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Sample Client Letter Regarding Merger Issues

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CONFIDENTIAL

Re: Merger Issues

Dear _____:

This is in response to your request that I share some of the non-legal, policy and organizational considerations that I have seen arise when trade associations merge or consolidate.

In my experience, the central issue in such combinations is “compatibility.” By that, I mean much more than just the integration of staff, computers, offices, bylaws, pension programs, taxes, and other legal issues. Although these are important matters which need to be addressed in detail in the due diligence phase, the “mechanical” problems can usually be worked out. Compatibility of associational style, philosophy, culture, and members can be even more important and even more difficult to anticipate and evaluate. The following are some examples of these types of compatibility factors that can arise in an association marriage. I have erred on the side of including subjects which might be obvious, but nonetheless should not be ignored:

1. Association Demographics. I understand that _____ has approximately _____ members, of an average size of \$_____ million in assets as compared to _____ members with an average asset size of \$_____ million in _____. INSERT on different membership types and categories. This difference can prompt several issues:

A. Voting Procedures and Control. Will the successor organization have procedures whereby the larger _____ members can still control the Association on matters of importance to them? Strict democracy would make them a small minority. There are ways of allocating seats on a board to different classes of members and vesting decision-making power on certain issues to subgroups that are uniquely impacted. The difference in membership

numbers and demographics can, nonetheless, create strains and contribute to a “big vs. small” climate.

B. Dues Equity. A cursory review of the 990 comparison shows a dramatically different financial support base. With approximately the same overall budget, _____ is much more reliant on member dues. The level of individual dues for the members of _____ is no doubt substantially higher than those of _____ members who have both a larger member base and the non-dues revenue support. The integration of the dues structure can be difficult. Should members with roughly the same revenues from the different associations pay roughly the same dues? Sticker shock might ensue. On the other hand, companies that are paying a high or disproportionate share of dues are likely to want more attention to their views and agendas. Dues considerations are often tied to issues of voting control.

C. Focus. A larger, broader based organization has a variety of advantages: increased funding, efficiencies of scale, more coordination on problems of mutual concern, broader constituent contacts on legislative and governmental issues, greater prestige, etc. However, there is a potential down-side -- a dilution of focus on issues that are of critical concern. This can occur in many senses: (i) The merged group may simply not agree with the previous substantive positions and may vote to change or alter policy. (ii) Even if an associational position is approved, the expression of contrary views by association members can be harmful in the public policy arena where government officials and legislators do not like to deal with industries or associations that have not worked out their differences internally. (iii) The new group may not share the previous prioritization of issues and could vote to pare back the funding and other resources committed to an effort. (iv) Top level executives may not want to participate on Boards or Committees that deal with a variety of issues that they are not directly concerned about. (See Item 3, below)

2. Decision-Making Style. Some groups function based on consensus. They seek unanimity and do not take on projects or positions without overwhelming support of the members. This restriction can be by Bylaw requirement for super-majorities on votes, but is more often a result of historical group culture. Other associations have a style of confrontation and diversity, or at least frank and conflicting discussion of issues. Action is taken based on a simple majority even if there is a sizable minority. The tenor of member interactions tends to vary with these two different types of groups.

3. Level of Company Participation. Boards that are composed of company CEO's or business unit managers who can make decisions and take creative approaches without having to go back to headquarters for approval have a distinct advantage. Other groups function with lower level managers on their Boards who are unable to make major decisions on their own.

4. Association Role. There is a spectrum of how different industries rely on their trade associations. Some look primarily to the association to solve problems -- governmental, promotional, technical, training and even commercial difficulties. Others have a very limited view of the association's purpose and role, leaving many subjects for members to deal with independently. This disparity is often tied to fiscal approach, with the association minimalists typically having a low-dues, more penurious bent.

5. Approach to Problems. Some obvious culture differences in this category include:

- + Proactive -- Reactive Styles
- + Reliant on government to solve problems vs. antagonism to government
- + Regulatory activism vs. regulatory defensiveness

6. Association Identity and Pride Factors. Problems often arise out of the perception of dominance and subservience in the two merger partners. In some situations it is clear from the outset that one party is "taking over" the other. Obviously the merged organization's CEO can have a dramatic role in this factor. If the transaction is viewed more as a melding of two equal groups, factors of organizational pride can crop up in areas such as the new name, the offices that are retained, and staff positioning among others. Although these are minor in substance, they often are the most emotional issues to overcome.

7. Staff and Leaders. Although discussed last, this item can have the most dramatic impact on the course of merger discussions. Although some merging groups have worked out "co-CEO" positions for a combined association, this rarely is implemented and rarely is effective. There needs to be a clear understanding at an early juncture between the merger partners as to the roles of the previous volunteer and staff leaders.

I do not mean to suggest by the discussion of potential compatibility issues a negative disposition to the merger concept; I have raised them at your request merely to stimulate discussion.

The following are a generic list of pros and cons for association mergers

PROS

Increased size
Enhanced financial resources
A more powerful voice on substantive issues
Broader constituent clout on legislative matters
Opportunity to address more issues of common concern
Opportunity to unify industry positions internally
Staffing Issues:
 Efficiencies of scale and avoidance of duplication
 Increased specialization of in-house capabilities
 Opportunities for staff advancement
Members have more opportunity to network with other players in the industry

CONS

Potential for battling cultures
Dilution of substantive focus
Potential loss of control
Dislocation of staff and member energy to complete the merger
Increased anti-trust vulnerability if customers and suppliers are also members
More chance for disagreement on issues with a more diverse membership
Staff redundancy and cuts

Please give me a call if I can be of any further assistance.

Very truly yours,

Brock R. Landry