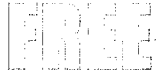


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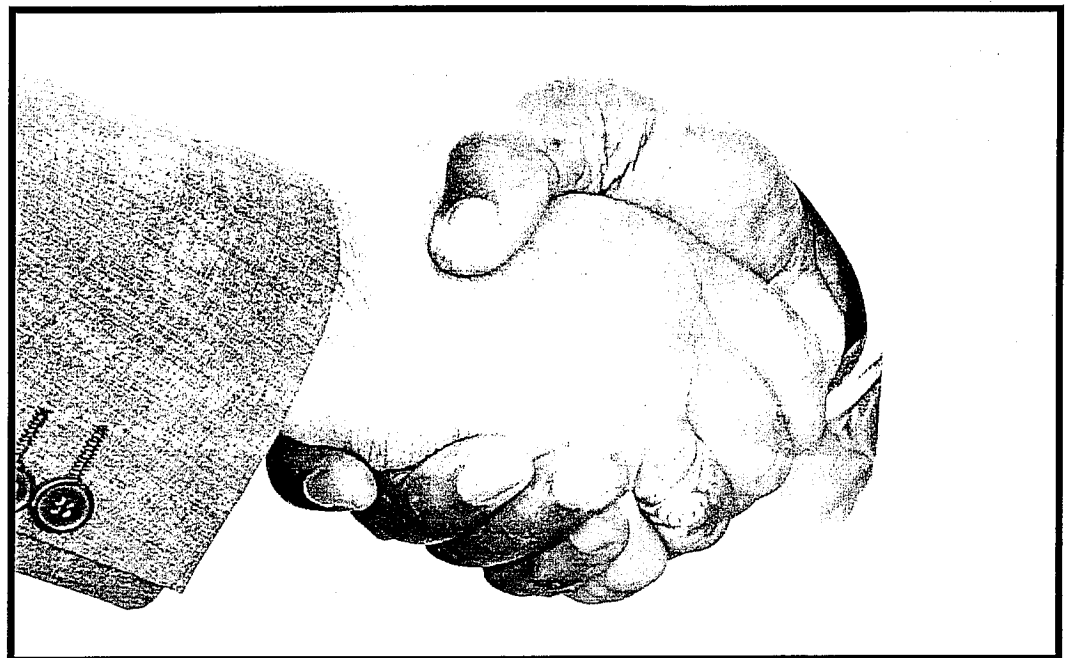
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MERGERS

Nonprofits Getting Together



by Fred Scaglione

What can take many different forms and strikes fear into the hearts of men and women throughout the nonprofit sector? No, it's not the Devil. It's a merger!

Mergers, it seems, are those dreaded forced marriages between two nonprofits. One is small and weak, but mission-driven; community-based and high quality with a dedicated staff of committed, underpaid professionals; innovative and pioneering, even historic. The other is large, powerful and aggressive; well-funded, evidence-based, outcome-focused, and, yes, corporate. Mergers

are imposed upon us by government officials, foundation program officers, performance contracting, Medicaid reimbursement and Republicans. Mergers are an infectious disease spawned in the world of business along with their evil twin – "Acquisitions". Yes, the mere mention of the word "merger" can get people upset.

While this caricature may be a little outdated, there is no question that the prospect of a merger still is unsettling to those involved. Mergers are a threat to the world as we know it; or at least the world where we make our living and find our professional identify.

Yet, mergers are often the only way that

many struggling programs – which usually are both weaker than we imagine and a little less excellent than we wish to believe – can survive. In fact, mergers may be the vehicle by which these programs can receive the financial and administrative support necessary to achieve true excellence. Be all you can be, merge!

Mergers have become a pretty hot topic in nonprofit circles in recent years. They have been touted as a cure for the apparently cancerous growth in the number of 501c3s as well as the much hyped future shortage

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of executive directors to lead them. Mergers are a mainstay panel topic at many nonprofit sector conferences and several foundations are sponsoring targeted workshops on the topic of Strategic Restructuring. Everybody is talking about mergers. Some people are even doing them.

