



A STUDY

A synopsis of a study of 41 direct service organization mergers in Minnesota
1999-2010

Synopsis: Success Factors in Nonprofit Mergers

July 2012



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Joint research project of MAP for Nonprofits and Wilder Research

Project staff:

Greg Owen, Brian Pittman,
Laura Martell Kelly

Ron Reed

Wilder Research
451 Lexington Parkway North
Saint Paul, Minnesota 55104
651-280-2700
www.wilderresearch.org

MAP for Nonprofits
2314 University Avenue, Suite 28
Saint Paul, Minnesota 55114
651-647-1216
www.mapfornonprofits.org



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The mergers studied for this report were identified from a list supplied by the Office of the Minnesota Secretary of State. GuideStar provided 990 tax data for financial analysis.

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Dear Friends,

More and more nonprofit leaders are considering the opportunity to re-design their nonprofit organizations through mergers, joint ventures, program transfers, shared services, and acquisitions.

As a capacity building organization, we see this first-hand. In 2007, we added merger/redesign consultation to our mix of services. Since then, our ReDesign team has completed 65 realignments affecting more than 120 organizations. The interest in mergers and other types of realignment continues to grow today, as nonprofit leaders seek to create more sustainable structures from which to provide essential community and human services.

In addition to providing redesign consultation, we also created and published *MergeMinnesota: Nonprofit merger as an opportunity for survival and growth* (Reed & Dowd, 2009). While preparing *MergeMinnesota*, we observed an absence of information on what factors influence merger outcomes. We decided additional research was needed to add to the sector's understanding and adeptness related to mergers and redesign.

Our conclusion led us to Wilder Research, with whom we embarked upon a multi-year research initiative, culminating in the July 2012 publication of *Success Factors in Nonprofit Mergers* which is summarized in this document. We believe this research is the first to comprehensively look beyond the nonprofit merger process to assess what happens after the merger, especially in the operations and functioning of merged organizations.

As we assess the research results, we see evidence that mergers are producing positive outcomes for our communities. The research provides valuable lessons that will help us all to craft a more vibrant and effective nonprofit sector. We trust the lessons are helpful throughout the sector, and for many years to come.

Sincerely,

A handwritten signature in black ink that reads "Judy Alnes". The signature is fluid and cursive, with a long horizontal line extending from the end.

Judith E. Alnes
Executive Director
MAP for Nonprofits



Participating Organizations

This research would not have taken place without the support of the executive directors of the following 41 merged organizations included in the study.

Animal Humane Society	Janelle Dixon
Big Brothers Big Sisters of Southern Minnesota	Greg Zweber
Bloomington Theatre and Art Center	Andrea Specht
Boys & Girls Clubs of the Twin Cities	Erin Carlin
Camp Fire USA Minnesota Council	Marnie Wells
Center for Alcohol & Drug Treatment, Inc.	Gary Olson
Channel One Food Bank	Jennifer Woodford
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Clare Housing	Lee Lewis
COMPAS, Inc.	Bob Olsen
Copeland Valley Youth Centers	Russ Salgy
Danish American Center	Glen Olsen
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FamilyMeans	Arba-Della Beck
Functional Industries, Inc.	Rod Pederson
Girl Scouts of Minnesota & Wisconsin Lakes & Pines	Leigh Ann Davis
Girl Scouts of Minnesota and Wisconsin River Valleys	Linda Keene
Hands of Hope Resource Center, Inc.	Stephenie Och
Headway Emotional Health Services	Patrick Dale
Intermedia Arts	Theresa Sweetland
Keystone Community Services	Eric Nyberg
LDA Minnesota (Learning Disabilities Association)	Kitty Christiansen
Lyndale Neighborhood Association	Mark Hinds
Metro Deaf School	Dyan Sherwood
Metropolitan Area Agency on Aging, Inc.	Dawn Simonson
Minnesota Dance Theatre & the Dance Institute	Marsha Walker
Nemadji Community Resource Center	Deb Kangas
National Child Protection Training Center	Victor Vieth
Northern Star Council, Boy Scouts of America	John Andrews
NorthPoint Health & Wellness Center, Inc.	Stella Whitney-West
PRISM (People Responding in Social Ministry)	Elizabeth Johnson
Project for Pride in Living, Inc. (PPL)	Steve Cramer
Rochester Area Family YMCA	Steve Courts
RS EDEN	Dan Cain
Second Harvest Heartland	Rob Zeaske
Support Within Reach Sexual Violence Resource Center	Amanda Ysen
The Arc Greater Twin Cities	Kim Keprios
The Arc Southeastern Minnesota	Elisabeth Hennessey
VINE Faith in Action	Pam Determan
Vision Loss Resources	Kate Grathwol
West Side Community Health Services	Jaeson Fournier



