefit plan. Look for operational errors, compliance issues – such as delinquency or a backlog of fees – or even underfunded plans. Identifying these details among your partner's plan is vital, because you as the acquirer will accept all of these costs post-merger.

"The earlier you consult professionals, the easier time you will have understanding potential pitfalls and creating a viable strategy to avoid problems."

Should you find issues before the merger, do your best to fix these problems before they multiply. One option you have is to place provisions in the language of the purchase agreement to adjust the price, should the condition of the employee benefit plan reduce the value of the target firm. Two small employers can have skewed opinions of the financial health of their companies, so take a step back and look at these elements from an objective perspective.

With that said, four steps you can take when performing due diligence on both companies and your employee benefit plans are:

1. **Resolve all outstanding debt**
2. **Fix compliance errors**
3. **Amend the purchase agreement, if needed**
4. **Consult professionals, including attorneys and advisors**

BRING IN CONSULTANTS PRIOR TO MERGER

This last step is incredibly important. If you are a smaller employer breaching the ACA's 50-employee threshold through your merger, you will become subject to a wide array of new healthcare and benefit plan rules.

The earlier you consult professionals, the easier time you will have understanding potential pitfalls and creating a viable strategy to avoid problems. Your new mix of employees will be drastically different than your current situation, and the best reason to bring in help from an outside source is awareness.

Consultants can advise on unfamiliar topics, in addition to steps you should be taking to streamline the process. The best advisors will come in, look over the deal and say:

"Here's what you may not be aware of that can have a major financial impact later if you don't address it."

"As you prepare for a merger or acquisition, keep in mind culture, in addition to the other elements of the deal, to balance the needs of your organization with the rules and regulations of the ACA and employee benefits."

DEFINE THE FUTURE OF YOUR COMPANY

Employee benefits and finances are but two of the elements that you must take into consideration ahead of your merger. The third is culture – a critical piece of the puzzle that can derail a deal even if every other detail is in order. If you don't account for culture, you are leaving the future of your merged company up to chance.

Addressing the issue of culture can be broken down into several components:

1. ANALYZE EXISTING CULTURES

First, look into the culture of each company – yours and your target's. What are your similarities? Where are your strengths and weaknesses? Predict where culture will clash moving forward, and see if you can make any changes to avoid that from happening. Be mindful of the position the target firm is coming from – in all likelihood, they enjoy their culture, and don't want it to change.

2. IDENTIFY THE KEY ELEMENTS OF EACH CULTURE

Next, you must determine the best parts of each culture. These are the elements that should be fostered following the merger. Make a list and be ready to circulate that with your staff members. Don't be afraid to ask for help, as you may be surprised about how your opinion differs from a fellow colleague.

3. PICK A DESTINATION

Finally, you need to decide how you want the combined culture to look. Using feedback from staff members, as well as the list of strengths and weaknesses, you can make an outline of the ideal destination. Because benefits contribute to workplace culture, you'll want to view your health insurance offerings through that lens.

These four steps apply to every company. As you prepare for a merger or acquisition, keep in mind culture, in addition to the other elements of the deal, to balance the needs of your organization with the rules and regulations of the ACA and employee benefits.

"Adopting a larger plan will remove the need to alter the smaller plan for healthcare reform."

ADJUST YOUR BENEFITS PLANS POST-MERGER

The time has come to address the benefit plans following your merger. You know the nuances of the ACA, you've consulted professionals, you've checked over finances and you've developed a plan for the combined culture – now, you can finally alter the employee benefit plans as you see fit.

The first step is to look over every option you have at this time. It will likely come down to two:

- **Combine the plans or discard the smaller plan**
- **Leave the employee benefits alone**

1. COMBINE THE PLANS OR DISCARD THE SMALLER PLAN

In most cases, this is the path of least resistance during a merger. A smaller plan may or may not be ACA-compliant given the 50-employee threshold, but the larger company's plan most likely is – assuming it already has more than 50 employees. Therefore, adopting this larger plan will remove the need to alter the smaller plan for healthcare reform. Combining the two plans is also one viable option should they be of similar size, with few significant differences.

This strategy is not without its downside, however. Consider the factors that could adversely affect your insured employees in the future, should the plans combine. There could be a shift in benefits or premiums that create friction within your merged company.

A second option you have moving forward following the merger is to eliminate the smaller plan. This will then leave the employees once covered by that plan without insurance, so immediately absorb them into the remaining plan. This can address the similar issue of ACA compliance experienced with the first strategy, but by dissolving the smaller plan it removes the need for any action to fix compliance issues, as long as the remaining plan is in order.

"No matter what, you can't foretell changes to healthcare reform and employee benefits."

2. LEAVE EMPLOYEES BENEFITS ALONE

It is possible you won't need to take any action on benefits post merger. Both plans may be ACA-compliant – even with the new requirements – and the easiest way to cope with the merger might be to leave the employee benefits alone. However, that will leave you with one workforce receiving two different benefits packages.

No matter the strategy you choose, there will be some post-merger integration issues. For example, the ACA requires employers to provide insurance for all workers and their dependents – but not their spouses. This can come into play should any number of your staff members have spouses in foreign countries. They could be using their insurance to cover their significant other, but that might change following your merger. This distinction has a significant impact on the members of your workforce, so your decision on this detail and others like it matters to your employees.

These nuances can directly impact planning. Your goal should be to forecast costs and company problems that could impact employee benefits. Then, you can pick a strategy that makes the most sense. Considering how your employees will react should you change their insurance can help you choose a course of action.

No matter what, you can't guess or foretell changes to healthcare reform and employee benefits. Work with what is available today, and don't put off decisions in the hopes of better conditions down the road.

"At Clark Schaefer Hackell, our dedicated employee benefit plan services group has worked with numerous clients for over 40 years."

LOOK AT THE BIG PICTURE

Given the desire of the Obama administration to bring health insurance to the masses, employers across the country face an evolving environment when it comes to employee benefits. Factor in the drastic changes that accompany mergers and acquisitions, and you have the potential for oversight and errors that can hamper a company's profitability in the future.

Looking at your upcoming deal with employee benefits and the ACA in mind will help you prevent unpleasant surprises. While there is no quick-fix solution here, following these steps and performing your due diligence will keep you informed and proactive. Combine that with the assistance of a trusted advisor, and you have a recipe for success.

At Clark Schaefer Hackett, our dedicated employee benefit plan services group has worked with numerous clients for over 40 years. Many stay with us for more than 20 years, due to our in-depth consulting and administration services that save time and money. While our expertise extends to healthcare benefits, we also focus on 401(k) and 403(b) plans and benefit plan audit services, so you will have comprehensive assistance at all times.

The ongoing evolution of healthcare reform and the fluctuating environment of mergers and acquisitions makes effective employer planning a challenge. However, that does not mean you will not have a compliant and satisfactory employee benefit plan at the end – it just means that you must consider the current landscape of both the ACA and M&A activity and perform adequate due diligence.

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