10 STEPS TO SUCCESSFUL CREDIT UNION MERGERS

d. hilton associates inc.

TEN STEPS TO SUCCESSFUL
CREDIT UNION MERGERS

D. Hilton's 30 years of experience in credit union mergers has taught us that no two credit unions are exactly alike. As such, these ten steps are meant to provide a foundation for executing a successful merger, but are by no means absolute. As a third party consultant, D. Hilton's job is to assist both credit unions in navigating these steps and ensure member value at all stages.

1 CULTURAL DUE DILIGENCE

First, both organizations must become acclimated with each other's culture and value proposition through a series of meetings. Participants typically include key senior managers and Board members. The sessions typically take place in offsite locations to protect confidentiality. Discussions should be high level and focused on culture, member value, and employee value. D. Hilton acts as facilitator through the sessions to build relationships and begin identifying potential deal breakers. The key question that should be answered in step one is, "Would our two credit unions be better together than either would be on its own?"

2 BOARD DECISION TO EXPLORE DEEPER

At the conclusion of step one, the Board at each credit union should determine their interest in moving forward towards operational due diligence. This is a critical juncture as due diligence work is time consuming and has expense. Each Board should ask two questions:

Question 1: "Based on what we know today and the value we think can be created, does the Board wish to merge with the other credit union?" The Board should know that this does not mean the deal is set in stone but is more of a "rubber meets road" milestone.

Question 2: "Are there any absolutes that the other credit union must honor for the merger to take place?" The objective here is to get any absolutes on the table early. Rarely are these absolutes negotiated to a final offering, but instead are more of an "agreement in principal" before money and time is spent on formal due diligence. For example, if the logo of one credit union must absolutely remain in place, it is better to know now than later. D. Hilton facilitates these discussions with each credit union to identify these deal breakers and acts as independent third party to assist both organizations in reaching a compromise.

3 LETTER OF INTENT

Should both credit unions wish to move forward towards due diligence, it is important that a discussion take place about those absolutes to ensure both parties are in "agreement in principal". The letter of intent serves as a formal agreement between both parties and includes any absolutes that have been discussed, an agreement of confidentiality, handling of expenses, and a stated exclusivity period. D. Hilton assists both organizations with developing the letter of intent and ensures that the details agreed upon are clearly articulated. Both Boards will make a formal motion to proceed with merger due diligence and execute the letter of intent. Because this letter of intent does not mean that the merger will happen, it is important to keep the Board decision as confidential as possible. Notification to the employees and membership is not typically recommended at this stage to protect both organizations should merger discussions cease.

4 DUE DILIGENCE

Both parties will need to conduct various due diligence across a wide spectrum of areas. Examples of areas included in due diligence are human resources, products, contracts, accounting, technology, etc. D. Hilton has extensive experience in evaluating the various aspects of a merger and will work with both credit unions to review and provide guidance throughout the due diligence process. The goal is to determine what the merger will cost (one time and ongoing), what the combined organization will look like, and what the membership gains through the merger. Both credit unions will receive a due diligence report that details all findings, presents a business plan for the combined organization and clearly demonstrates the degree of member value through the merger. Examples of areas D. Hilton typically reviews include, but are not limited to:

- **Goals/objectives of the proposed merger;**
- **Model for organizational structure and reporting structure for all front and back office functions based on discussion by both parties;**
- **Board and committee structure for the combined organization;**
- **Both credit union's policies and procedures and any changes in policies/procedures under the combined organization;**
- **Both credit union's products and service offerings for discrepancies;**
- **Impact the merger will have on product and service offerings (including terms);**
- **Product and service offerings for the combined organization (gains/losses);**
- **Rates and fees of both credit unions and illustration of the cost additions or savings that both memberships would receive under the combined organization;**
- **Executive and staff compensation programs (base salaries and incentive/bonus programs) and illustration of the program for the combined credit union (including timeline for cancellation of vendors);**
- **Health and welfare benefits providers, program components, and contracts in place and illustration of the offerings for the combined credit union (additions/subtractions);**
- **Retirement program vendors, program components and contractual review and outline of the offerings of a combined credit union (including timeline for cancellation of vendors);**
- **Potential expense savings of a merger, one time related expenses, and growth scenarios based on a merger;**
- **Combined financials and estimations of future performance and benefit to the member;**
- **Major third-party contracts, costs of contract termination, and expense savings from consolidation.**

5 NEGOTIATION/AGREEMENT TO MERGE

At this point, both parties need to be clear on what each is promising. Examples of commitments that may be discussed include employee commitments, volunteer commitments, and operations commitments. D. Hilton will work with both Boards to negotiate all final issues. Once completed, these agreements will be formalized in a modified letter of intent titled "Agreement to Merge" that D. Hilton will provide. Both Boards will make a motion to move forward with the merger (application process) and execute the agreement.

