

Legal Issues to Consider When Organizations Merge

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Why?

- Continued viability increasingly doubtful
- Weakening leadership
- Loss of key staff – founder retiring?
- Not enough capacity
- Stronger together?
- Funder insists

Making a Decision

- Force the issue?
- Do your homework – investigate options, consult advisors
- Strategic planning session?
- Engage key stakeholders to consider alternatives, get buy-in
- Not too late? Important to discuss

Alternatives?

- Will merged organization keep original focus that made it unique?
- Larger organizations can be more bureaucratic, and can be more costly to run
- Share resources, short of merger? “Back office”?

Preparing a Package

- Outline key information needed to evaluate pursuit of a merger.
- Statement of perceived strengths, weaknesses, why a merger is being explored
- Clarifies what you want, whether merger is the right answer. It may not be.

Package Contents

- Financial statements
- material terms of employment contracts
- if unionized, the collective agreement
- assets and approximate value of liabilities
- outstanding litigation – covered by insurer?
- funder relationships and commitments – transferable?
- Client volume and service needs
- List of your organization's professionals

Finding a “Partner”

- May approach you - underutilized resources – human, financial, and/or assets, and want to expand
- More likely, recognizing need to merge, your organization will be approaching another.
- How to choose who to talk to?

What is important to preserve?

- Quality of services you provide
- Retention of valued employees, opportunity for career advancement
- Funding relationships
- Core values of your organization – are they compatible with the core values of your “target”?

The “intangible” – you do want the spark!

What do you look for in the target?

- Compatibility – if staff, clients to continue
- Complementary – strengths and weaknesses of yours addressed by target's own.
- Values – how will the approach your organization has adopted in its relations with its clients change?

Is There a Good Fit?

- Achieving efficiencies of scale,
- needing access to more sophisticated resources,
- funders' insistence, or
- insufficient organizational energy to continue.
- The “intangible” – like a marriage, you do want the spark!

LOI & NDA

Letter of Intent

- the key business points
- not legally binding, documents and clarifies business terms agreed upon

Non-Disclosure Agreement

- legally binding
- ensure confidentiality
- control communications to your stakeholders, including your staff and clients

Member Approval

- Sale of all or substantially all assets of a corporation requires the approval of the membership by a 2/3 vote at a meeting of members (majority if ONCA applies)
- Amalgamation: same

When? Depends on membership, anticipated reaction

Structuring the Deal

- Legal structure of a merger can vary
- Depends on assets and liabilities held, intended governance, and tax issues.
- One option – amalgamation: two merging organizations become one, in law
- Other option - asset transfer: selling organization transfers specified assets – could include employment contracts

Amalgamation Agreement

- What is the name of the amalgamated entity?
- How would the amalgamated corporation be governed?
- The Amalgamation Agreement sets out how that happens:
- What Bylaws will be in force
- Who the members of the amalgamated corporation will be
- Who the first board is?

Consents

Often there will be consents to obtain as preconditions to closing:

- Landlord, depends on the lease wording
- Mortgage being assumed
- Funders – depends on terms of grants

Finalizing the Agreement

- Signing an Agreement obliges the parties to close
- Sets out all the binding terms,
- Warranties – or promises – the other party intends to rely on
- How closing occurs – who does what
- What the closing documents are

Price

- Often nominal – mission to continue, assets are applied for the mission going forward
- What would the transferring organization do with substantial purchase price? Would a purchaser be willing to pay above nominal? Is impressed with an obligation to pursue the mission in any event.

Address Liabilities

- Due diligence – no surprises
- Amalgamation – are assumed automatically
- Asset Sale – need not be, BUT need to consider creditors' rights:
 - Terminate employment contracts, leases
 - Apply funds from sale to pay off debts
- Transfer by a charity – caution
- No recourse post-closing if something turns up

Taxes

- Land transfer tax on transfer of real estate: even if the assets acquired for a nominal price, LTT payable on the value of the encumbrances assumed – rate varies, but is about 1.5% - doubled in Toronto
- HST – consider, although most non-profits are not registered
- Income tax – not an issue for most

Employees

Some employees might be kept

- If amalgamation, automatically become employees of the amalgamated corporation.

If employees not kept, need to terminate them, without cause, with appropriate notice, or pay in lieu.

If unionized, “successor rights” may apply.

- Enacted to preserve collective bargaining rights for employees where a business is sold
- Apply to non-profits as much as for-profits

Closing the Deal

- Document drafting – might be appended to the Merger Agreement
- Due diligence – lawyers on the acquiring side ensure their client gets what they contracted for
- Satisfy conditions
- Sign the documents – often done electronically these days.

Dissolution

- If asset sale, you'll be stuck with a shell corporation – no assets, hopefully no liabilities, that has to be dissolved. There are a number of consents that are rare required, and finally, filling an application to the government to dissolve.

Costs

- You can never tell what will come up.
 - the lawyer on the other side can be difficult.
 - serious problems with the union – if there is one.
 - If real estate, there could be a serious title problem
- Reality is often dozens of documents to be drafted, negotiated, and signed, and extensive due diligence
- Ensure there's a decent budget for legals and other merger expenses
- If a funder is driving the merger, it's very likely that it will pay the bills