"We currently are working on six different alliances between nonprofit corporations in New York City," said Linda S. Manley, Legal Director at Lawyer's Alliance for New York (LANY). "I would say we maintain a pretty constant diet at that level. As soon as one ends; another walks in the door."

At this pace, it doesn't take long to put together a fairly extensive list of nonprofits that have joined together organizationally in common pursuit of their missions. "I have been at Lawyer's Alliance for ten years, so I have probably worked on about 60 of these," says Manley. The Dyson Foundation has made a total of 15 grants over the past few years in support of organizational restructuring throughout the Hudson Valley.

As a result, there are a lot of merger case studies in which to look for patterns and find valuable lessons learned. In preparing

this article, we've spoken to a participants on both sides of several mergers – some recent and some not so recent – to learn just a little about how they came about, how to get through them and the various forms they can take.

A "Merger" by Any Other Name...

A "merger" can take a variety of forms. In many, if not most cases, it may not even be a "merger."

In May, the Center for Nonprofit Strategy and Management at Baruch College's School of Public Affairs hosted a panel discussion featuring case studies on two recent "mergers" between local organizations. In one case, St. Nicholas Neighborhood Preservation Corporation (St. Nicks) had come together with School Settlement Association. In the other, Goddard Riverside Community Center had established an alliance with St. Matthew's and St. Timothy's Neighborhood Center. In neither case, had there been a formal, legal merger.

"We called this seminar 'Mergers and Acquisitions in the Nonprofit Sector' to get you in the door," Jack Krauskopf, the Center's Director, told the audience. "But, it is really more about strategic alliances."

To some extent this cautious wordplay may appear designed to assuage the delicate sensibilities of those working in nonprofit human services. However, there is more than just linguistic political correctness at play.

Legally speaking, "mergers" and "consolidations" occur through a statutory process by which two or more corporations become one corporation. In a "merger" the "surviving corporation" is one of the original corporations. In a "consolidation," the two original corporations both cease to exist and a new combined corporation is formed.

There certainly are good reasons for

two nonprofit corporations to legally merge or consolidate, primarily the ability to combine property and other assets. However, there are even more reasons why nonprofits may choose a different path towards an organizational alliance. Legal mergers are extremely complicated and time consuming, requiring review by the Office of the Attorney General and approval by the New York State Supreme Court. Equally important, a merger of property and assets also means a sharing of liabilities, both current and potential. Since many, although certainly not all, nonprofit mergers are driven

St. Nicholas Neighborhood Preservation Corp.

School Settlement Association

St. Nicholas Neighborhood Preservation Corp. (St. Nicks) was formed in 1975 in response to the decline and disinvestment confronting the Williamsburg Section of Brooklyn. Over the years it has become a major community force in the areas of housing, economic development, employment training and services, health care and youth services. "We serve about 8,800 people and have a staff of about 1,200 with a budget of about \$50 million," says Executive Director Michael Rochford.

School Settlement Association traces its history in Williamsburg back to 1901. "They are a very old

institution with very deep roots in the community," says Rochford. "Their home is one of the oldest settlement houses in the City, certainly the oldest in Brooklyn."

"I thought for some time it would make a lot of sense to work together," Rochford continues. "Their focus around youth and services fit very neatly with what St. Nicks was doing at that point. There was no reason for us to compete and there was a lot of strength in the possibility of an alliance."

The strategic alliance between St. Nicks and School Settlement evolved from SSA's deepening financial problems. For fiscal year 2005, the agency had just \$182,847 in revenues and a net deficit of almost \$60,000. "Over time, we saw a decline in the capacity of School Settlement. At the point we stepped in, they were on brink of bankruptcy," says Rochford.

Key to their successful collaboration was the active involvement of a long-time SSA board member who was elected SSA chair, says Rochford. "He was the one person who was not wedded to any old animosities and rivalries that had existed.

