Commercial

Mergers and Acquisitions: An Overview (Article 1 of 3)

The key idea behind an M&A deal is that two companies together are more valuable than two separate companies. This can be an attractive idea to companies that are in financial hardship. Likewise, stronger companies will act to buy other companies to create a more competitive, cost-efficient organisation. Target companies will often agree to be purchased when they realise that they cannot survive alone – or if the shareholders want to cash in on their investment.

What is an acquisition? It is when one company takes over another and establishes itself as the new owner. The target company ceases to exist; the buyer effectively 'swallows' the business.

What is a merger? A merger happens when two companies agree to go forward as a single new company rather than remain separately owned and operated – known as a 'merger of equals'.

The reality: Mergers of equals rarely happen. Usually, one company will buy another and as part of the deal, the acquired company will be allowed to proclaim that the action is a merger of equals, even if it is really an acquisition. Describing it as a merger makes it more attractive for stake-holders and can also help to retain existing clients of that business.

The language of M&A: Synergy

In M&A deals, you will hear the word 'synergy' used throughout. It is the driving force behind enhanced cost efficiencies of the new business. It takes the form of revenue enhancement and cost savings. By way of a merger, the companies hope to benefit from:

Staff reductions: employers will know that mergers tend to mean job losses. A lot of money will be saved from the reduction of staff whose roles are duplicated (like accounting, marketing, etc).

Economies of scale: a merger should also improve purchasing power, with the merged (larger) company having greater ability to negotiate prices with their suppliers.

Acquiring new technology: by buying a smaller company with unique technologies, a large company can maintain or develop a competitive edge. Companies must stay on top of technological developments and their business applications.

Improved market research and industry visibility: one of the intentions in buying a new company will be to reach new markets and grow revenues and earnings. A merger will give the companies new sales opportunities by expanding their marketing and distribution. It will also give the new company a better standing in the investment community as large companies often have an easier time raising capital than smaller ones.

Synergy is not automatically realised when two companies merge. The opportunities may be envisioned by the corporate leaders and deal-makers, and are often much talked about when the deal is being negotiated, but the reality can sometimes be different. The risk that the market will see through the image that has been created is very real, which is why M&A deals are so complex and often an ongoing matter.

Of course, it is also important within any M&A deal to be aware of the employment aspects – both legal and practical. On the legal side, depending on the way in which the arrangement is structured it is likely that it will be necessary to at least consider the application of TUPE (the Transfer of Undertakings (Protection of Employment) Regulations) and the legal consequences that will follow. TUPE can create new liabilities for entities as well as effectively creating certain restrictions on how affected employees can be handled in the future, for example in terms of any intended changes to contracts of employment or even day to day working practices.

Employees are likely to be an organisation's key asset, and therefore it is vital to consider the practical aspects of any M&A arrangement in order to ensure that productivity is maintained both leading up to and after the deal. This means considering ways of maintaining employee morale throughout this time as well as giving consideration to any new roles that may be required in the future – and also of course whether or not any efficiencies achieved by the M&A process may mean that fewer employees are required. This may thereby give rise to a redundancy situation, which will need to be even more carefully managed if TUPE is also applicable.

Our next Commercial article will deal with the different varieties of mergers and acquisitions. Should you have any queries in the meantime, please do not hesitate to contact the Commercial team at 3HR Legal.

Shamina Chowdhury
Solicitor
E: shamina.chowdhury@3hrlegal.com