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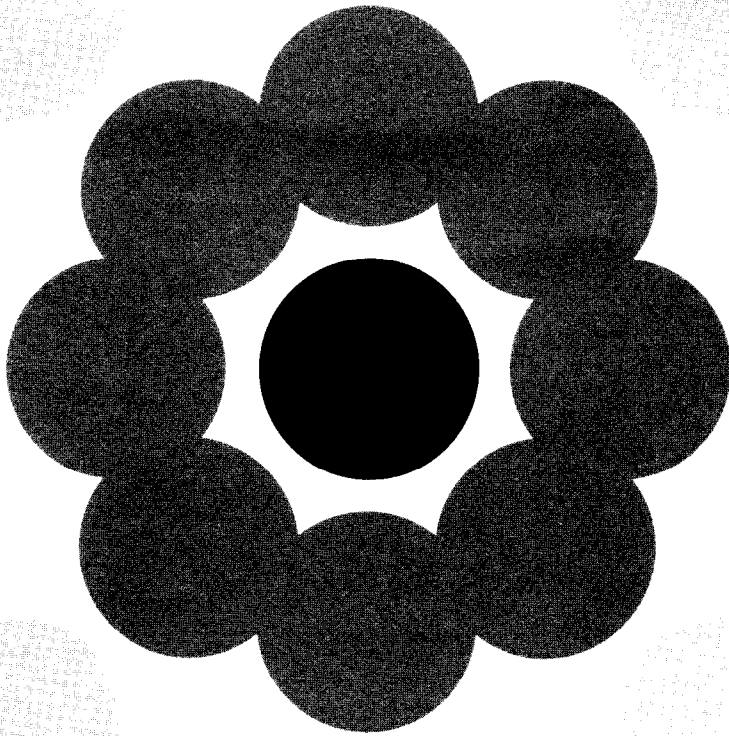
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# Cooperative Merger/Consolidation Negotiations

## The Important Role of Facilitation



# Contents

Why Use a Facilitator? .....	1
Three Phases of the Merger/Consolidation Process .....	2
Major Steps and Approval Stages .....	4
Why Feasible Combinations Get Rejected .....	6
Guidelines for Negotiators .....	7
Develop Producer-to-Producer Contact .....	8
Follow a Strategic Plan for Merger/Consolidation .....	8
Joint Committee's Role .....	9
Make All Positions, Opinions, and Concerns Known .....	9
Maintain Objectivity and Work Toward Solution .....	9
Use the Word "We" .....	9
Establish a Definite Timeframe .....	10
Facilitator's Role .....	10
Differences from Mediation .....	11
Extent of Formality and Procedure .....	12
Use Transcripts of Previous Sessions .....	13
Analyzing Emerging Issues .....	13
Priority of Reaching Agreement .....	14
Using Professional Advisors .....	15
Contacting Cooperative Services .....	17
Appendix A: Issues To Consider in a Cooperative Merger .....	18

# Cooperative Merger/Consolidation Negotiations— The Important Role of Facilitation

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## Why Use a Facilitator?

This bulletin describes some of the difficulties encountered when cooperatives consider combining their organizations and how use of an outside facilitator can help this process. The overall context of major phases and steps in a merger/consolidation process are surveyed, followed by a more detailed examination of just the negotiating phase.

When meetings occur between the cooperatives trying to reach agreement on a plan for combination, a facilitator helps improve communications and the process of developing alternative solutions to many of the problems that arise. Some problems may seem to be solvable without a facilitator, such as making decisions on various business operating changes for a combined organization. However, the participating organizations usually have different preferences and priorities. Customarily, each participating organization has an equal number of representatives on a joint merger committee. Frequently, two cooperatives are involved in negotiating a combination, which sets the stage for group decisions to become deadlocked. A facilitator initiates team-building discussions aimed at finding alternative ways around these deadlocks.

A major challenge in combining cooperatives into one organization is the different cultures and decision-making norms that each brings to a negotiation. The negotiation process is in part an initial test to see if these distinct cooperative cultures can overcome their differences in order to reach an agreement. Being someone from the outside, someone with no vested interest in

these cultures, is the key attribute that a facilitator brings to a negotiation. This attribute helps the facilitator guide discussions in an impartial and fair direction.