"The SSA board wanted to keep their board in existence. They wanted to protect their staff and they wanted to keep their name. Those were their three big issues," says Rochford. "My board was concerned that by merging we would take on liabilities. We spent the next 18 months working through the issues of a few board members until we could build a consensus within both boards to go forward."

The two organizations structured a strategic alliance whereby SSA converted to a membership association with St. Nicks as the sole member with rights to appoint the SSA board. The structure has allowed SSA to maintain its identity and rebuild its organizational capacity. "By keeping the School Settlement Association name and the board, we have been able to rebuild the board," says Rochford. "We now have eight members and they are going out to raise money. Today, as of this summer we now serve 250 children in after-school at SSA – 100 on-site and another 150 off-site at a public school – as well as a teen program.

"If it were not for St. Nick's involvement, they would have closed and that would have been the end of what was a very strong and proud organization."



From L-R Michael Rochford, Executive Director, St. Nicholas Neighborhood Preservation Corporation; Assemblyman Joseph Lentol; Borough President Marty Markowitz; John D'Arizeno, Board President of School Settlement Association and Vincent Abate of School Settlement; join together to celebrate the Strategic Alliance between the two organizations and the opening of a new computer center at School Settlement. The Strategic Alliance permitted the two organizations to share resources and kept Brooklyn's oldest settlement house from closing.

Goddard Riverside

Goddard Riverside Community Center is a multi-faceted human service organization with 22 programs at 16 sites on the Upper West Side and in West Harlem. It provides services for children, youth and families; homeless people; and older adults, while also developing and managing affordable housing. The agency has a total budget of approximately \$20 million.

St. Matthews's and St. Timothy's Neighborhood Center was a small, church-sponsored settlement house on 84th Street with six programs – three day care centers, meals-on-wheels, an after-school program and a learning center. With annual revenues of approximately \$3 million, the agency was also experiencing financial pressures in the form of recurring deficits and declining assets. Between fiscal years 2000 and 2005, the agency saw its net assets drop from almost \$1.2 million to less than \$500,000.

"Someone on the board just woke up and said we can't do this any more. Let's go to Goddard," says Stephan Russo, Executive Director of Goddard Riverside.

Russo was already a believer in the quality of the agency's programs and had approached them about a possible collaboration in the past.

In the months that followed, Russo brought on a consultant team of Barbara Krasne and David LaGrecca to help facilitate and help manage the due diligence process.

"What we did first was to stop and take a step back," says Krasne. "We asked Stefan what a successful merger would mean for Goddard and what he wanted to achieve through the merger."

"We were very clear," explains Russo. "The reason we were doing this was to save these community programs."

"We talked about Goddard's organizational culture and whether or not it could really tolerate this," says Krasne.

"There was not complete organizational consensus that we should pursue this," says Russo. "Some staff at Goddard felt that it would put too great a strain on the agency. I had to deal with that and manage that internally."

In the end, however, the board remained committed to moving forward. Once again, the strategic alliance was effectuated when the St. Mathew's St. and Timothy's board voted to become a membership association with Goddard Riverside as the sole member, effectively giving over control to the Goddard board.

St. Matthew's and St. Timothy's



Stephan Russo

MERGERS

by financial problems at one of the entities, a stronger or lead agency may be reluctant to take on the debts and other liabilities of its weaker merger partner. Finally, legal mergers will generally trigger "change of control" provisions which may prevent

transfers of government contracts from one agency to another.

For these reasons, nonprofits may find alternative ways to "merge".

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Harlem United

FROST'D

Harlem United was founded in 1988 by a group of priests, religious and social workers who wanted to develop a safe space for homeless people who were active substance abusers living with HIV/AIDS. They began with a social day care model operating out of church basements. In 1992, the organization got its first contract to provide scattered site house, a program which has grown from an initial 20 units to over 400 today. In 1997, Harlem United was one of the first agencies to open a new Adult Day Healthcare Program, which it then adapted to become a support for people with multiple issues and co-morbidities in adhering to the new and complex regimens associated with anti-retroviral medication. In 2000, Harlem United took the major step of adding primary healthcare to the services it offered. Soon afterwards, it added oral health and then mental health services. The agency expanded its preventive services division, focusing on work with individuals already HIV-positive, after 2000.

