NonProfit PRO

How Nonprofits Can Use a Merger or Acquisition to Further Their Missions

By Frank Williamson

Nonprofits are often founded with a single-minded mission by an individual or a small, well-intentioned group of people. Some of these organizations grow in scale and influence, many others start out modestly sized and stay that way — and a full 30% fail within the first 10 years.

The pandemic has added to the financial strain for for-profit businesses and charitable organizations alike, as what used to look certain about future levels of revenue was suddenly no longer guaranteed.

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For many nonprofits, their three main sources of income — the sale of goods or services, grants and donations — were negatively affected by the unstable economy. Now, as the latest wave of COVID-19 continues to spread, many organizations are contemplating what the future holds, and whether they can survive another difficult economic stretch.

So, how do you maintain your organization's financial health and sustainability when your main source (or sources) of revenue are diminished or cut off entirely? The first step is taking a deep dive into your expenses and analyzing where you can make cuts. How much revenue do you expect to bring in this quarter and this year, and how can you ensure your operational costs don't exceed that number? Every area of an organization should be flexible in how it operates, and be open to the idea of altering and improving its offerings.

Sometimes, though, operating sustainably isn't possible with budget cuts alone, and that's when leadership should consider merging with another like-minded, purpose-driven organization. That could mean a fellow nonprofit, but it could also mean a for-profit company that does (or has a division that does) similar work to your organization.

Positives of a Successful Merger

Once you've identified a partner whose mission and culture align with yours, ask yourself this question: Can our two organizations be more effective by combining?

"More effective" isn't necessarily quantifiable, so use these metrics to determine whether or not a merger is the right step forward:

Will you spend money more efficiently? When cash flowing into an organization is low, it's obviously imperative to decrease the amount flowing out. There are certain overhead costs — accounting systems, human resources, office space, etc. — that can be easily reduced by combining two companies into one.

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Will you add new skills or aptitudes in a more effective way than hiring? Sometimes adding new skills to your organization can be achieved by hiring one or two experts in a certain field. However, it's an entirely different upgrade when you bring in a whole organization that complements and improves the work you're already doing. By expanding your skill set, you're ultimately expanding the organization's offerings and value.

Will you magnify your social impact? In the end, charitable organizations exist to further a specific cause, so it's important that your merger is completed with the same goal in mind.

Complexities of a Merger

As with every business transaction, there are complexities that come with merging two organizations. Being aware of them on the front end will allow leaders to address the issues before they become problems. Here are a couple of challenges to be mindful of before and during a merger:

Passionate leaders. Often, charitable organizations are built around the vision of a single, charismatic person who cares deeply about a particular cause. It's part of what makes those nonprofits successful, but it can also make it challenging to combine two organizations with highly driven leaders. In the end, both leaders need to agree that their impact on society would be greater together than it would be separately. To avoid conflict, the two leaders can work in complementary roles in the new combined organization, or one may decide it's time to step down.

No outside owner to make decisions. Unlike for-profit businesses, charitable organizations are not owned by any person or group of people, so there's no one to pay money to in exchange for control of the organization. With that in mind, each organization must convince the other's leaders and trustees — those with the legal and fiduciary responsibilities of the organization — that the transaction is a good idea. Because there is typically no exchange of money during a nonprofit merger, using "a higher price for the seller" as a persuasion tool is off the table. Instead, the organizations must convince each other that the transaction will enable both parties to advance their missions more effectively than they could independently.

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Two Examples of Favorable Mergers

One buy-side client was a well-funded nonprofit looking to grow, but in its particular industry, which includes government contracting, winning a new business is relatively challenging. Meanwhile, a small company serving the same clients became available; the owner was an entrepreneur who was planning for retirement. The nonprofit offered her a reasonable sum of money and created a prominent role for her in the combined organization. The buyer justified the investment by comparing the financial and mission impact of this transaction to what it could accomplish within its endowment. By merging, the two organizations became a much bigger player in their industry, allowing them to apply more effectively for contracts and accelerating their mission. The entrepreneur, on the other hand, was persuaded by the satisfactory, ongoing business relationship to combine her company with the nonprofit.

On the other hand, a sell-side client had received an offer for its business from a for-profit business. The management and board had to examine the organization's sustainability and current social impact, and compare that with its potential under new ownership and the ways it could further its mission using the deal proceeds. This organization faced the rare opportunity to declare victory in one chapter of pursuing its mission, while starting an entirely new chapter.

In the end, charitable organizations operate very similarly to for-profit businesses — and, in good times and bad, the goal for both is to operate sustainably so that today's service to stakeholders will continue tomorrow. If your organization is struggling to make ends meet or navigate a changing world, consider a merger or acquisition to continue achieving your mission with more tools in your belt.

Frank Williamson is the founder of Oaklyn Consulting, a consulting firm that helps investor groups and private businesses, from startup to middle market, with mergers, acquisitions, capital-raising, investor relations, succession and other strategic corporate finance decisions. Oaklyn Consulting does not work as a broker but as an extension of clients' boards and management teams, charging time-based fees for investment banking advice.