Synopsis: Success Factors in Nonprofit Mergers

Mergers have become a common topic of discussion among nonprofit leaders, boards, and funders. They are often seen as a way to preserve and strengthen needed community services. However, organizations have been challenged by the lack of research based information about what factors influence the outcomes of a merger. This study was done to add to the body of knowledge about why direct service nonprofits decide to merge, how the process is completed, what happens following a merger, and what factors most influence merger outcomes.

The findings suggest that significant benefit can be achieved through the exploration and careful consideration of merger as an option for many types of nonprofits. Study respondents have made it clear that, although this is both challenging and sometimes stressful work, it may be worth pursuing in the interest of a greater community good.

Study results clearly indicate that mergers may work best when organizations have some history of partnership and openness, when non-administrative staff members and funders have input and involvement in the process, and when there is transparency in both legal and financial matters.

In difficult economic times, and in times when the demand for health and human services is expanding, it appears that mergers can contribute to the stability of the nonprofit environment and, at the same time, preserve and sometimes expand services.

Background

This presents the results of an analysis of 41 mergers of direct service nonprofit organizations based in Minnesota. It is intended to help nonprofit leaders, staff, funders, board members, and other stakeholders make decisions and assess the potential for success in nonprofit mergers. It is part of a larger study effort that began with the publication of *MergeMinnesota: Nonprofit merger as an opportunity for survival and growth* (Reed & Dowd, 2009), designed as a toolkit for organizations considering mergers and based on advice from nonprofit leaders and consultants. This was followed by the publication of *What do we know about nonprofit mergers?* (Owen, Martell Kelly, Pittman, Wagner, & Reed, 2011), which presented findings from a literature review of research articles based on data collected to answer specific research questions. It also reported information from a focus group and key informant interviews with executive directors, funders, attorneys, consultants, financial advisors, and others involved in nonprofit mergers. Both of these reports have shed light on factors that influence merger outcomes, and have been used to shape the research presented here.



Study approach and methods

To learn more about nonprofit mergers, the study team reviewed a comprehensive list of nonprofit mergers from the Office of the Minnesota Secretary of State to identify potential cases for this study. To be eligible, a merger needed to include direct service organizations and have occurred between January 1999 and June 2010. For purposes of the study, a merger is defined as an integration of two or more separate organizations into one legal entity in which at least one organization ceases to exist. In addition, eligible mergers had to include a transfer of programs or services, and a transfer of assets or staff. Of the 66 potential mergers identified, 46 were determined to be eligible for study participation. Of those, 41 agreed to participate resulting in an 89 percent participation rate.

Study participation was secured through telephone contact with executive directors by a former executive director who was also a lead member of the study team. Each executive director contacted was in turn asked to identify board members, financial managers, and other staff or volunteers who would have detailed knowledge regarding the merger.

In-depth phone interviews, lasting between one and two hours each, were conducted with 201 individuals. The number of respondents representing each merger ranged from three to eight. All 41 mergers were represented by at least the current executive director, a board member, and one representative from an organization that ceased to exist following merger. In order to fully use information from all 201 study respondents, the research team constructed case-level files for each of the 41 mergers. This construction was based on the level of consensus among respondents on each study measure. Each measure was classified based on whether or not there was consistent agreement among respondents. In this analysis, merger cases for which there was consistent agreement were compared to those cases in which there were inconsistent or contradictory responses. Based on these groupings, pre-merger and merger process related questions were cross tabulated with responses to questions related to post-merger success and tested for statistical significance.

In addition, financial data were obtained from publicly available 990 tax forms accessed from GuideStar. When available, forms were collected for the three years prior to the merger for all organizations involved, the first year of merged operations, and the three years following the merger.

