

The Myths and Reality of Nonprofit Collaboration: Observations from Six Years in the Trenches

John MacIntosh, Partner, SeaChange Capital Partners and
Lois Savage, President, The Lodestar Foundation

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The Lodestar Foundation has been funding nonprofit collaboration since 1999. In 2009, Lodestar began a partnership with SeaChange Capital Partners to increase the scope of collaborative activity. Since then, SeaChange and Lodestar have evaluated roughly 400 transactions and made more than 100 grants to support nonprofits in exploring or completing mergers, acquisitions, joint-ventures, and other types of formal, long-term collaborations. In parallel, we've worked with partners in the sector – umbrella groups, funders, consultants – to promulgate collaboration as an effective strategic tool that should be considered in the normal course of business within nonprofit boardrooms and executive offices, and as an important form of capacity-building worthy of funder support. It has been satisfying, challenging and fulfilling work; what we've learned dispels many of the myths that keep nonprofits, funders and others in the sector from realizing the full potential of

collaboration.

A Word on Terminology

"Collaboration," "repositioning," "consolidation," "combination," "merger and acquisition," "partnership," "alliance," and "strategic restructuring" are ill-defined and often used interchangeably to mean very different things.

In this piece, we use "collaboration" to describe any transaction whereby two or more nonprofits combine some (or all) of their important activities in a formal, long-term way. Possible forms of collaboration include mergers, acquisitions and various other forms such as joint purchasing, administrative consolidations, co-locations and the creation of joint-ventures or programmatic partnerships. We use "collaboration" because it includes not only mergers, acquisitions and consolidations, common terms in the for-profit world that tend to make nonprofits nervous, but also the broader range of less intensive ways nonprofits can come together.

Myth #1: For-profit mergers and other similar transactions are driven by cost savings and shareholder value.

Nonprofits have different motivations, so there is little role for these types of transactions in the nonprofit sector.

There are over a million nonprofit organizations in the

United States operating in a dynamic environment of social, demographic, technological, political and financial change. Over the last 15 years, the US population has grown 17%, giving has increased by 34%, and the number of nonprofits has doubled. Nonprofits face challenges of scale, succession, duplication of effort, high fundraising costs and limited funding. In an environment of this scale and complexity, numerous opportunities exist to explore collaboration as a strategy to improve efficiency, effectiveness and stability. Not surprisingly, nonprofits report a wide-range of motivations to explore collaboration:

1. Economies of scale (programmatic and financial)
2. Broader geographic and programmatic impact
3. An increase in access to potential funding from new donors
4. Potential creation of joint programs for more robust services to the community
5. Preservation and sustainability of financially unstable programs
6. Strengthening of organizational leadership, easing of leadership transitions and recruitment of high quality professional talent

"Cost savings" is not on the list, even though some collaborations – though probably a minority – do offer the potential to meaningfully reduce costs over time. But nonprofits don't see cost savings as an end in itself (they don't have owners to whom they can distribute the

money); they see it as a means to grow or sustain programming.

Myth #2: "Collaboration" is a euphemism for the merger of financially weak organizations, the acquisition of the weak by the strong or the small by the large. It's generally a sign of weakness.

The most common collaborations are between strong or stable organizations (~75%); strong-weak combinations are a distant second (~20%), while only ~5% involve two organizations struggling financially. While mergers and acquisitions represent roughly two-thirds of the potential transactions we have reviewed, a full one-third are programmatic alliances, back-office collaborations, nonprofit consortiums and the like.

Most collaborations are between organizations of similar budgets. Organizations of all sizes are active in exploring collaborations, though the smallest ones (budgets of less than \$500,000) appear to be underrepresented (40% of the total transactions that we have seen versus 75% of the nonprofits in the country).

Myth #3: Nonprofits need help identifying potential partners.

Collaborations usually involve organizations that already

know each other well through some combination of staff connections (60%), joint programming (70%), common funders (50%) and overlapping board members (10-20%); less than 5% involve organizations that have no pre-existing connections. Nonprofits don't usually need help in identifying these potential partners, but they do need help approaching them to identify the best fit.

Myth #4: Once partners have found one another, exploring collaboration is easy.

Nothing could be further from the truth. Even once potential partners have identified one another, exploring a potential collaboration requires clear, mission-focused thinking by executive directors and boards and a deliberate process to explore issues related to mission alignment, programmatic fit, leadership, staffing, economics, branding and the like. This takes time. In fact, two-thirds of collaboration discussions take six months or more to progress, with 15% taking more than two years. In almost 20% of the cases we have seen, the organizations are pursuing collaborations for a second time after a failed first attempt with the same potential partner.

A challenge is often the need for confidentiality.

Organizations regularly begin meaningful exploratory discussions before they feel it is appropriate to inform board members (22%), staff (54%), funders (75%), or

clients (92%), and executive directors and boards find it difficult to figure out when and how to bring stakeholders "in the know."

Given these challenges, it is no surprise that organizations often decide (in one-third to one-half of the cases) to engage an outside consultant/facilitator to help. In our experience, a carefully selected, jointly-retained consultant with the right capabilities can be vital in bringing discipline to the process and in ensuring clear communication between the organizations.

Myth #5: The executive director is critical; the board follows his/her lead.

Both the executive director and the board are critical.