The Foundation for Research on Sexually Transmitted Diseases, Inc. (FROST'D) is one of the oldest HIV/AIDS organizations and the first to really recognize that women and transgender individuals were at particular risk from the epidemic. Founded in 1984 by Dr. Joyce Wallace, FROST'D initially focused on sex workers, developing a strong capacity for outreach and HIV education. As part of this effort, the agency operates needle exchange programs at six different sites. In the late 1980s, they opened the first emergency transitional residence for people with AIDS - Foundation House. A second residence - Foundation House North came later.

Like Harlem United, FROST'D understood the need to provide primary health-care for its clients and opened a program of its own. "Primary care is a money-losing operation and ours was operating on an impossibly small scale," says Josh Sippen who became executive director at FROST'D in 2003. Sippen and the board undertook a strategic planning process which culminated in a decision to close the primary care program. The strategic planning effort also raised questions about the long term viability of a small \$4 million agency without connections to primary health care in the increasingly medicalized environment of HIV/AIDS services. "There was no immediate financial crisis," says Sippen. "But we were concerned about our ability to maintain funding levels over the longer term. We decided to look for a partner."

"For us, FROST'D was appealing because they were operating needle exchange sites," says Patrick McGovern, Executive Director at Harlem United. "Those waivers are very difficult to get. We had become more and more convinced that the days of isolated HIV testing were over and that we needed to integrated testing and counseling into a broader array of services, including needle exchange, STD screening, hepatitis screening, and vaccinations." Foundation House and Foundation North, which added emergency transitional shelter to Harlem United's existing scattered site programs, was "icing on the cake."

FROST'D recognized that an alliance with Harlem United would bring additional benefits beyond access to a quality primary care program. "Part of their vision is a focus on the need for outcome evaluations," says Sippen. "They have very sophisticated evaluation programs. That is unusual among AIDS services organizations."

The two organizations also appeared to fit together culturally. "I was able to determine pretty quickly that they had a similar philosophy to ours," says McGovern, who had explored and turned down other merger opportunities where he didn't see a good fit.

The Harlem United/FROST'D strategic alliance moved extremely quickly, taking less than a year from initial contacts to a revision of the FROST'D corporate bylaws effectively making it a subsidiary of Harlem United.

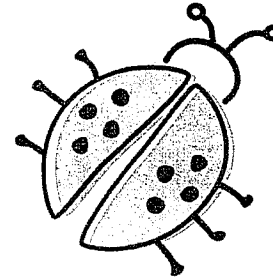
"I have been told that the lack of ego problems was one reason we were able to do this as fast as we did," says Sippen, who agreed to step down as executive director and has taken a program director position at Harlem United.

"Josh was extremely selfless throughout this process," says McGovern. "He was primarily interested in what was good for the organization and in protecting the interests of its clients."

FROST'D's staff and board were concerned about ensuring that the agency's name and legacy be maintained going forward. "We eventually settled on establishing a core group of programming within our Prevention Division called FROST'D at Harlem United," says McGovern. "It is essentially an injection drug users' help center with a full continuum of health related services. Foundation House North and South are also remaining intact."

"We still use the FROST'D name for our outreach services," says Sippen. "It still says FROST'D on our van. That is how people know us."

Elizabeth Seton Pediatric Center



About Elizabeth Seton Pediatric Center's Home Care Program

The Elizabeth Seton Pediatric Center was established in 1988 by the Sisters of Charity. We provide comprehensive rehabilitative care for children with a wide range of medical conditions and disabilities. All of our programs are centered on our children and their families, respecting individual cultural beliefs and practices. The Center has developed an expertise in pediatric care and has established the Home Care Program to bring that expertise from our home to yours.



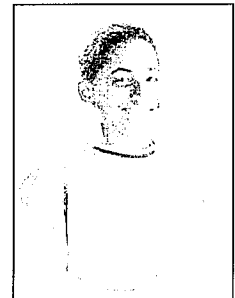
Who Is Eligible For Long Term Home Health Care?

