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Memorandum

Frequently Asked Questions About the Merger of New Jersey Nonprofits

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The reasons for mergers in the nonprofit sector are as varied as reasons for business combinations among for-profit businesses. For instance, organizations with complimentary missions combine to improve the efficiency and scope of services they are able to provide together rather than separately. Or, organizations delivering similar services to the same served community (e.g., shelter for transitionally homeless) might combine to improve their collaboration in delivering needed services while eliminating their competition for funding sources. Whatever might the reason be for considering a merger, the process of organizing the legal and practical aspects of combining two or more nonprofit organizations involves hard work and unfamiliar requirements. We hope, by demystifying the legal steps needed to effect a merger with these FAQs, to help everyone involved in the merger process to stay focused on achieving whatever expected benefits underlie the decision to work toward a combination of nonprofit organizations.

What are the Legal Implications of a Corporate Merger?

The merger of two or more nonprofit corporations – hereinafter referred to as the "merging corporations" – is accomplished through "operation of law", which means that a statute (the New Jersey Nonprofit Corporation Act) both directs how a merger occurs and controls the end result. [*See N.J.S.A. 15A:10-1 et seq*.] For ease of discussion in these FAQs, we will discuss the merger of just two nonprofits. In some cases, multiple nonprofits merge at the same time, and the process is essentially the same.

The primary legal implication of a merger is that post-merger one of the merging corporations will no longer exist. At the point of merger, one corporation simply become part of another corporation, which is known as the **surviving corporation**. The other corporation is said to have been "merged out of existence" and is know as the **merged corporation**. The surviving corporation generally maintains the name and tax-exempt status of the corporation as it existed prior to the merger. However, in some cases the name of the surviving corporation is changed to give it a new, post-merger public identity.

After the Boards of Trustees of the merging corporations work out the merger details, these details are described in a **Plan of Merger** that is filed, along with a **Certificate of Merger**, with the New Jersey Department of the Treasury.[1] The act of filing the Plan of

[1] A sample Certification of Merger is available at www.state.nj.us/treasury/revenue/dcr/pdforms/umc3.pdf

Merger triggers the implementation of the merger. If any of the corporations involved in the merger has been recognized by the IRS (federal government) as tax exempt, the IRS must receive notice of the merger, along with a copy of the Certificate of Merger that was filed with the State of New Jersey.

What Must Happen Prior to the Actual Merger?

The Board of Trustees of each of the merging corporations must inform themselves about all the pros and cons of merging with the other organization. This is accomplished through the assistance of professionals, generally corporate attorneys and/or accountants, who organize an investigation of each corporation's finances, assets, and liabilities. This process is known as "due diligence". The purpose of due diligence is to uncover any legal or financial issues that will be inherited by the surviving corporation, or that would pose a barrier to the merger in the first place. The due diligence process can take time, as it entails review of corporate documents that may or may not be readily accessible. *See included sample "Due Diligence Request*".

Once due diligence has been completed, the results are presented to the Board of Trustees of each organization involved in the merger. This ensures that each board is fully informed and can make a prudent decision about the wisdom of merging with the other organization.

What Happens to the Assets and Liabilities of the Corporation Merged Out of Existence?

At the moment of merger, both the assets and the debts/liabilities of the merged corporation become the assets of the surviving corporation. This means that all the property (including cash on hand, land, vehicles, equipment, and office supplies) owned by the merged corporation becomes the property of the surviving organization. Similarly, all debts, such as leases, bank loans, compensation owed to employees, utility bills, become the responsibility of the surviving corporation.

What Impact Does a Merger Have on the Boards of Trustees?

It is the legal responsibility of each Board of Trustees of the merging corporations to approve a Plan of Merger, and to direct that the Plan and a Certificate of Merger are properly filed with the New Jersey Department of the Treasury. To approve a Plan of Merger, the board of each corporation must determine that the merger is in the best interests of that corporation. This usually entails an examination of the mission and activities of the corporations and sometimes will require an amendment to the mission statement or purposes clause of the Certificate of Incorporation of the surviving

corporation. If any corporation is a *membership* nonprofit, the members must vote to approve the Plan of Merger, if they have such voting powers.

Sometimes the Board of Trustees of the surviving corporation will be expanded to include some members of the merged corporation, although this is not a legal requirement. Other times, the surviving board will be totally reconstituted to reflect a combination of the board members of each nonprofit.

How Does the Merger Actually Happen?

After the due diligence process has been completed, all the information is sorted through and the Boards of Trustees, or committees thereof, determine how to address any outstanding issues relating to (1) the transfer of assets and liabilities and (2) the post-merger operations of the surviving corporation. A document is drafted that describes the road map for the merger. Sometimes the road map takes the form of a detailed (but usually non-binding) "Memorandum of Understanding" or "Letter of Intent", though more often the parties negotiate a legally binding "Agreement of Merger". Experienced business lawyers can guide the organizations to determine the appropriate scope and genesis of the "road map" document(s) based on cultural and practical considerations. What all road maps have in common is a **Plan of Merger**. The Plan of Merger must be approved by each Board of Trustees of the merging corporations. New Jersey law specifies that a Plan of Merger must contain:

1. The names of the corporations proposing to merge, and the name of the surviving corporation;

2. The terms and conditions of the proposed merger, including a statement of any amendments to the Certificate of Incorporation of the surviving corporation that are necessary due to the merger;

3. If any corporation is a membership corporation, the manner and basis of converting the membership from the merged corporation into the surviving corporation; and

4. Any other provisions that are deemed necessary, such as the date that the merger is to become effective, if not the date of filing the Certificate of Merger with the Department of the Treasury.

The Plan of Merger is then presented to each nonprofit's Board of Trustees, as a board resolution at a board meeting that is called for the express purpose of voting on the Plan of Merger. Proper notice must be given for the meeting, in accordance with the Bylaws of each corporation. Each Board of Trustees must approve the Plan of Merger by an

affirmative vote of two-thirds of the board members present at a meeting at which there is a quorum, unless a greater percentage is called for by the Certificate of Incorporation of Bylaws. Alternatively, if there is no physical meeting of the board members, then the Plan of Merger must be approved by "unanimous written consent" (a signature of each board member must be obtained approving the Plan of Merger – this can be accomplished by fax). Special voting rules apply in the case of membership nonprofits.

A **Certificate of Merger** is then prepared, describing the approval of the Plan of Merger (i.e., how many Trustees voted to approve versus how many disapproved, or whether the Plan of Merger was approved by unanimous written consent; effective date of merger). The Certificate of Merger, with a copy of the Plan of Merger attached, is filed with the New Jersey Department of Treasury, along with a filing fee (currently $75).

Once the Certificate of Merger and Plan of Merger have been filed, the merger is effective, unless a later date has been specified in the Plan of Merger and Certificate or Merger. A duplicate copy of the Plan of Merger and Certificate of Merger is returned to the surviving corporation, with the date of filing stamped on the documents, as proof that the merger occurred.

The final step is to inform the IRS of the merger through correspondence that includes a copy of the Plan of Merger and Certificate of Merger.

Last revised: April 2012