### **Three Phases of the Merger/Consolidation Process**

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Farmer cooperatives must often consider the alternative of merger or consolidation' as a strategy for maintaining financial strength and the effectiveness of services provided to members. Of course, not all combinations of cooperatives are economically worthwhile, and some members might be apprehensive that consolidating into a much larger cooperative may weaken their control over the quality and kinds of services offered. From the moment the issue of merging is first raised, numerous questions arise. When cooperatives pursue the idea of a combination in earnest, the questions become increasingly complicated. The complexity of combining cooperatives often requires an extended period of time from the inception of the idea to its completion. The process usually moves through three phases: planning, negotiation, and implementation.\*

A key question must be answered before extensive planning and negotiating take place: what is the estimated net gain after all costs and disadvantages of combining operations have been considered? A merger study is designed to answer this question.

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<sup>1</sup> Business combinations are often discussed as following one of three paths. In merger, one cooperative is absorbed by another, which retains its corporate identity. In a consolidation, a new cooperative is formed and both of the existing cooperatives disappear. Or, one cooperative may purchase or acquire all of the assets of the other without formal combination of any aspect of the two organizations. Which path to follow is one of the many decisions that need to be made during the merger/consolidation process. This report uses the terms "merger" and "consolidation" interchangeably to refer to any organizational combination of cooperatives.

<sup>2</sup> The entire process of merging in terms of the three phases is described in Merging Cooperatives: Planning, Negotiating, Implementing, by Bruce L. Swanson, USDA, ACS Research Report 43, 1985.

Studies of this kind are carried out either internally by the participating organizations or by an outside source such as private consultants or USDA's Cooperative Services.

A merger study is the central task of the planning phase. If results are positive, planning continues. Each participating cooperative appoints representatives from its board of directors to a joint merger planning and negotiating committee. While planning is continual, a distinct negotiation phase is necessary to harmonize ideas about merging and to develop a plan that is acceptable to all participating cooperatives.

The planning and negotiation phases determine what actions and changes must occur in the later implementation phase. Viewing the combining of organizations as a process in three distinct phases helps participants to understand the overall direction and time frame of their task, but planning, negotiation, and implementation -as activities- occur throughout.

Implementation is not just a matter of carrying out the details of an agreement. This phase begins before members vote on a merger/consolidation plan. Members must be informed about the plans and justifications for proposed actions. If approved, plan implementation proceeds by contracting with various professionals for carrying out official preparations and certain legally required actions. The last special section of this report is devoted to the roles professionals play and the advantages of selecting neutral advisors, those having no client relationships with any of the participating cooperatives. Several issues and tasks associated with the implementation phase are outlined in appendix A.

Some facets of implementation extend well beyond the official starting date of a combined cooperative, such as the phasing in of operational adjustments. Overlooking one facet of implementation can be detrimental to a newly combined organization. Specifically, management and the board should continue the process of melding the different cooperative cultures. Otherwise,

different operating philosophies of the participating organizations will inhibit a new cooperative from achieving a consistent and unified direction.

### ***Major Steps and Approval Stages***

Members and employees of cooperatives are often concerned about the approval process, or when and how major decisions are made. Applicable State law or the bylaws of each organization may specify certain procedures to follow in approving mergers. Figure 1 provides a more specific breakdown of the three phases in the merger process, showing a typical pattern of major decision and approval steps.

