



## Working Better Together, Part Two: Mergers as a Strategy for Success



**CAPLAW Training Webinar**  
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## Agenda

- Why merge?
- Issues to consider before moving forward
- Overview of merger process
- Who are the players and what are their roles?
- Lessons learned from other CAAs

## Polling Question #1

### 1. Has your CAA ever *(select all that apply)*:

- a. Merged with another CAA?
- b. Merged with another non-CAA organization?
- c. Started the merger process but ultimately decide not to complete the merger?
- d. None of the above

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## Merger Case Study

### Agency A

- Non-profit CAA; \$15M annual revenue
- 24 board members; 92 employees
- Serves 3 counties (mix urban/rural)
- **Programs:**
  - CSBG
  - Head Start
  - Energy assistance
  - Weatherization

### Agency B

- Non-profit CAA; \$5M annual revenue
- 18 board members; 65 employees
- Serves 2 counties, adjacent to Agency A's 3 counties (urban)
- **Facing financial difficulty** (significant loans that CAA cannot repay; built a number of homes as part of a housing development that could not be sold).
- **Programs:**
  - CSBG
  - Head Start
  - Energy assistance
  - Weatherization

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## Why Merge?

- Cuts in government funding and intensified competition for funding
- Be better equipped to meet increased funding source expectation for effectiveness, efficiency and oversight
- Strengthen financial position
- Increase exposure within community
- Expand service programmatic offerings
- Executive/leadership transitions

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## Working Definition of Merger

- **Working Definition**
  - General term used to describe a partnership in which two or more organizations become one
    - *Legally, governed by state nonprofit corporate law and generally describes a transaction where one organization is the successor to all of the assets and liabilities of the other organization*
- **Many different ways of structuring a merger**
  - First, discuss **goals** of partnership
  - **Form** (choice of partner and structure) will follow **function** (what we hope to achieve)
  - Language matters in framing partnership

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## Issues to Consider Before Moving Forward

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## Issues to Consider

- When to start thinking about a merger?
- Choosing merger partners
- Choosing a merger structure
- Funding source rules
- Overview of merger process

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## When Should We Start?

- **Before it is necessary** (i.e., before there is a crisis/before programs have been damaged)
- Often **leadership transitions** can be a good time to initiate conversations internally and externally

## Choosing Merger Partners

- **What are some ways of identifying potential partners?**
  - Existing alliances and collaborations
  - Board or ED contacts/relationships
  - Working with a consultant
    - E.g., state CSBG office or CAA state/regional association

## Choosing Merger Partners

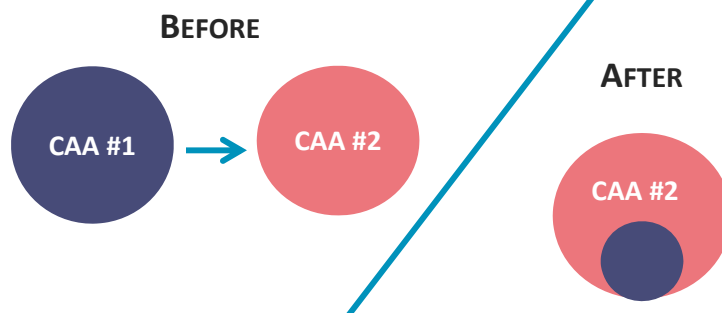
- **What should we look for in a partner?**
  - May, but need not necessarily be, another CAA or Head Start grantee
  - Both organizations bring strengths (e.g., resources, relationships, experience, skills) to the table
  - Compatible missions, services, organizational cultures
  - Strategic service fit
  - Geographic fit

## Choosing a Merger Structure

## Changes in Corporate Structure

### Acquisition Merger

Surviving corporation assumes assets and liabilities of one or more corporations, which then cease to exist (non-surviving corporations)



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## Changes in Corporate Structure

### Acquisition Merger

#### MERGER CASE STUDY

Merger between Peoples' Regional Opportunity Program, Inc. and Youth Alternatives Ingraham to form the Opportunity Alliance

*This case study is based on CAPLAW's interview with Mike Tarpinian, Chief Executive Officer of the Opportunity Alliance in Portland, Maine, about the merger of a Community Action Agency, Peoples' Regional Opportunity Program, Inc., with Youth Alternatives Ingraham to form the Opportunity Alliance.*

