

Mechanics of a Nonprofit Merger

Written on February 10, 2012 by [Ellis Carter](#)



More and more nonprofits are considering merging or consolidating as a strategy to survive or even grow as government and private sources of funding shrink. Merger proposals are being prompted by reduction of funding sources, the tight economy, the need for succession planning and a desire to consolidate expenses and increase capacity.

Also, many funders prefer to deal with fewer providers of the same programs or services and encourage mergers and other

forms of collaboration to reduce overhead and increase capacity.

2
tweets
retweet

Share

Share

0

There are special challenges for nonprofits considering a merger. Commercial mergers are driven by increasing value to shareholders. Advancing the shareholder's interest is a clear objective that drives the structure of the deal. Conversely, in the case of a nonprofit corporation that has no owners, other factors, such as increased capacity and cost savings, drive the deal. Because these benefits can be more difficult to quantify, a proposed merger can feel threatening to a nonprofit board who feels they may lose power and influence. For this reason, it's important to discuss potential deal breakers such as name, headquarters, board make-up, leadership positions, and continuation of key programs early in the process.

The Mechanics of a Merger

A merger is basically a legal process by which two separate organizations become one organization. A merger requires one corporation (the merging corporation) to merge into another corporation (the surviving corporation). The surviving corporation takes on all of the merging corporation's assets, liabilities and debts and is substituted in place of the merging corporation in any lawsuits. For this reason, many organizations contemplating a merger choose to structure their transaction in a manner that avoids taking on the other corporation's liabilities such as an asset acquisition. Regardless of how the transaction is legally structured, the technical steps are similar and begin with honest and forthright discussions among the leaders.

Discussions among Leadership

The first phase typically begins with discussions between the organizations' leaders. An organization that is looking for a merger will likely spend some time identifying potential merger partners. Then, leadership may engage in discussions with peers at various organizations to assess interest.

Once the parties are committed to moving the discussion forward, it is customary to develop a brief document outlining the objects and key terms that have been discussed, as well as to memorialize mutual promises of confidentiality, agreement on payment of fees and costs, and other key terms that may emerge in the preliminary discussions. This document is typically titled a "Term Sheet," "Letter of Intent," or "Memorandum of Understanding." This document is then approved by each parties' board of directors and signals the seriousness of the parties.

At this stage, many organizations form a joint merger committee comprised of executives and board members of each organization. The joint merger committee can streamline the merger process and help ensure both organizations have an active voice. The joint merger committee also acts as a liaison to the full board.

Some nonprofits find it helpful to engage an experienced merger consultant at this stage to guide them through the merger process, remain focused on the benefits to both organizations, facilitate board discussions, and mediate sensitive issues that may arise.

Merger Agreement

Once the parties have defined the key terms, the lawyers will draft a merger agreement. The merger agreement will set forth the key terms negotiated by the parties including but not limited to the name of the organization, amending governing documents, board make-up, leadership positions, and the continuation of key programs. The merger agreement will also contain representations and warranties and other conditions that must be satisfied to close the transaction. If the transaction is structured differently, a purchase agreement or affiliation agreement may be prepared covering similar concepts.

Due Diligence

Though often over-looked, due diligence is an important step in the merger process as it satisfies the officers' and directors' fiduciary duties to their respective organizations. Due diligence is where an organization conducts a thorough investigation to ensure they understand the business of the other organization. Generally, due diligence puts the onus on the surviving organization to conduct the due diligence investigation. However, the merging organization will sometimes conduct a due diligence investigation to determine if the surviving entity is in the position to carry on the merging organization's vision and programs. Typically categories of information investigated in the due diligence process include corporate structure and records, contracts, finances/debts, existing or threatened lawsuits, intellectual property, employment matters and compensation arrangements.

Approvals

A vote of an organization's board of directors may not be the only approval required to enter into a merger transaction. Consents and approvals of members (if the nonprofit is a member organization), third parties or government may be required as well. Consents or approvals may be required for the transaction itself or to transfer an agreement at the closing of the merger. For example, many lease agreements require landlord approval before the lease agreement can be assigned. On the other hand, a master service agreement or grant may require prior consent to the merger transaction itself. A list of required approvals and consents must be developed through the due diligence process and any required approvals must be obtained or waived prior to closing.

Closing the Transaction

The parties are ready to close the transaction when the parties have finalized a merger agreement, conducted the due diligence investigation (and are satisfied with the findings), obtained any required consents or approvals and fulfilled any other conditions set forth in the agreement. On or before the closing date, filings will be made in the state where each organization is incorporated, in the form

required by the state. Once the merger filings are accepted, the merger is complete

Mergers, done properly, are sophisticated transactions and can be resource intensive. Cutting corners can result in ugly surprises that eat into or even destroy the value of the merger. While a merger transaction can be daunting, securing the assistance of experienced counsel and an experienced merger consultant will help to ensure a smooth transaction.

Like

Be the first of your friends to like this.

0 Comments - [Leave a comment!](#)