Children who have extended care needs that require hospitalization or placement in a long term care facility and want to live at home are eligible.



Those children may include:

- Children with special needs such as
- Respiratory Therapy
- Tube feedings
- Special skin care
- Medication injections
- Mental Disability



Children with multiple care needs and a complex plan of care

Children whose health status is apt to deteriorate rapidly

Children whose health or functional status can be expected to stabilize or improve with the provision of home care services

Children with a poor prognosis for recovery

Service Areas

- * Manhattan
- * Queens
- * Brooklyn
- * Bronx

Ages Served

Birth to 21 years

Payment Sources

Medicaid Medicare
Private Insurance
Private Pay

Please call or fax the Home Care Program to make a referral or discuss questions or concerns.

Tel: 212.239.6586

Fax: 212.239.6719

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Parents and Children

In the case of both Goddard Riverside/St. Matthew's St. Timothy's and St. Nicholas NPC/School Settlement Assn., the organizations chose to establish a "parent/subsidiary" relationship.

"There isn't stock in nonprofit corporations," says Manley. "You can't go after another nonprofit in the market and get ownership by buying it. You get control by controlling the board." In both of the examples cited above, the bylaws of the subsidiary corporation were changed to make it a membership corporation with the "parent" being the sole member and having authority to appoint the subsidiary's board. "Depending on how many bells and whistles they put into the bylaws, the parent can have power to elect the executive director, approve the budget or authorize expenditures over a certain amount," says Manley.

Unlike a legal merger, this approach requires no application to the Attorney General's Office and no approval by the Supreme Court — only a vote by the subsidiary's current board of directors to change the by-laws.

If structured correctly, this approach also shields the parent corporation itself from liabilities of the subsidiary corporation, even if it implies a level of organizational commitment to maintaining the subsidiary's programs. Nor does the arrangement typically trigger "change of control" provisions in government contracts.

This type of strategic alliance, which maintains both the subsidiary corporation's legal existence and separate board of directors, may also be valuable in preserving a sense of programmatic and historic identity for agencies being "acquired." "That could be valuable," says Bob McMahon, Executive Director of SCO Family of Services which has completed several mergers over the years — although never a strategic alliance using this form. "It is difficult for a smaller nonprofit to give up its identity. Losing your 501c3 is hard to swallow."

However, despite the continuation of their separate corporate structure and a board of directors, nonprofits considering this type of subsidiary relationship must be clear on what it means. Once they pass that bylaw amendment, they have given over control. If the parent wants to make changes, they can just elect a new board. "I never sugar coat it," says Manley. "All the promises that may have been made during negotiations about preserving the name and keeping your secretary on staff — none of those are enforceable obligations."

A Transfer of Contracts

In some recent cases, local nonprofits have "merged" simply by arranging the reassignment of existing government contracts to provide services. Last year, Episcopal Social Services announced that it had "acquired" the child care programs of Sheltering Arms Children's Services. "The Administration for Children's Services thought highly of the programs and was supportive of their transfer as a unit to ESS," says Robert Gutheil, Executive Director at ESS.

Good Shepherd Services

In 1996, Good Shepherd Services was a well-respected provider of community-based youth programs and residential foster care services focusing on the specialized needs of adolescents.

McMahon Services for Children was a small, but high quality foster boarding home and adoption program. "We were very small," says Mary Ellen McLaughlin, the Executive Director of McMahon at that time. "The board had consciously decided they wanted quality over quantity." They had actually set a limit of only 250 children.

However, in the rapidly evolving world of child welfare services, it was becoming clear that a small, single-program agency like McMahon was unlikely to survive. "We were doing strategic planning. We needed either to diversify our programs and build more fundraising capacity or we had to find a partner," says McLaughlin.

There was no financial crisis. In fact, McMahon even had a small endowment. "We didn't want to wait too long," says McLaughlin. "Then, you are not attractive to other agencies."