##### PEOPLES' REGIONAL OPPORTUNITY PROGRAM, INC.

Peoples' Regional Opportunity Program, Inc. (PROP) was a 501(c)(3) Community Action Agency (CAA) with annual revenue of approximately \$17 million and about 225 employees. PROP provided the following services to low-income people in Maine, particularly in the Portland area:

- Head Start, Early Head Start and child care services

##### YOUTH ALTERNATIVES INGRAHAM

Youth Alternatives Ingraham (YI) was a 501(c)(3) organization with annual revenue of approximately \$19 million and about 260 employees. YI, based in South Portland, Maine, served children, youth, adults, seniors, families, and communities throughout Maine. YI provided the following:

- Crisis prevention and intervention services

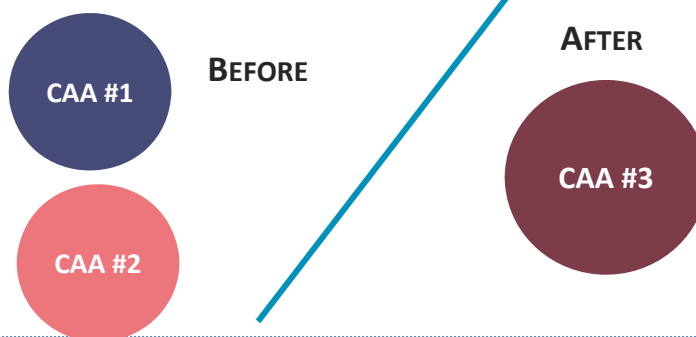
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## Changes in Corporate Structure

### Consolidation

A new corporation is created, which assumes assets and liabilities of two or more other corporations, which cease to exist



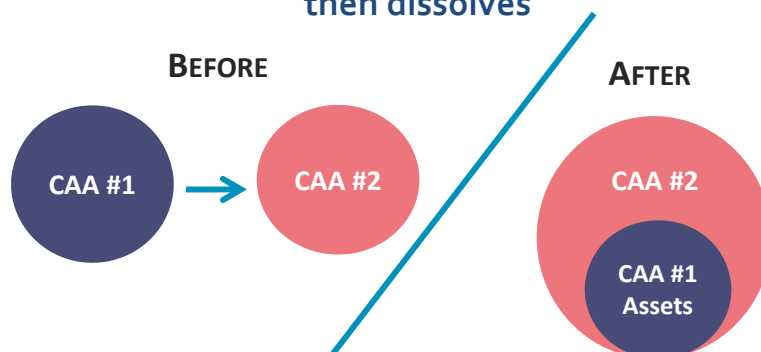
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## Changes in Corporate Structure

### Asset Acquisition/Transfer

One corporation transfers all or a portion of its assets (but usually not liabilities) to another and then dissolves



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## Changes in Corporate Structure

### Asset Acquisition/Transfer

#### MERGER CASE STUDY

Merger between Mahube  
Community Council (Mahube) and  
Otter Tail-Wadena Community  
Action Council (Otter Tail)

*This case study is based on CAPLAW's interview with Dr. Leah Pigatti, executive director of Mahube-Otwa Community Action Partnership (Mahube-Otwa) in Minnesota, as well as a review of Mahube-Otwa's website. This case study presents an example of the combination of a CAA experiencing financial difficulties with a larger and healthier CAA.*

##### MAHUBE COMMUNITY COUNCIL

Mahube Community Council (Mahube) was a 501(c)(3) Community Action Agency (CAA) that served three counties and that had an annual budget of approximately \$12-15 million and about 92 employees.

##### OTTER TAIL-WADENA COMMUNITY ACTION COUNCIL

Otter Tail-Wadena Community Action Council (Otter Tail) was a 501(c)(3) CAA that served two counties and that had an annual budget of approximately \$5 million and about 65 employees. Both ran similar programs, including Head Start, energy assistance, and weatherization.