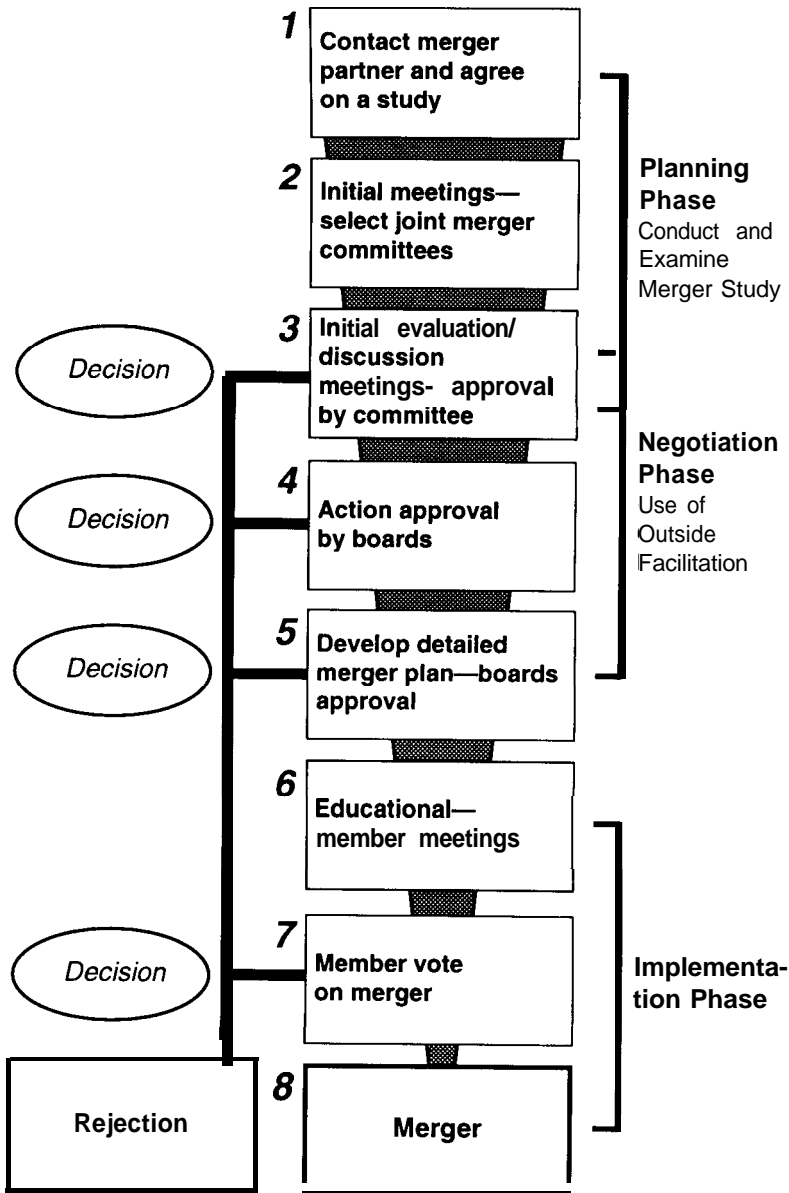
In Step 1, potential participants initiate contacts and decide to proceed with an initial merger study. The crux of a study is to estimate a net gain from merging. If the gain is significant, it becomes a benchmark value which all parties to the negotiation would sacrifice, or “leave on the table,” if they fail to reach an agreement.

In Step 2, a merger committee is formed from representatives from each cooperative’s board. The committee works with the managers to develop a merger plan. Their work comprises the negotiation phase of decision and approval (Steps 3-5).

A detailed and specific timetable should be established indicating a completion date for each step outlined in figure 1. Deadlines keep negotiations from becoming prolonged. In contrast, it is worthwhile to give ample time for Steps 6-8 in the implementation phase. Some of the implementation steps may require more time, such as providing adequate information when a cooperative has a large membership (Step 6).

If a merger is approved, the implementation phase continues beyond Step 8. Organizational restructuring and adjustments in operations are carried out. Appendix A shows some of the issues and steps during the implementation phase.

Figure 1— Steps in a Merger/Consolidation





## Why Feasible Combinations Get Rejected

Many merger studies of cooperatives show a potential for net gain, but lack sufficient member support. Scant information is available about rejected merger or consolidation projects. The aggregate potential advantage forgone by not implementing feasible mergers of U.S. farmer cooperatives is unknown but would probably be quite significant.

Consolidations are usually more difficult to negotiate than mergers, especially when merging a financially weaker organization into a stronger one. The surviving cooperative holds most of the bargaining chips. The weaker organization has little room to negotiate. When the economic strength and value of the cooperative to be merged is closer to that of the surviving organization, its merger committee and directors possess significant, if not equal, bargaining power. Merger negotiations in these situations face the same pressures for making tradeoffs and compromises as in consolidation talks.

