2009

Mergers and Acquisitions in the Non-profit Space

Jared Tham

MERGERS AND ACQUISITIONS in the Non-profit Space

M&A are a given in the for-profit sector, but at least in the local non-profit sector they are rare. Jared Tham believes this should not be the case.

Mergers and acquisitions (M&A) serve several purposes, inter alia to reduce market competition, cut costs, reduce taxes, or even to 'empire-build'.

This business-like approach may be seen as too calculative when applied to the non-profit sector – a world known for its emphasis on putting people first and ensuring the good of their beneficiaries. But as several non-profit experiences show, M&As do not only help the organisations to cut costs, it also paves the way for more strategic impact.

M&A for the Beneficiaries' Good

M&As can be undertaken in a positive spirit, whether it is a merger of two non-profit organisations (NPO) of comparable size, or an acquisition with a larger NPO taking a smaller NPO under its wing. Instead of increasing profits as a motivation for M&As, the key motivation is altogether different for NPOs, which have their clients' needs uppermost in their minds.

Taken in this light, M&As can provide significant economies of scale. Take for example the Arizona's Children Association. Back in 1994, it was a US$4.5 million organisation, focused primarily on offering residential services in Tuscon, USA.

But through a series of six acquisitions, they grew into a US$40 million state-wide NPO with a broad continuum of care for children and their families. Not only did each merger double or triple the number of clients served, but their per client cost was also cut by 11 to 40 % each.[1]

The concept of mergers has already been established in parts of the US non-profit scene. Researchers William Foster, Alex Cortez and Katie Smith Milway in a Bridgespan Group research project[2], examined more than 3,300 non-profit mergers over an 11-year period in four American states, and found a cumulative merger rate of 1.5% among NPOs, a figure that is comparable to the 1.7% among their for-profit counterparts.

In the Singapore non-profit space, news of M&A is rare. But those who have taken this path show promise. Take the case of the merger between Halogen Foundation Singapore (HFS, formerly Young Leaders Foundation Singapore) and Promiseworks in 2008. The common infrastructure now shared by the two bodies allows HFS to focus on developing a framework for building young leaders while Promiseworks continues to do its groundwork in mentoring youths.

According to Halogen's Executive Director, Martin Tan, focus on the beneficiaries and alignment in vision had helped the respective organisations to see sense in merging. There are cost savings for PromiseWorks in operational areas like accounts, rental and administration while for HFS, a wider portfolio of programmes now exists and includes mentoring programmes in schools that would otherwise not be possible to provide.

Shared Services - An Intermediate Solution

To be sure, intermediate solutions do exist in the provision of shared services – a collective of NPOs sharing back-office functions while maintaining their separate identities, governing structures and programmes – whose main purpose is to gain operating efficiencies and increase the quality of back-office functions by merging several non-profit operations.

In Singapore, similar economies of scale have been achieved. The most widely recognised is the Shared Services scheme administered by the National Council of Social Services (NCSS), in which functions such as Human Resource Management, Administration Services, Medical & Healthcare Services, Design & Printing Services, Audit Services, IT Services and IT Bulk Purchases are collectively outsourced to third-party providers.

There are also multi-service centres that provide the co-location option. Here, voluntary welfare organisations (VWOs) providing services for different groups of clients are aggregated in one location, thus providing a one-stop social service centre.

M&A as the Next Step

M&A go beyond consolidating NPO back-end operations. It places relevant NPO players in a better position to view the beneficiaries' needs and environment in their entirety.

There is market opportunity for mergers. The school social work sector in Singapore, which includes youth workers as well as school counsellors, is an example. Within this sector, there are about 40 NPOs[3] providing a potential pool of 324 primary and secondary schools[4] with preventive, development and remedial services for students. While the ratio may seem enviable (1 NPO to every eight schools), the reality is that only a handful of schools seek such services each year. There are about five large NPOs which have already achieved economies of scale, and are able to serve eight to 10 schools each. Where does this leave the rest of the small players that have at most two programme staff?

This fragmented state leads to a highly competitive situation in which the livelihoods of entire NPOs (and their youth workers) hinge on their ability to attract the patronage of particular schools. This is especially difficult if the NPO has a short track record, yet needs to prove its capability in order to receive funding.

Should two or three of the smaller youth agencies decide to merge, they would be in a better position to achieve economies of scale and stretch donor money to cater to more schools. And if an NPO that does mainstream youth work decides to merge with an agency that specialises in school social work, both agencies are better placed to provide a continuum of services for any youth they meet.

The Real Questions

The biggest concern of management and staff of NPOs regarding M&A is that they are going to lose their sense of identity, along with the organisation's mission. This is especially so when people have invested a significant part of their lives to build their organisations. At times, founders who successfully start NPOs may not have the necessary qualities to enable it to scale up its operations. They may therefore spend more time defending their "turf", rather than exploring all possible means to ensure the welfare of their clients. The fear of job losses for staff may also be a key factor that hinders M&As.

Unlike the for-profit companies, financial incentives for the NPO management to initiate M&As are non-existent.

Furthermore, due diligence is needed to address governance issues and financial liabilities. And while there are cost savings in the long run, the period of transition may incur more costs.

Yet, the last thing we want is to have NPOs coast along, content with performing below maximum efficiency. But sometimes, it requires getting out of their comfort zone in order to see that drastic changes are necessary in order to create drastic improvements for the beneficiaries they serve. ❖

[1] Alexander Cortex, William Foster and Katie Smith Milway, "Nonprofit M&A: More Than a Tool for Tough Times," *The Bridgespan Group* (February 2009) <http://www.bridgespan.org/Nonprofit-M-and-A.aspx>

[2] Ibid.

[3] Personal estimate based on having worked with several NPOs providing school social work services.

[4] 2007 figures from Ministry of Education, Singapore. Available at <http://www.moe.gov.sg/education/education-statistics-digest/online-interactive/tables/table-18-2007.pdf>

Jared Tham manages research and programmes at the Lien Centre for Social Innovation. His experience spans various sectors, such as youth, international volunteerism and social services and he has an interest in fostering greater collaboration among non-profit organisations.