

There are many reasons why two not-for-profit organisations may wish to merge. This briefing note provides an introduction to the main types of merger, the due diligence process and the key transaction documents.

What is a merger?

Mergers of not-for-profit organisations can take a number of different forms. The three most common models are:

1. Two or more organisations forming a new entity with a new identity to take over the work and assets of all the organisations involved. This is often referred to as a '**unified full merger**'.
2. One organisation retaining its identity and taking over another organisation's work and assets. This is often referred to as a '**unified takeover**'.
3. One organisation taking over the management of another or keeping it as a separate organisation or brand within a group. This is often referred to as a '**group structure**'.

A unified full merger can either be achieved by transferring the assets of one organisation to the other (a form of takeover) or by creating a new organisation. A unified takeover is achieved by transferring the assets of one organisation to the other. A group structure can either be achieved by one organisation becoming a subsidiary of the other (a form of takeover) or by creating a new holding company with both organisations as subsidiaries.

It is important to fully understand and agree the proposed structure of a merger. Although all three models summarised above result in a "merger", there are important differences between the models that will impact the timing, cost and outcomes.

The structure should be discussed at an early stage in negotiations to ensure that the parties are aligned in achieving the same outcomes and to fully understand the implications for your organisation. It is also important to discuss the proposed structure with your legal advisers.

Due diligence: do your homework!

Any organisation considering a merger should complete proper due diligence in respect of its proposed merger partner. Proper due diligence can help ensure the merger process and, most importantly, the long term integration of two organisations is a success.

Due diligence is the process by which a party carries out an investigation of the organisation it intends to partner with. This is often referred to as a due diligence review.

The primary purpose of a due diligence review is to obtain sufficient information about the potential merger partner's organisation to enable a party to decide whether the proposed merger is in its best interests. Proper due diligence also helps with structuring the proposed transaction (for example, it will likely determine any consents required and determine any ancillary documentation needed) and with integration of the parties upon completion of a merger.

The form and depth of due diligence will depend on the relationship between the parties and the proposed form of merger. A due diligence review will often focus on a potential merger partner's legal, financial and business affairs.

- **Legal due diligence** focuses on the legal risks with the proposed transaction. It will often involve a review of the potential merger party's constitutional documents, minutes of meetings, material contracts, loan and funding arrangements, ownership of assets and any potential litigation. The key areas for review when conducting legal due diligence will vary depending on the nature of the proposed merger partner's organisation. Legal due diligence is often carried out by lawyers.
- **Business due diligence** focuses on the market in which the potential merger partner operates, its clients and customers, its strengths and weaknesses and its prospects. This is often carried out by the party considering the merger.
- **Financial due diligence** focuses on the financial aspects of the potential merger partner's business and those areas of the potential merger partner's financial affairs that a party considers material to its decision to proceed with the transaction, so that it can identify and assess the potential financial risks and opportunities and, in light of this, whether the merger is the right thing to do. This is often carried out by accountants.

When to seek legal advice?

Where possible, it is important to involve advisers early on in the merger process and before any documentation is signed (including heads of terms). Lawyers will assist throughout the process including:

- Exploration**
- Initial legal advice including in respect of proposed structures and any key issues.
 - Identifying if the proposed parties have the power to merge and whether there are any restrictions on the use of the assets or funds of your organisation (or the proposed merger partner).
 - Advising in respect of the choice of merger model.
 - Preparing heads of terms.
- Planning and structuring**
- Assisting with legal due diligence.
 - Structuring the transaction.
 - Assistance in respect of corporate law, employment law (including any TUPE considerations), pensions law, property law and charity law.
- Implementation**
- Preparing and negotiation the transfer documents.
 - Assisting with any employee or pensions issues (particularly in the context of a transfer of assets).
 - Implementing the transfer and helping to identify and complete any registrations, filings or other requirements.

Key documentation

Below is a high level summary of some of the key documentation you will likely need to implement a merger:

- Heads of terms**
- A heads of terms sets out the key principle terms of a proposed merger. This will likely include details of the proposed structure, details of the board changes, timing etc.
 - Although generally not binding, it is important to discuss the proposed heads of terms with your lawyers to ensure they properly reflect the parties' commercial agreement regarding the proposed transaction.
- Confidentiality agreement or non-disclosure agreement**
- One or both of the parties may wish to enter into a confidentiality agreement at the outset of discussions to govern the disclosure of confidential information between the parties.
- Merger project plan**
- A well thought through and detailed project plan is key to the implementation of a successful merger. The project plan should set out the key steps required in respect of both parties to implement a merger.
- Due diligence report**
- Depending on the size of the merging entities and the merger model adopted, both parties and their respective

advisers (legal, accounting, commercial) may prepare due diligence reports summarising the findings of their review, identifying any key issues for consideration and recommending steps for implementation pre- or post-merger.

Constitution of merged organisation

- This will depend on the merger model adopted. In the case of a unified takeover it may be that no changes are required to the 'surviving entity' whereas in the case of a unified full merger it may be necessary to draft constitutional documents from scratch for the newly created entity.

Transfer document

- The transfer document is a legal contract between the parties that will implement the transfer. The nature and complexity of a transfer document will depend on the merger model adopted by the parties and the complexity of their respective organisations.
- Depending on the nature of the transaction, the transfer document will set out the assets being transferred or excluded.
- The transfer document may contain warranties and indemnities given by the respective parties in respect assets and liabilities being transferred as part of the merger.
- The transfer document will include any conditions to be satisfied by the parties and will set a date on which the merger will complete.

Ancillary transfer documentation

- It may be necessary to prepare separate ancillary transfer documentation in respect of certain assets. This may include assignments or novations of contracts, leases or IP.
- If there are employees or workers (as distinct from volunteers), specialist advice will be needed on the implications of the proposed merger and any specific steps that need to be followed.

Corporate approvals

- In addition to board and trustee consent (which must all be recorded in the ordinary and proper course), it may be necessary to obtain the consent of shareholders, members or other third parties.

Announcements, customer and client notifications

- The parties should agree a communications plan so that there is a consistent message.

As decision to merger should not be taken lightly as it may dramatically change the direction and prospects of a not-for-profit organisation. That said, with proper planning, thorough due diligence and appropriate third party advice, the board of trustees or directors on an organisation will be fully equipped to determine whether a merger is in its best interests. Proper preparation and planning is key!

This guide is for information purposes only and should not be relied on as a statement of law or as a substitute for appropriate advice.

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