Acquisitions and mergers occur more often than consolidations. USDA's Cooperative Services survey of cooperative combinations shows, for example, that in 1993 there were at least 50 mergers and 8 acquisitions, but no consolidations. In 1994, there were at least 42 mergers, 18 acquisitions, and 4 consolidations.

The relative infrequency of successful consolidations may result from there being more attempts to combine cooperatives by merger and acquisition. Attempts to consolidate may possibly be about as frequent but have a much lower rate of success. Either way, the infrequency of consolidations reflects the greater difficulty of negotiating when the bargaining strength of participants is comparable. Nevertheless, whether proposed as consolidations, mergers, or acquisitions, there are always many challenges to negotiating an agreement.

Some cooperatives report having visited the consolidation issue at several points in their histories. Only after one of the partners falls into economic hardship is a merger or acquisition implemented. At this point there is little or nothing to negotiate. The process of cooperative combinations has the appearance of a wait-

ing game. Each organization with a history of failed consolidation negotiations waits for the other to falter. Once a cooperative exhausts its staying power, a merger or acquisition can be put together with minimum negotiation. But such waiting games significantly waste cooperative resources and diminish future growth potential.

Most aspects of a proposed combination are considered in very general terms in a feasibility study. As plans and compromises are negotiated in more concrete terms and specific detail, merger committee members reevaluate the estimated net gains of combining. The drawback to this way of reevaluating is that costs and disadvantages of various specific proposals within these compromises are out of context from the total picture.

Negotiators often try to make decisions with multiple sources of information that lack integration into the whole picture. When information is fragmented in this way, negotiators tend to give too much weight to disadvantages and too little to the offsetting advantages. A third-party analyst who can address questions or issues that may emerge during negotiations is seldom present at merger talks. In these situations, a facilitator can pull various factors and concerns into an integrated decision-making framework and offer outside analysis of issues as the need arises. Yet, in most cooperative merger/consolidation talks, the services of an outside analyst and facilitator are limited to the feasibility study, leaving the participating cooperatives on their own to navigate through the difficult waters of a negotiation.

This report highlights the negotiation phase to describe the services of an outside facilitator. Even if one is not used, negotiations can be greatly improved by following some specific guidelines in conducting talks.

## **Guidelines for Negotiators**

Although the circumstances of any particular negotiation are apt to vary significantly, a few key points can generally help the process run smoothly and effectively.

### ***Develop Producer-To-Producer Contact***

Experience shows that durable progress in consolidation or merger talks requires directors to be the leaders in the discussion and planning sessions. A joint merger committee should formally consist of directors. Managers serve as advisors and provide information as experts in operations and the industry. Committee members will usually seek the opinions and judgement of managers of their cooperatives on important decisions. But, the board should not permit managers to exercise excessive influence over the progress and direction of talks.

A merger committee of producers from different cooperatives should have ample opportunity to get to know one another and to develop trust. Discussions that are primarily farmer to farmer, i.e., director to director, are more conducive to reaching a merger or consolidation agreement. Although committee members represent different cooperatives, and in some cases different regions of the United States, they share a common experience and vantage point as farmers.

### ***Follow a Strategic Plan***

Before a merger committee convenes, it should develop a strategic plan that sets out major objectives. For example, increased economic efficiency of the cooperative is usually a major objective of mergers and consolidations. As negotiating progresses, the committee will face numerous difficult decisions and trade-offs. A strategic plan provides criteria for making hard decisions. Efficiency-related objectives specified in a strategic plan help the committee give adequate weight to choices that will “increase the economic pie” and prevent contentious “pie sharing” issues from derailing the process.

The distinct roles of directors and management are particularly clear in strategic planning. Directors are responsible for developing a strategic plan and defining the vision for a new organization. The joint merger committee is charged with developing a consensus plan. Management’s role is to advise on feasibility and to carry out the agreement.

### ***Joint Committee's Role***

A joint merger committee attempts to reach consensus about how to combine their cooperatives. Most consensus proposals are a product of give-and-take debate and contain various compromises and tradeoffs. It is important to keep the detailed work of a joint committee independent from pressures of management, employees, fellow board members, and the membership at large. Negotiations may be derailed if committee members bring non-negotiable mandates from their staffs, boards, or membership districts to the discussion table. Reasonable and fair solutions emerge only from open and honest discussions by an appointed joint committee.