6 MERGER ANNOUNCEMENT

A communication plan needs to be initiated that involves notifying the members and community. The employee announcement and a member mailing will need to take place. D. Hilton recommends the first notification be a simple letter from both CEOs or Board Chairs detailing what is happening and promises of more information to come. D. Hilton recommends a second mailer in advance of the member vote that discusses benefits of the merger and instructs the member to look for a vote packet in the near future. D. Hilton will develop a communication strategy for both credit unions, create multiple communications pieces for all stakeholders (members, employees, volunteers, community), and act as both credit unions' communications partner in ensuring the member value message is delivered. Depending on the size and complexity of the merger, announcements may need to take place before due diligence begins.

7 MERGER APPLICATION

A formal merger application will be developed by D. Hilton for state and/or federal regulators. Included in this application are official merger forms, a merger plan, financials, member vote materials, etc. The application is submitted by the continuing credit union and requests permission from regulators to proceed with a membership vote. Application review and initial approval to proceed with a member vote is roughly 60 days. D. Hilton handles all application development, provides guidance on all form submissions and assists in any regulator clarifications or document changes needed.

8 SPECIAL MEETING AND MEMBER VOTE PROCESS

No merger is complete without a majority affirmative vote by the membership (majority of those who vote must vote yes). The merging credit union must provide members the opportunity to vote on the merger, typically by holding a special meeting of the membership and/or conducting a mail ballot process. D. Hilton recommends a mail ballot be conducted to ensure all members (especially out of state members) have the opportunity to voice their opinion. D. Hilton creates all ballot materials and handles the vote process to ensure the credit union complies with federal regulations regarding ballot timelines. D. Hilton also relies on an independent third party for tabulation services to demonstrate impartiality. The entire process takes about six weeks to complete. All votes are documented and certified for regulators.

9 FINAL REGULATORY APPROVAL

Upon a successful vote, D. Hilton will provide guidance to both credit unions for submission of the final vote results along with a request to merge. Regulators will approve the request and provide a final closing date for the merger, at which time the charter of the merging credit union will become inactive. This represents the completion of the merger on paper, but not in actuality.

10 INTEGRATION

Upon final approval from the regulator, both credit unions can begin the integration process. This can take anywhere from six months to two years, depending on the complexity of operations, technology, and staffing. D. Hilton will provide guidance to senior management throughout the integration process to ensure a smooth transition.

IN CONCLUSION

Mergers require significant time and resources, but the right fit can provide both institutions with success and great opportunities for growth. Utilizing a third party like D. Hilton gives both credit unions an independent advisor who can navigate the sometimes difficult process of bringing together two organizations with unique cultures, executives, and perspectives.

For more information on D. Hilton's Merger Services, contact:

Brian Kidwell
Executive Vice President
800.367.0433, ext. 125
Brian@DHilton.com

d. hilton associates inc.

WE SET THE INDUSTRY STANDARD

Since 1985, D. Hilton Associates Inc. has been launching new initiatives and pioneering consulting and outsourcing processes for the credit union industry. We are the largest and most experienced company of our kind.

WE ARE INDEPENDENT

At D. Hilton Associates, we base our recommendations on your organization's unique situation and needs. We are not affiliated or associated with any other credit union service provider. This ensures that our recommendations are entirely independent.

WE WORK EXCLUSIVELY WITH CREDIT UNIONS

D. Hilton Associates specializes in the credit union industry, so we really know your business. We devote our full energy to providing you with specialized expertise in each practice area.

WE OFFER A LARGE IN-HOUSE STAFF

Your organization can rest assured that it is partnering with our full-time, in-house professionals that have outstanding credentials in all our practices. Our practice leaders offer you practical solutions to your concerns and challenges.

WE ARE THE MOST QUALIFIED FIRM IN THE BUSINESS

No other individual or group offers the breadth and depth of both analytical and operational services available through D. Hilton Associates. Our unique blend of credit union experience and technical expertise offers you the option of sole-source support through our variety of inter-related practices.

For a thorough description of our consulting services, please visit our website at www.dhilton.com.

D. HILTON ASSOCIATES INC.
9450 Grogan's Mill Road, Suite 200, The Woodlands, Texas 77380 | 800.367.0433