Analysis involved calculating financial ratios that were used to assess the financial health and stability of merged organizations.



Indicators of merger success

This research is unique. It is the first to comprehensively look beyond the merger process to assess what happens after the merger, especially in the operations and functioning of merged organizations. For purposes of this study, the following outcomes are regarded as key indicators of success for merged organizations:

- Improved image, reputation, or public support
- Improved, expanded, or preserved services
- Increased quality of operations
- Increased efficiency of operations
- Improved financial stability
- Development of a positive organizational culture

The study focuses primarily on the question of which factors predict success in nonprofit mergers. In particular, the study examines how the preservation of services and the administrative operations of newly-merged entities are affected by what happens prior to the merger.

Study results

Merging is a complex and sometimes arduous process. It requires the successful negotiation of a wide range of relationships and sensitivities, as well as clarity about the ultimate social good that one is striving to achieve through the combining of services. An analysis of the 41 mergers in the Minnesota study sample reveals the following:

Reasons for merging

Most mergers are pursued for a combination of strategic and survival motives.

- Strategically, organizations pursued merger to increase service delivery (93%), because the organization had a strategic vision that included merger (66%), or to improve what was already regarded as a reasonably solid financial status (61%).
- Primary survival motivations for merger included an interest in increasing long-term financial viability or solvency for at least one pre-merger organization (93%), a chance to save services that would otherwise be lost (75%), or a way to avoid imminent financial crisis (37%). However, few of the organizations studied reported a struggle to meet payroll (12%) or a need to sustain daily operations with a line of credit prior to the merger (7%).



Respondents also said the merger was done with the hopes of improving programs and providing better services. Sometimes they sought to acquire characteristics of another organization.

- Just over a half (56%) of the mergers sought to expand services to new market areas or populations. About one-quarter (29%) sought to expand the types of services offered to consumers.
- Respondents for 17 organizations reported the merger was motivated in part by a desire to expand their donor base. Eight organizations wanted to achieve greater staff expertise through merger, and five intended to expand physical space through the merger.

The role of the executive director and board

The presence of a leader committed to merger or the recent departure or retirement of an executive director can significantly influence an organization's approach to merger.

- Respondents from 95 percent of the mergers agreed that if not for one of the executive directors, the merger would never have happened. In addition, for 80 percent of the mergers, an executive director had recently left or was soon to retire in at least one of the pre-merger organizations.

Typically, an organization's board of directors also has significant influence on the decision and approach to pursue merger.

- In 61 percent of the mergers, having a board member from at least one of the pre-merger organizations pushing for merger was a primary reason for pursuing the merger.
- In 46 percent of the mergers, a board member was identified as a "champion" of the merger. In 78 percent of the mergers the decision to merge had strong support from board members.

Mission alignment and prior organizational relationships

Contrary to conventional wisdom, study results show that just over half of all mergers in the sample were closely matched on mission and vision, and only about one-third had previous collaboration or partnership arrangements.

- Fifty-four percent of the mergers studied were consistently reported to share a similar vision and mission. Fewer pre-merger organizations shared client or member populations (44%) and program focus (34%).



- Respondents for 32 percent of the mergers consistently agreed that the pre-merger organizations had previously collaborated or partnered, and 24 percent of the mergers were reported to have pre-merger executives who had a strong working relationship.

External environment

Conditions outside of the organization's control, such as the general economic climate or increased competition for resources, can also play a key role in an organization's decision to merge. Funders may also influence the process.

- Competition for funding was a primary motivation to merge in almost one-half (46%) of all mergers. Less than one-third (29%) of the mergers identified increased competition for providing services as a primary reason for merging.
- Respondents for one-third (34%) of the mergers said the economy influenced the decision to merge, and respondents for about one in eight mergers (12%) identified funder pressure as an important influence.

Merging process

Mergers typically involve a variety of tasks which may include establishing goals; identifying organizational participants; pursuing due diligence related to fiscal, legal, and administrative matters; engaging consultants and stakeholders; and integrating organizational systems. This study looks at the extent to which each of these tasks is considered and completed in pursuing the goal of a successful merger. Results indicate:

- Seventy-eight percent of merger partners had agreed on a defined process for the merger.
- Sixty-three percent of the mergers had specified one or more outcome goals such as financial stability, service preservation, improved operations, and/or reduced expenses.
- Eighty percent of mergers represented in the study were completed according to a time frame set forth in the planning process.