### ***Make All Positions, Opinions, and Concerns Known***

Directors must be open and up-front with their concerns so that a committee will develop trust and make sincere efforts to reach an agreement. Holding back or keeping hidden agendas might make initial meetings easier but may inadvertently undermine trust at later stages of negotiation. Issues of concern and strong positions of directors must be communicated. A round-robin forum, in which each director and manager voices his/her concerns and priorities, is a good way to accomplish this.

### ***Maintain Objectivity and Work Toward Solution***

Once concerns are known, they must be resolved. Directors must avidly seek solutions and maintain objectivity. They must focus on the future and set aside differences, pride, and emotions as they discuss and negotiate sensitive issues. Instead of moving to a hard bargaining position in consolidation/merger talks, directors should view the entire process as a joint problem-solving endeavor.

### ***Use the Word "WE"***

Directors must focus on using the word "we" during discussions. They must avoid employing protective "card playing" traits and getting caught up in a game of who is coming to the table

with the most to offer. Usually, each cooperative brings “value” to a potential combination. It is important to avoid arguing about who is offering or contributing the most. While cooperative directors must protect the assets and operations with which they are entrusted by members, they must also keep an open mind while creating a new, unified cooperative.

### ***Establish a Definite Timeframe***

All parties need adequate time to think through and grasp all the various impacts of different proposals. Conversely, too much time or continuous postponements usually offer little benefit and often have negative consequences. A cut-off date should be set once the initial study is complete and a merger committee begins its discussions. If an agreement cannot be reached by that date, both sides should then be able to amicably withdraw from the negotiations with an attitude of keeping the channels of communication open for a renewal of discussions at a later date.

Deadlines help prevent procrastination. They take on an even greater importance in merger discussions. When negotiations become too prolonged, the participants might be avoiding difficult decisions or hoping their terms will somehow eventually be accepted by the other side. In fact, the prolonging of merger negotiations often elicits ill will, increases the odds of failure and diminishes the prospects for future renewal of talks.

### **Facilitator’s Role**

Cooperative mergers and consolidations can capture substantial savings and improved positioning within the industry. But this requires the willingness of the involved organizations to make difficult tradeoffs and sacrifices that are reciprocating and fair. Merger participants have a natural tendency to overvalue what they are asked to give up and to undervalue concessions the other side is making in return. This may result from taking too narrow a view of the issues. An impartial facilitator can reframe the issues in ways that open channels of communication and pro-

vide a better understanding of the tradeoffs. The very presence of an outside and independent point of view helps reduce frictions and uncertainties. An outside facilitator can also be an unbiased source of information in a process sometimes fraught with complexities and unanticipated risks.

Before negotiations start, an appointed facilitator conducts separate interviews with management and a committee representative from each of the participating cooperatives. If the facilitator has been involved with the planning phase, particularly in preparing the feasibility study, then the interviews will be expedited. These preparatory interviews enable a facilitator to spot various points of potential disagreement and to identify potential openings for reaching agreement.

Although any facilitator or mediator has less direct and concrete understanding than the participants about what is at stake, private meetings with all involved parties enable them to develop a broader understanding of the issues. Their perspective is particularly useful in helping a committee develop an agenda. A facilitator can assess when those issues that committee members want to have immediately resolved would be more appropriately held for later discussion, so that less controversial items could be advanced on the agenda. By meeting separately with the participants, a facilitator learns what views the participants share and how they can become a basis for resolving some of the potentially difficult issues.

### ***Differences From Mediation***

Facilitation is similar to mediation, but has some important differences. Facilitation is less controlling than mediation in that it assists talks by fostering a teamwork approach, rather than focusing on mediating proposals and counter-proposals between the parties.

Resolving disagreements over how to combine cooperatives is far different than negotiations handled through mediated conflict resolution. In a cooperative merger discussion, there is typically neither conflict nor any requirement to reach an agreement.

In contrast to a mediator, a facilitator is on the sidelines and not in the middle of a negotiation. Mediators sometimes conduct most of the communications between parties and take a lead role in developing a compromise agreement. In fact, some mediated negotiations do not even involve face-to-face meetings of the involved parties.