McLaughlin started looking for another child welfare agency where she could take McMahon as a full program. Good Shepherd was a perfect fit. "We had never done foster boarding care," says Sr. Paulette LoMonaco, Executive Director at Good Shepherd. "We had done group care and neighborhood-based services. This expanded our continuum of care."

And, McLaughlin was more than willing to step down from her position as Executive Director. "I had been at McMahon for five years and certainly enjoyed it," she explains. "But I had always loved being in the program itself."

"Mary Ellen said that she would stay and run the program and she has been true to her word," says LoMonaco.

Not surprisingly, McMahon's board and staff were interested in maintaining the agency's name and programmatic identity, something which seemed doable at Good Shepherd. The program continues to operate as McMahon Services for Children in the same way that Good Shepherd's other programs — Euphrasian Residence, Marian Hall and St. Helena's — carry their own identities.

In order to bring in McMahon's endowment assets — a factor which helped reassure the board against the potential risk of unforeseen liabilities — the agencies went through a formal legal merger process.

McLaughlin believes that the merger has helped her program thrive, almost doubling in size to a current capacity of 450 children and significantly strengthening its level of financial and operational support. "We were able to bring them our expertise in working with adolescents," says LoMonaco.

"We are getting everything I could have hoped for," says McLaughlin. "We get foundation support. What we gained from having central administrative support is amazing. There is strong IT and fabulous quality improvement staff who help me with my reporting. We are really able to focus much more on outcomes for children and families."

Similarly, Good Shepherd Services' "merger" with the Bronx Community Programs of Pius XII Youth and Family Services also represented simply a reassignment of contracts by government agencies which were supportive of their move to a new home.

In both of these cases, the original sponsoring agencies — Sheltering Arms and Pius XII — had indicated that they were not prepared to continue the programs in question. "If they didn't come to us, they would have been shutting down," says Sr. Paulette LoMonaco, Executive Director of Good Shepherd Services.

Why? Why? Why?

Nonprofit mergers can happen for a range of reasons. In all the cases we have already mentioned, critical financial pressures forced the weaker entity to seek a stronger partner or give up its programs entirely.

While fiscal crises are common, they are not the only driving factor in mergers. In the recent strategic alliance between Harlem United and FROST'D, it was a longer term strategic assessment of its prospects in a changing service environ-

ment that led the board to seek a stronger partner. "There was no financial crisis," says former FROST'D executive director Josh Sippen.

A 1996 merger between Good Shepherd Services and McMahon Services for Children followed a similar pattern. McMahon's strategic planning indicated that, despite its strong balance sheet, the agency would have trouble surviving as a small, single-program provider.

Stronger agencies also decide to merge for a variety of reasons. In the case of both Goddard Riverside and St. Nicks, their decision to step in was driven by a desire to save what they saw as valuable community programs — programs which would surely close without their help. A similar rationale clearly helped to motivate Good Shepherd in its decision to take on the Bronx Community Programs of Pius XII, even if in this case the programs were located in an entirely different borough. "These were great programs," says Sr. Paulette. "They are exactly the same kinds of programs that we were running in Brooklyn."

In other cases, a stronger partner can be

McMahon Services for Children



Sister Paulette LoMonaco



Mary Ellen McLaughlin

motivated by strategic reasons. In the case of Harlem United, Patrick McGovern saw particular value in adding the FROST'D needle exchange programs — as well as emergency transitional residences — to its range of services. Good Shepherd's 1996 merger with McMahon expanded the agency's continuum of care to include foster boarding homes and adoption. Episcopal Social Services' "acquisition" of the Sheltering Arm child care programs was its first venture into that programmatic sector.

It's Tough

Mergers aren't easy. Regardless of your reasons for considering one, or the form it is going to take, the process of due diligence, decision making and implementation are demanding, time-consuming and stressful. There are always surprises, but rarely pleasant ones. Even the smoothest merger almost never goes smoothly. In upcoming issues we'll look at the steps involved in the process and get some tips from those who have been through them. No matter how they turn out, everyone appears to have learned something they would have done at least a little differently.