During the merging process, "due diligence" includes the identification or mitigation of risk in an attempt to increase the potential for success.

- In 68 percent of mergers there was consistent agreement that key merger leaders were given adequate time to develop relationships and negotiate the merger process, which for some was considered a part of "due diligence."



- In 76 percent of the mergers there was consistent agreement that each organization was able to examine financial and legal information about the other organization. Respondents from 32 of the mergers consistently reported that financial due diligence was one of the most important aspects of the merger process.

Consultants played an integral role in the majority of mergers. They did so by facilitating plans, meetings, and discussions or providing expertise and a third-party perspective.

- Eighty-five percent of the mergers studied used a consultant in some capacity. When consultants were involved, respondents for more than one-half (57%) of the mergers reported that the consultant performed tasks that the organization's staff or board members could not have done on their own.
- Respondents for 51 percent of the mergers that involved a consultant reported that the consultant was critical to the success of the merger.
- Respondents for 96 percent of the mergers would involve a consultant if they were doing another merger.

Involving key organizational stakeholders such as organization executives, board members, leadership and administrative staff, clients, funders, and the public-at-large is critical to the success of any merger process.

- In 88 percent of the mergers, an executive committed to considering strategic restructuring was present. The executive was described as the chief proponent of the merger process in 61 percent of cases.
- In open ended comments, respondents for 22 mergers said that the merger would likely have not happened without the commitment of the boards of directors.
- While non-administrative staff members were kept informed about the progress of merger (78%), they were not usually included in merger planning and processes (29%).
- About one-quarter of the mergers gave funders the opportunity to provide input (24%) or provided funders with regular updates on their work (22%).

As organizations engaged in the merging process, the integration of board and governance structures received significantly more attention than the integration of organizational cultures.



- Respondents for almost all of the mergers reported that there was a plan for how the board and governance structure would be affected by the merger (93%) and how the operations of the two organizations would be combined (90%).
- Far fewer (17%) said there was a plan to integrate the cultures of the merging organizations.

Financial analysis

An analysis of aggregate financial information available for each of the organizations involved in the 41 mergers shows that there was a slight decrease in short term fiscal stability and a slight increase in long-term fiscal stability. Looking at the three years before each merger and the three years after merger, there was a:

- Fourteen percent improvement in the overall aggregate debt ratio (total liabilities divided by unrestricted assets).
- Seventeen percent decrease in the current ratio (current assets divided by current liabilities).

Analyzing the 21 mergers for which complete financial data are available shows the complex and mixed financial outcomes of merger. Forty-eight percent of these mergers were determined to have strong post-merger financial stability while another 33 percent showed moderate financial stability. The remaining 19 percent of the mergers were determined to have weak financial stability.

To help understand the fiscal stability of these post-merger organizations, the study analyzed their financial data from the year of their merger (baseline) and three years after the merger (follow-up).

- Fifty-two percent increased their days cash on hand (the number of days a nonprofit is able to cover their budgeted operational expenses with their liquid assets), but only 38 percent of the mergers had 90 days cash on hand at follow-up.
- Forty-eight percent improved their debt ratio, and 86 percent of the mergers met the standard 2:1 debt ratio at follow-up.
- Thirty-eight percent improved their current ratio, but 86 percent of the mergers met the standard 1:1 current ratio at follow-up.



Furthermore, analyzing revenues and expenses for these mergers three years after the merger shows the complexities of post-merger financial stability.

- Fifty-two percent of organizations experienced decreased revenue from contributions and grants, but total revenue from these sources increased by 9 percent for the 21 organizations.
- Sixty-two percent of organizations experienced increased program service revenue, and total program service revenue increased 12 percent.
- Sixty-seven percent of organizations experienced increases in total expenses, and total expenses increased 8 percent in aggregate (total revenue also increased by 8%).
- Seventy-one percent of organizations experienced increases in accounts payable and accrued interest (short-term expenses), with a total aggregate increase of 18 percent.

Overall, these findings indicate reasonable strength in the long-term financial picture and some weakening in short-term financial positions. These results suggest there may be a short-term need for cash to cover merging expenses, new costs, or more operational expenses. These results may also reflect a strategic decision to pay down long-term debt.