Face-to-face discussions are essential for cooperatives negotiating a merger/consolidation because they are doing more than just searching for ways to resolve conflicting points of view. The negotiation process is in part a testing ground to see if the members of the participating cooperatives can effectively work together and develop trust. Should a consolidation be carried out, a cohesive organization would result. The less intrusive role of a facilitator respects the integrity of this process.

### ***Extent of Formality and Procedure***

Cooperative negotiations on mergers/consolidations need not be conducted in the formal manner of rule-making bodies. Negotiations are more likely to make progress in informal and open discussion. When participants prefer parliamentary procedure, a facilitator can outline appropriate rules and offer to chair meetings accordingly.

When cooperatives negotiate a combination, there are more factors involved than just producing a consensus plan. Participants are exploring the possibility of long-term working relationships. Brainstorming and teamwork approaches are conducive to resolving different viewpoints and concerns. Merger committee meetings are initially exploratory, so a formal structure to these talks may inhibit the free flow of ideas. As the committee moves into the phase of developing a merger plan, members should not feel constrained in expressing their opinions and comments. Decisions of a merger committee are preliminary and not binding. Therefore, open and creative discussions should be encouraged.

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A facilitator usually chairs merger discussion meetings. This allows all merger committee members to devote their full attention to discussions. As chair, a facilitator ensures that the agenda is followed and items are addressed in the allotted time.

Merger committees usually have only 6 to 10 participants, so discussions should flow freely. But participants should respect the basic norm of taking turns. For example, when a question or concern is raised about particular policies or actions of a participating cooperative, no further queries should be raised until a representative of the organization in question has had an opportunity to respond.

### ***Use Transcripts of Previous Sessions***

It is important to have a written record of each meeting to document the progress of talks. A facilitator does not take minutes, so either a recording device or transcriber should be used. When this is not possible, a facilitator can summarize key points. In fact, facilitators usually summarize the progress of talks when a new session begins. However, it should be noted that their summaries are not the same as the official minutes. Facilitators' notes may include observations about overall direction of the talks and suggestions for resolving differences.

A transcript of earlier meetings is used in preparing for the next round of talks. A facilitator and committee members can reinforce their understanding of the extent of progress and develop more insight about the viewpoints of others in order to help resolve remaining issues on the agenda. Both the facilitator and committee participants should carefully review the transcripts and correct any potential errors or omissions of important statements.

### ***Analyzing Emerging Issues***

A facilitator of farmer cooperative merger discussions should be well versed in cooperative principles and practices, as well as in economic analysis. During negotiations, many new issues emerge, and negotiators need to know the impact of alter-



native methods or policies for resolving them. For example, negotiators might be concerned about fairness when their organization has lower debt or differences in equity or in its revolvment. If a facilitator can demonstrate alternative ways to reduce these differences or show how certain economic factors of a potential consolidation would offset imbalances between the cooperatives, the odds on resolving differences are greatly increased.

A facilitator is often asked to comment on or offer suggestions about proposals during merger discussions. These comments or suggestions can be helpful, particularly when talks run into roadblocks. In the early stages of talks, a committee should try to reach agreements with as little outside help as possible. A facilitator must be very circumspect in his or her comments or suggestions, and in the early stages of a negotiation, will want to be very general and brief.

### ***Priority of Reaching Agreement***

The extent to which negotiating parties are willing to make tradeoffs and develop new approaches is largely determined by their need to reach an agreement. The net gain estimated in a merger study is a major reference point, particularly when it forms the basis for future economic solvency of cooperatives. When participating cooperatives are confident about their future stability and solvency without a combination, the need to reach an agreement will be less critical.

When reaching an agreement on merger/consolidation has a very high priority, but efforts to achieve it remain illusive, a facilitator may act more like a mediator by developing compromise solutions for the negotiators to use as a point of reference. However, even when reaching an agreement is a high priority and directors are fully committed to merger/consolidation, negotiations may still deadlock on certain issues.

