

A merger of convenience

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By Pamela Ryckman

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NetAid was already flagging when Doug Arthur joined the board. The non-profit, which used the internet to mobilise American youth to alleviate poverty, was founded with a \$20m grant, but its large staff and expensive Manhattan headquarters were a drain on the institution, and board members struggled to find sustainable funding. "We were burning through cash quickly. There was a lot of commotion, not much motion," he says.

By the time Mr Arthur, a former Morgan Stanley managing director now working at a hedge fund, became board president, NetAid's best option was a merger. Toward the end of last year, NetAid took steps to make itself an attractive partner; it narrowed focus, cut staff, closed field operations and used its remaining \$3m endowment to rally interest from other organisations.

"We didn't want to go on the market as a completely broken-down engine," Mr Arthur says. "It came down to dollars and cents. We could daydream all we wanted about the mission, but if we didn't have money it was moot."

NetAid approached Mercy Corps, a global leader in humanitarian relief, and the two organisations appeared compatible. NetAid brought technological prowess and an ability to engage young people, as well as a downtown foothold that proved valuable to Portland, Oregon-based Mercy Corps, which had recently won a contract to develop its World Hunger Action Center in Lower Manhattan.

NetAid and Mercy Corps collaborated to unite staff and safeguard NetAid's vision. "We couldn't just wash our hands once the deal was signed," Mr Arthur says. "We need to keep following up to make sure NetAid isn't just swallowed and dissipated."

Mergers like this have become more common as the number of non-profits has exploded, intensifying competition for funding.

Even the record \$295bn donated to charity last year was not enough to keep them all in business. At the same time, savvy board members and professionally trained executive directors striving for corporate standards of efficiency and fiscal health have sought to maximise return on donors' investments through strategic partnerships.

Non-profits such as University Settlement, which provides social services to immigrants and low-income families on Manhattan's Lower East Side, have improved operations by combining administrative functions and sharing facilities with other groups while keeping their brands and programmes discrete.

Seven years ago, Michael Zisser, University Settlement's executive director, presided over the creation of a parent-subsidiary relationship with The Door, a youth services non-profit in the same neighbourhood that had strong name-recognition but was financially unstable. The Door needed money to keep its services running, while University Settlement wanted to connect with young people and saw the advantage of expanding.

Mr Zisser, who was on the board of The Door, assumed the role of executive director for both organisations and consolidated the human resources, finance, technology, and fund-raising departments, but left their programmes, cultures, and boards largely intact. "I sensed from the beginning that we'd be better off financially and programmatically. Our mission would be expanded and we'd be seen as a stronger institution," he says. Since 2000, The Door's revenue has more than doubled, from \$5m to \$11m, while University Settlement's revenue has risen from less than \$10m to \$16m.

Less than two years ago, University Settlement agreed to jointly own and operate a new \$14m community centre with the Chinatown YMCA. "The developer and the city asked us to create a forced marriage of organisations with different missions and economic models, but this facility is actually stronger because the two of us are there," Mr Zisser says. The non-profits share time in the centre, and University Settlement has extended subsidised space rentals to 180 different community groups. "For an underserved neighbourhood with minimal social infrastructure, the answer is for non-profits either to merge or figure out strategic alliances," he adds.

The NetAid and University Settlement mergers bear witness to a trend noted by David La Piana, president and founder of La Piana Associates, a California-based non-profit consulting firm. "Ten years ago, there were a lot of [non-profits] with financial problems that were looking for a bailout. What we've seen evolve is a much more strategic approach," says Mr La Piana, a former executive director who has facilitated more than 100 non-profit mergers. Alliances, mergers and strategic restructuring now account for one third of his firm's business.

Similarly, Sandy Lamb, a former Lazard Freres managing director, who brought 20 years of mergers and acquisitions acumen to the non-profit community when she founded Lamb Advisors in 2003, says non-profits should consider these unions before descending into financial crisis. "If the 'seller' is already troubled, it's probably too late. Their brand equity is likely gone and they're headed for a liquidation," she says. Ms Lamb's clients tend to be prescient and proactive executive directors and board members who identify funding or managerial concerns on the horizon.

"People who run non-profits are starting to think like people who run businesses," Mr Zisser says.

Generally, when organisations have complementary missions, they will attempt a strategic alliance, while competing organisations with identical goals tend to merge. Ms Lamb says the process to combine non-profits is similar to a for-profit merger, but the transaction's structure is more flexible. Valuation is more art than science. Because no market exists to determine the worth of non-profit "businesses", Ms Lamb relies on "intangibles". She works with the executive director and the board of an ailing agency to determine their priorities and the things they aim to preserve; this may be the non-profit's original mission, a brand name, a location, a particular grant, or the potential to retain seats on the board of the new, conjoined organisation.

Mr La Piana stresses the difference in attitude inherent in a non-profit joint venture. "You can't 'acquire' anything and there are no hostile takeovers, so even when a group is much smaller you have to treat them fairly and with respect or they'll just say no."

Still, Mr La Piana attests to a decade-long increase in non-profit mergers, culminating in a dramatic spike over the past two years. Many expect further consolidation as agencies try to broaden impact ahead of a possible recession. "There's now an emphasis on business functions – personnel, legal issues, fund-raising, economic modelling," Mr Zisser says. "A merger is one way to get stronger financing, better measures. I think we'll see this even more as new leadership and board members become familiar with, not fearful of, the language of M&A."

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