Success factors in nonprofit mergers

The majority of findings in this section are based on cross tabular analyses of pre-merger and merger process measures in relationship to post-merger outcomes and indicators of success. When such relationships are reported in this section, findings are considered statistically significant using probability criteria of .06. This criteria is used (rather than the standard .05 value) in order to call attention to relationships that are likely to be meaningful but which would not have otherwise been reported using the more stringent standard. In this context, findings mean that the relationship between pre-merger and merging process measures are statistically associated with post-merger outcomes and that there is a low probability of these relationships occurring by chance.



Executive leadership

- The study finds that there is a clear and significant relationship between the presence of strong working relationships among executives prior to a merger and the preservation of services following merger.
- When an executive is a champion for the merger there is a statistically greater likelihood that the organization's image, reputation, or level of public support will be greater following merger.
- A strong working relationship among executives prior to the merger is also positively associated with greater financial stability and improved post-merger integration when the merger is complete.

This suggests that significant attention must be paid to the executive leadership participating in any merger and that funders and other stakeholders must take the presence or absence of these leadership characteristics into account when considering how and when to best support the pursuit of a merger.

Board involvement

As indicated earlier, board involvement and encouragement appears to be an important element in the majority of mergers described in this report.

- When respondents consistently report that the board of each premerger organization was integrally involved in the merger process, they were also more likely to report that the merged entity had improved its image, reputation, or public support in the three years following the merger.
- Open-ended comments indicate that boards are seldom unanimous in their willingness to consider merger and it is often the financial position of the organization that motivates board members to urge consideration of such an option.

It appears from a governance standpoint that it may be useful to educate board members with evidence-based information regarding nonprofit mergers so that they will be informed by the best available knowledge and resources.



Shared vision of benefits associated with merger

It was somewhat surprising to find that respondents for just over half of the mergers consistently agreed that the pre-merger organizations shared a similar mission and vision. This is not to say, however, that there was not significant overlap in these areas. Specifically the study finds:

- When organizations were able to identify potential mutual gains that could be realized in the merger there was a statistically greater likelihood that staff would integrate well into the new organization and be better aligned with the needs of the new organization and those whom it intended to serve.

This finding suggests that similarity of (and not necessarily identical) focus is likely to be important, but that it is not the only thing to be considered when looking at the compatibility of two or more agencies as potential merger partners.

Merger consultants

The vast majority of mergers described in this report (85%) engaged a consultant to assist with the merger. Moreover, in the majority of mergers, consultants performed functions that could not be performed by staff or board members on their own.

- Consultants especially added value as experts, including the specialized knowledge they could bring regarding organizational structure and function, finances, and legal aspects of merger.
- Consultants were also seen to have value as facilitators and third-party observers who could take a more objective view of the issues being faced by the organizations considering merger.
- In a few cases, consultants served in a more specialized role, serving as an interim executive director. In these circumstances, consultants become leaders within the organization to manage change, assess current issues, and engage boards in considering a range of possible actions including restructuring, reorganization, and merger.

Overall, it appears that consultants help to steady the process of merger because of the experience they bring and the reassurances that they can give during difficult transitions. They also appear to be critical in helping organizations take the appropriate steps at the appropriate times, and in avoiding or at least mitigating pitfalls that can come from limited experience with such major structural changes.



Financial distress

In at least one-third of the mergers described in the study, one of the organizations seeking merger was experiencing some type of serious financial difficulty. In two-thirds of all mergers, at least one of the partners reported that the goal of long-term financial viability was a primary motive in considering merger. In this sense, financial concerns are quite often an important motivator of those considering merger.

Interestingly, the study also shows that some level of financial distress may not only encourage merger, but may also mitigate difficulties related to the integration of organizational cultures following merger. In particular, the study shows:

- There is less likelihood of looking back at the pre-merger organizations with a sense of grief and loss when the pre-merger organizations struggled to make payroll or pay expenses.
- In contrast to this, when the pre-merger organizations had adequate assets to collateralize loans prior to the merger, respondents were less likely to report that staff from the pre-merger organizations integrated well following merger.