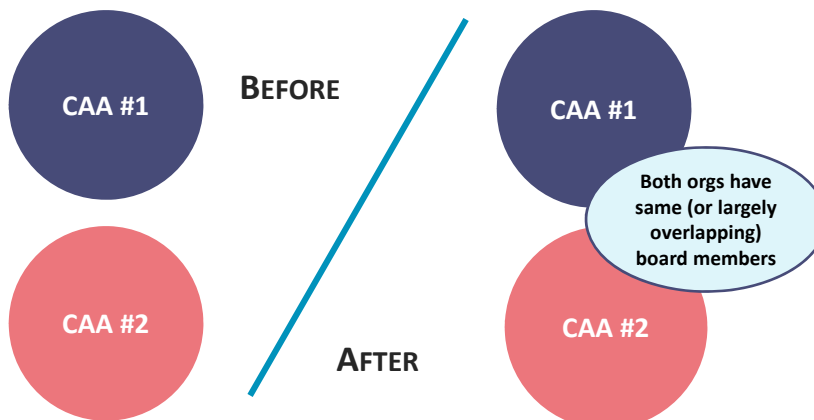
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## Changes in Control

### Interlocking boards

#### One organization controls both boards



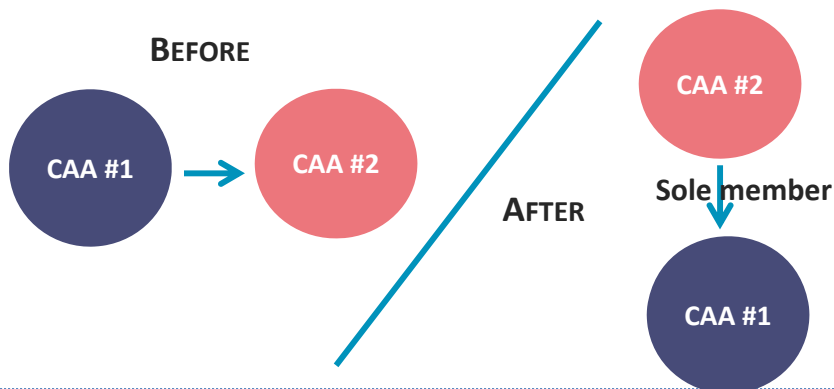
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## Changes in Control

### Parent-Subsidiary

One corporation becomes a subsidiary of another corporation (parent)



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## Changes in Control

### Parent-Subsidiary

#### MERGER CASE STUDY

Merger between Mesa Community  
Action Network (MesaCAN) and A  
New Leaf, Inc. (A New Leaf)

*This case study is based on CAPLAW's interview with Kathy Di Nolf, Executive Director of MesaCAN, and Michael Hughes, CEO of A New Leaf. This case study presents an example of a parent-subsidiary merger between a small, non-profit CAA facing significant financial challenges and a larger, more financially robust non-profit organization providing overlapping social services in the same service area.*

#### Mesa Community Action Network

At the time of the merger, MesaCAN was a 501(c)(3) non-profit community action agency (CAA) that provided a variety of anti-poverty services in Mesa, AZ, including homelessness prevention and emergency housing assistance, Low-Income Home Energy Assistance Program (LIHEAP), a men's homeless shelter, emergency food assistance and referrals, Individual Development Accounts (IDA), income tax preparation, and financial literacy classes. MesaCAN had an annual operating budget of approximately \$2 million and around 25 employees.

#### A New Leaf

At the time of the merger, A New Leaf was a 501(c)(3) non-profit organization that provided a broad array of social services in Mesa, AZ, including affordable housing units, domestic violence shelters and services, a family homeless shelter and services and youth and behavioral health services. A New Leaf had an annual operating budget of approximately \$20 million and around 250 employees.

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## Funding Source Rules

### ■ CSBG

- Get state CSBG office on board
- Will new designation be required?
  - For all mergers, **maintain tripartite board** composition

## Funding Source Rules

### ■ Head Start

- If **Head Start grantee's "legal status" changes**, HHS will require recompetition (*45 C.F.R. § 1304.5(a)(2)(iii)*)
  - **Recompetition not required** if Head Start grantee survives the merger
- **Need to notify OHS** of name change
- **Need OHS approval** of change in (1) Head Start Director and (2) Executive Director/Chief Financial Officer (if >50% salary paid out of Head Start funds or listed in grant application as key personnel) (*45 C.F.R. § 75.308(c)(ii)*)

## Other Issues . . .

- Ability to transfer other government grants/contracts
- Merger costs likely to be unallowable charges to federal grants, except with prior approval
  - See Uniform Guidance, 2 C.F.R. § 200.455
- **Keep your funding sources informed!**
- Accreditation/licensing
- Union issues