Many negotiations break off **when a** deadlock on an issue(s) cannot be resolved. Deadlocks can arise for a variety of reasons. A breakdown in talks is preferable when there are significant opportunities to accomplish more efficient restructuring in the near

future. Other deadlocked negotiations may only involve perceptions of fairness or the need to save face because participants do not want to be responsible for making decisions that involve emotional attachments or seem to compromise their loyalties. These cases are unfortunate because the issue in dispute is usually of much lesser value to all participants than the net gain from reaching an agreement. In such cases, an alternative to breaking off talks is to seek outside opinions by experts or even to arrange for a binding decision from an outside expert who has examined the situation. This type of service is outside the scope of a facilitator and should be arranged with a different professional adviser.

### **Using Professional Advisers**

Use of a facilitator does not eliminate the need to involve accounting, financial, and legal experts in the merger process. But the facilitator can help assure that these people remain in their proper role as consultants.

One of the first steps in a merger is to evaluate the assets and liabilities of each association. Accountants can examine the financial records of the merging cooperatives and answer any questions about them. An accounting and recordkeeping system will also be needed for the merged association.

Sometimes the actual value of assets and liabilities will differ substantially from their posted book value. Financial professionals may need to appraise these items. They can also be useful in forecasting the equity and debt capital needs of the new venture and devising methods, including arranging lines of credit, to make sure the new cooperative is adequately capitalized.

Legal assistance will be required throughout the process. First, both State incorporation laws and the organizational documents may contain passages concerning mergers. Each cooperative involved will have to comply with all procedural requirements that apply to it (and they may differ in important ways), or else the merger will be subject to subsequent legal challenge. Depending on State law and the type of merger plan used, articles

of incorporation and bylaws will have to be reviewed, amendments drafted, or entirely new documents prepared. The same applies to other legal documents such as contracts and marketing agreements.

A facilitator can help the merger committee avoid some common pitfalls in using professional advisers. One is to avoid being overawed by them or letting them dominate the entire process. While special attention should be paid to their opinions and recommendations in their respective areas of expertise, basic decisions on how to organize and operate the venture are the responsibility of the producer-directors. This duty should not be relinquished to outsiders.

The second pitfall is to forget that frequently these advisers have their own interests to protect. Unless the merging associations use the same accounting firm, lender, and law firm, these parties face the potential loss of a valuable client. While their professional opinions are likely to be ethically sound, their general observations—even their overall attitude toward the merger—may be influenced by their perception of whether it will result in more or less business for them.

CS experience in facilitation suggests that when different firms are providing these services to the merger participants, a single entity should be selected to work with the merger committee. Furthermore, a third firm should be selected to serve the merger effort, one that has no client relationship with the participating cooperatives. This may require some time and expense to educate the new adviser on the unique aspects of the parties. But it can also minimize the possibility of the atmosphere being poisoned by dueling experts.

Of course, the parties will be free to consult their own advisers at any time. The facilitator can be available to attend these sessions as the parties wish and make sure that during the merger committee meetings the focus remains on the members and their future needs and opportunities.

## **Contacting Cooperative Services**

USDA's Cooperative Services (CS) provides merger/consolidation feasibility studies and facilitation of merger/consolidation committee discussions among cooperatives. For more information on how to request these services, call (202) 720-7558.

## **Appendix A.**

### **Issues To Consider in a Cooperative Merger**

Here is a partial checklist of some of the organizational and operational issues the merger committee might have to consider. Each proposed merger has its own unique aspects to be reviewed and decided.

- I. General Issues.
  - A. Name.
  - B. Composition of the board of directors.
  - C. Selection of the accountant, lender, attorney.
  
- II. Personnel Issues.
  - A. Selection of the manager.
  - B. Staff realignments, hirings, firings.
  - C. Salary structure, pension plan merger, and other employee benefit issues, job descriptions, performance review procedures.
  - D. Labor negotiations.
  
- III. Member Issues.
  - A. Voting rights.
  - B. Membership composition - actively recruit, keep current status, restrictive qualifications.
  - C. Commitment to support merged cooperative.
  - D. Dissenters' rights.
  
- IV Finance Issues.
  - A. Facility closures, retentions, additions, replacements.
  - B. Valuation of assets.
  - C. Combining allocated equities.
  - D. Combining unallocated equities.
  - E. Equity redemption plan.
  - F. Combining accounting systems.
  - G. Computer compatibility.

- H. Combining lease agreements, loan agreements,  
insurance.
- I. Pending litigation.
- J. Due diligence.