Merging or acquiring another UK business? Have you considered the risks?

Companies of all sizes often consider merging or acquiring another business for many reasons. However, what often can be overlooked are the risks involved in undertaking such an exercise.

The importance of careful planning, due diligence and management of a merger cannot be stressed enough. The time spent on conducting due diligence and planning to ensure that all potential risks have been identified will be time well spent.

Insurers will want to know that such action has been taken and that law firms have carried out the appropriate due diligence, focusing on the risks they are taking on as much as the financial benefit of the potential merger.

Ensuring that the target firm is a good cultural fit is just one part of the process but equally as important is the need for law firms to understand the risks of the liabilities they may be taking on. To assist with understanding such risks, the claims history of the target firm needs to be examined thoroughly. All current and past liabilities of the target firm will pass to the merged firm (unless a separate run off policy is purchased which can cost as much as three times the annual premium). It is recommended that the claims history going back six years is reviewed, including any prior practices within the target firm. Analysing the claims history should not be rushed, the policy is a claims made policy.

It is essential that the true nature and extent of the existing claims are identified and understood, so that preventative measures can be implemented to stop such claims arising once the merger has taken place. Law firms must also understand the rules around successor practice.

It is important that the target firm has carried out its own internal investigation to ensure that all circumstances that may give rise to a claim have been notified to its insurers. Remember, there is a risk that any failure to notify a circumstance or a claim prior to the merger may result in disputes around coverage, as the ongoing insurer may refuse cover on the grounds of a late notification.

It is recommended that the SRA is notified about the potential merger and checks are carried out to establish whether any individuals at the target firm are the subject of any disciplinary proceedings.

In addition to assessing the risks from claims, identifying potential conflicts, both legal and business conflicts needs to be explored. Compliance with the SRA Code of Conduct 2011 and SRA Accounts Rules 2011 must also be considered.

The financial information needs to be reviewed including liabilities and debts and obligations to HM Treasury. On a practical point, how client account monies will be transferred over to the merged firm needs to be dealt with to ensure that there are no deficiencies.

Another area that must be taken into consideration is whether there is any outstanding litigation against the target firm, their principals and staff. In addition, what will happen to the staff following the merger, have the terms of employment been reviewed and agreed?

How will the information be transferred to the merged firm? Consideration needs to be given to client care letters being sent to existing clients to notify them of the existing merger. What is happening with the IT infrastructure? Has a data protection impact assessment been carried out to ensure that all personal data is protected at all times during the merger?

From a housekeeping perspective, storage of archived files and who will have ownership once the target firm closes should be considered.

All these factors and more must be taken into consideration as part of the merger process.

As mentioned at the outset, thorough planning, due diligence and good management of the merger process, whilst it may seem time consuming and costly at the time will be beneficial in the long run as such measures will ultimately result in an successful merger.

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