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## Polling Question #2

2. What do you see as the biggest obstacle to your CAA merging with another organization? (*select one*)
- a. Loss of identity and goodwill in the community
  - b. Amount of money, time, and effort required to merge
  - c. Staff concerns about employment post-merger
  - d. Need to recompetete Head Start grant
  - e. Not enough information about the merger process

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## Overview of Merger Process

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## Overview of Merger Process

- **Start with an organizational self-assessment**
  - Motivations
  - Desired goals
  - Critical issues
  - Organizational obstacles and red flags
  - Financial position

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## Overview of Merger Process

- **Initially, have a discussion between organizations' leaders**
  - Identify potential merger partners
  - Engage in discussions with leaders of various organizations to assess interest
- **Once parties are committed to moving forward**
  - Often sign a "Letter of Intent" (also known as a "Term Sheet" or a "Memorandum of Understanding")
    - Outlines objectives and key terms that have been discussed, including payment of fees and costs
  - Enter into a Confidentiality Agreement

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## Overview of Merger Process

- **Consider forming a joint merger committee**
  - Comprised of senior management and board members of both organizations
  - Streamlines merger process
  - Ensures both organizations have an active voice in process
- **Consider engaging a merger consultant**
- **Draft a merger agreement**
  - Each organization should have outside counsel's assistance

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## Overview of Merger Process

### ▪ Conduct due diligence

- Each organization conducts thorough investigation to ensure it understands the **operations, assets, and liabilities (actual and potential)** of the other organization
- Satisfies the directors' **fiduciary duties** to their respective organizations
- Categories of information to inspect:
  - ☐ Corporate structure and records
  - ☐ Intellectual property
  - ☐ Contracts
  - ☐ Employment matters
  - ☐ Finances/debts
  - ☐ Compensation arrangements
  - ☐ Existing or threatened lawsuits

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## Overview of Merger Process

### ▪ Obtain necessary approvals

- Funding sources
- Board of directors
- State/government officials (e.g., Attorney General)
- Third parties to transfer contracts (e.g., landlord)

### ▪ Merger filings

- Secretary of State
- Notify IRS via final Form 990 filing

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## Who Are the Players and What Roles Do They Play?

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### Board Members

#### Role

- Analyzes **pros and cons** of merging, whether and how it will fulfill mission
- **Board committee**
  - Explores options and partners, including (especially for mergers) meeting with potential partners and overseeing negotiations
  - Oversees due diligence (in case of merger or setting up new entity)
  - Keeps full board informed
  - Makes recommendations to full board

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## Board Members

### Votes

- **Full board votes on:**
  - Creating committee and scope of its authority
  - Whether to merge
  - Merger Agreement
  - Corporate documents (if a merger, plan of merger and articles of merger, etc.)

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## Board Members

### Documenting the Decisions

- **Important to document board and committee discussions and votes in minutes**
  - Include the basis for board/committee decision(s)
  - Attach reports, other documents on which board/committee relied

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## Board Members

### Fiduciary Duties

- **Duty of Care:** In overseeing the organization, nonprofit board members must act with “the care an ordinarily prudent person in a like position would exercise under similar circumstances”
  - Possible personal liability if board members don’t carefully examine potential merger partner

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## Board Members

### Business Judgment Rule

- Under the “**business judgment rule**,” nonprofit board members who exercise good faith judgment will usually be protected from liability to the corporation
  - Even if the corporate action turns out to be unwise or unsuccessful

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## Board Members

### Duty of Care

- **Board members must make informed decisions**
  - Board should obtain and consider written reports and professional advice before making important decisions
  - Board should ensure that a full, deliberative process is conducted and that directors are able to ask hard questions and get answers

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## Sample Merger Decision Matrix

Variable	Value	Priority	Scores Based on 100 Total Points
Decisionmakers	Board leadership, Sr. Staff	H	
Timeframe	3-6 months	M	
Program/Mission Fit	X100	H	
Operations Fit	X75	M	
Culture	X75	M	
Relative fit of Board	X55	M	
Systems	X35	L	
Public Relations/Fundraising	X95	H	
Is there a need?	X55	H	
Economically Feasible?	X100	H	
Impact on other programs?	X55	M	
Can we provide a quality service?	X100	H	
Assets	X90	M-H	
Current Assets/Liabilities	X90	M-H	
Leases Obligations	X50	L	
Pending Litigation Issues	X100	H	
Other benefits the merger brings?		H	