While the executive director is far more likely to initiate collaboration discussions (80% of the time) than the board (20% of the time), boards are critical both in creating an environment where executive directors feel empowered to begin these discussions and in evaluating particular opportunities. Collaborations, particularly mergers, can strain the relationship between the executive director and the board if no agreement on their respective roles and responsibilities in the process is discussed, including (most likely) the creation of a special committee.

Boards and executive directors are more likely to see a given collaboration in the same light if they share a common understanding of the environment in which the organizations operate.

Myth #6: Collaborations are risky.

Collaborations are not nearly as risky as they are commonly thought to be. In our experience, nonprofits facing a potential collaboration see a consistent set of possible risks that need to be considered:

1. Loss of individual organizational independence and identity and a dilution of both organizations' missions
2. Loss of donor confidence leading to a reduction in funding, failure to raise enough capital to cover merger and future operational costs
3. Loss of credibility, reputation and support in the community
4. Lack of board, leadership and staff support resulting in staff resignations and confusion within the organization
5. Challenging integration due to organizational cultural differences
6. Lack of organizational capacity (staff and space) to carry out merger
7. Fear that a failed exploration will leave the organization weakened

Experience has shown that these risks most often are either (a) mainly perceptions, not real risks, or (b) can be assessed, and in most cases overcome, by good planning that addresses them strategically. To us, it is apparent that the large potential benefits greatly outweigh the noted risk factors; our analysis suggests that roughly 80%

of the completed collaborations we have supported have been successful, creating tangible programmatic and operational benefits that are multiples of the resources expended. According to Bridgespan research, executive directors across the country see similar levels of success for collaborations, particularly for more integrated forms of collaborations, such as mergers.

And even when a transaction is not ultimately pursued, the exploration process often serves as a “landscape” analysis that helps the organization determine its best course of action. Exploring a potential collaboration gives an organization an opportunity to take a step back and see itself as part of an ecosystem trying to have an impact in a given area, appreciate its strengths and weaknesses and clarify and reaffirm its mission.

Myth #7: Collaboration is expensive.

The one-time out-of-pocket costs of exploring or implementing a collaboration are generally \$20,000 to \$200,000 in areas including facilitation, legal/accounting help, rebranding, IT integration and severance (the larger cost is staff time, which is why a well-run process is so important). These are relatively minor costs when compared to the potential benefits. While potential cost savings are not a sufficient reason to pursue collaboration in the absence of mission alignment, they can still be very meaningful relative to the cost of making the collaboration happen.

For example, if a merger that will cost \$200,000 to consummate is expected to save \$600,000 over four years (because of reduced costs of \$150,000 per year), then, even in purely financial terms, it represents a highly leveraged 3:1 return. In effect, funding the collaboration is a highly-leveraged capacity-building grant. Moreover, even if the savings are modest relative to the total scale of the combined organization, they may be very important at the margin and will often come from a reduction in the type of expenses that are the most difficult to fund – overhead. And the reality of this 3:1 leverage would be no less true if, like many nonprofits, the organization chose to reallocate the \$600,000 to provide additional services rather than shrinking in absolute terms.

The good news is that potential cost savings are not difficult to estimate. The expenses of running most nonprofits are overwhelmingly personnel-related; people in nonprofits work hard and few are highly compensated. So unless the combined organization will be doing much less than they were before the collaboration, there will not be much opportunity to reduce costs in programmatic areas; however, there can often be easily identifiable redundancies in overhead functions (like HR, accounting, and development) as well as in areas like real estate, insurance, or technology.

Myth #8: Funders aggressively push collaboration but don't want to fund it.

It is true that while many funders would like to see more mergers (~50%) and back-office consolidations (~75%), they find it difficult to support these more integrated forms of collaboration. In fact, only 20% of nonprofit leaders said they received explicit support from their funders during the exploration or implementation of collaborations, be it introducing them to partners, due diligence, planning, integration, or full implementation.

This aligns with the results of a recent survey from Grantmakers for Effective Organizations (GEO) that found 53% of funders never or rarely funded collaborations and only 2% made it a consistent practice. Funders find it difficult to support collaboration because of the nature of the grants – fast, small, process-oriented, confidential – are so different from the programmatic, capacity-building, and other grants they consider year-over-year. Yet at the same time, recent research from Bridegspan suggests that more funders would support collaboration if their grantees simply asked.

Notwithstanding the historic lack of support, funders, acting individually or through funder collaboratives, have begun to focus on collaboration as an important form of capacity building. A recent national mapping exercise suggests that there are now 18 funder initiatives in support of nonprofit collaboration and this movement, while small, appears to be growing. These funders – of which we are a part – have also begun to share best practices, much of which come down to "checking their

own power" by creating a safe and fertile environment for collaboration discussions to take root while letting nonprofits choose their partners and agree to roles and goals on their own terms.

A Final Thought on Collaboration

Compared with "exponential growth," "collective impact," "social enterprise," "social impact bonds," or "catalytic philanthropy," "collaboration" may not seem very exciting; it is an idea that has been around for a long time and hasn't yet "gone viral" or "broken out." And it is true that collaboration is no panacea; even if it helps organizations become more efficient, effective, or stable than they would be working alone, the issues they address – poverty, racism, hunger, illness, etc. – will remain unresolved. But helping groups do what they know is right is satisfying. And we have seen that the right collaboration can be transformational for the organizations involved and the constituencies they serve.