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## Management

### Role

- The executive director or interim executive director, chief financial officer, chief operating officer (program or operations directors), other staff
- **Due diligence**
  - Programs and activities
  - Financial strength and viability
  - Sustainability
  - Staff culture and roles
- **Plan for integration**

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## Advisors

### Role of an Outside Attorney

- Involve attorney early on
- Work with attorney(s) in your state with relevant expertise
- CAPLAW is available to consult with CAAs on CSBG-, Head Start- and other government-grant specific issues
- Each partner should work with its own attorney
  - Until, in the case of a formal merger/consolidation, both organizations' boards vote to merge

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## Advisors

### Role of an Outside Attorney

- Evaluate organization's **current legal situation**
- Guide **choice of restructuring options**
  - Form follows function, legal rules
- **Advise the board** on its role and responsibilities
- Advise board and management during **negotiations**
- Conduct legal **due diligence**
- Draft **legal documents**
- Handle **filings** with state (Articles of Merger, etc.)

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## Merger Agreements

- **Typical provisions**
  - Merger structure
    - If asset acquisition, list of specific assets and liabilities being acquired
  - Name of surviving organization
  - Amending governing documents
  - Makeup of the board of the surviving organization
  - Senior leadership positions
  - Retention of employees
  - Continuation of key programs
  - Representations and warranties of each organization
  - Conditions for closing (e.g., obtaining needed approvals)

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## Advisors

### Role of Other Outside Professionals

- **Consultants** – help identify partners and facilitate merging or other partnership
- **Accountants** (especially for mergers) – tax filings, impact on financial statements, due diligence
- **Funding sources/state association/local municipality** – understand landscape of organizations with shared missions, providing similar services

## Lessons Learned from Other CAAs

## Lessons Learned

- **Build trust and familiarity with the other organization**
  - Good relationship prior to merger is essential
- **Ensure merger furthers each organization's mission**
- **Be clear about how a merger will enable each organization to achieve its overall goals**
- **Conduct thorough due diligence**
  - Be honest about each organization's assets, liabilities, strengths, and weaknesses

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## Lessons Learned

- **Have a strong advocate for the merger**
  - CEO, board/board chair
- **Keep your funding sources informed**
  - Involve major funding sources (government/private) early in the process
- **Communicate with and involve staff members**
  - Communicate early and often to get staff buy-in
  - Work to align organizational and staff interests
  - Clarify new roles

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## Lessons Learned

- **Don't overlook organizational culture issues**
  - Address integration issues from the outset
  - Anticipate future issues and concerns (size, reputation, financial strength, etc.)
- **Engage outside experts**
  - 3<sup>rd</sup> parties offer outside perspective
  - Rely on experts who are familiar with the merger process

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## Polling Question #3

3. What additional resources do you think would help your CAA be in a better position to consider a merger? *(select all that apply)*
- a. Additional case studies on CAA mergers
  - b. Sample documents (merger agreement, confidentiality agreement, etc.)
  - c. Resources/trainings on the due diligence process
  - d. Resources/trainings for board members on their role in the merger process
  - e. Other (please type into the chat panel)

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## Additional CAPLAW Resource

### Working Better Together: CAPLAW's Guide to Shared Services and Mergers

<http://www.capl原因.org/resources/PublicationDocuments/mergersandsharedservices/Introduction.html>

**Resources**

CAPLAW Shared Services and Merger Case Studies

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**Merger of a Maine CAA and a non-CAA**

This case study is based on CAPLAW's interview with Mike Tarjman, Chief Executive Officer of the Opportunity Alliance in Portland, Maine, about the merger of a Community Action Agency, Peoples' Regional Opportunity Program, Inc., with Youth Alternatives Inc. to form the Opportunity Alliance. [Read more](#)

**Management Agreement between Georgia CAAs**

This case study is based on CAPLAW's interview with Nancy Smith, Executive Director of Middle Georgia Community Action Agency, Inc. and Heart of Georgia Community Action Council, Inc., and a review of the management agreement between the two organizations and their annual reports. [Read more](#)

**Merger of CAA and non-CAA in Suffolk County, NY**

**Working Better Together**

- Introduction
- Shared Services
- Mergers

**Introduction**

- Why are CAAs looking at shared services and mergers?
- What are the benefits of shared services and mergers?
- What are the challenges of shared services and mergers?
- What are the steps to shared services and mergers?
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**Why Consider Sharing Services or Merging?**

## Questions

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