Stated a different way, when pre-merger organizations are in difficult financial straits, staff may be somewhat more flexible in adapting to a new organizational climate or culture.

It is clear from study results that significant attention was paid during the merger process to the financial conditions of each potential merger partner. In fact:

- Having an opportunity to examine the financial and legal information of each organization in detail was associated with improved reputation and public support following merger, as well as expansion or improvement in the quality of services following merger.

Finally, while it is clear that some organizations experienced financial difficulties that motivated their merger work few organizations in the sample were at imminent risk of closing. In general, it seems likely that there is a point that may be reached in an organization's financial status where things have become so distressed that the organization can no longer be seen as a viable merger partner by any other organization. This suggests that it is important for an organization to consider the potential role of merger during early points of financial difficulty or even during times of financial strength.



Involvement of non-administrative staff

One finding of particular interest is the fact that the communication with, buy-in from, and involvement of non-administrative staff prior to merger are all associated with a significant number of positive outcomes following merger. Specifically:

- Financial stability, service quality and/or expansion, organizational reputation, and the alignment of staffing with client needs, are all positively associated with one or more elements of communication with and involvement of non-administrative staff.

This is a compelling finding because most often it is the executive leadership and board members who are most deeply involved in the actual planning and execution of a merger. Nonetheless, this study indicates that careful attention to how other staff members are informed, involved, and brought along during the process of a merger is likely to yield significant beneficial results when the merger is concluded.

Funder involvement

Similar to the findings regarding the involvement of non-administrative staff, funder involvement is also positively associated with important beneficial merger outcomes. In particular:

- The participation of funders is one of the few measures that predict the preservation of services following a merger.
- Funder involvement is also associated with improved financial stability and the better alignment of staff with the needs of the organization and its clients.

Based on this finding, it is safe to conclude that funder involvement, particularly involvement that gives funders an opportunity to give input into the plan and process of merger, can result in outcomes that would be widely regarded as beneficial to the community including organizational stability and service preservation.

Financial stability and service preservation following merger

The study began with the hypothesis that mergers could be beneficial in strengthening the financial stability and preserving the services of nonprofit direct service organizations. Study results indicate that the best predictors of financial stability following merger are:

- Strong working relationships among executives prior to merger
- Collaborations or partnerships between organizations prior to merger
- The inclusion and support of non-administrative staff in planning and implementation
- Opportunities for funders to participate and give input into merger planning



In addition, study results indicate that the best predictors of the preservation or expansion of services following merger are:

- Strong working relationships among executives prior to merger
- Opportunities for organizations considering merger to examine the financial and legal information about their potential merger partner(s)
- The development of cost sharing agreements for expenses related to the merger process
- The support and inclusion of non-administrative staff during the merger process including the use of staff meetings to address merger tasks
- Opportunities for funders to participate in and give input into merger planning

Considerations for future research activities

This study attempts to add to the current body of knowledge about the reasons organizations decide to pursue merger, the merging process, and the success of mergers. It also examines relationships between the pre-merger motivations, merging process activities, and outcomes for the merged organization.

However, there are still gaps in the body of knowledge regarding nonprofit mergers that future research could address. Among topics that should receive attention:

- **Financial analyses.** Additional years of follow-up using accurate and detailed financial data could provide the information necessary to assess long-term financial effects of merger.
- **Analysis of perspectives.** Better understanding of how the perspectives of executive leadership, boards of directors, program administration, front line staff, and “merger champions” differ depending on the role they play would be a substantial contribution to the field.
- **Analysis of failed mergers.** There is a significant gap in knowledge regarding merger attempts that did not make it through the process. There would be significant benefit to be gained from a deeper analysis of the factors that influence a retreat from merger as a viable option for nonprofits, or the failure of nonprofits following a merger.



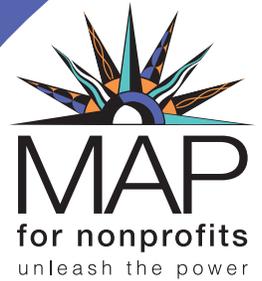
Finally, it is important to disseminate the results of this study in order that they can be discussed by those interested in nonprofit mergers and other types of realignments. Among the most important audiences are business leaders who sit on boards and support the decision making process, funders who are asked to support the merging process, nonprofit organizations that can use the information to make more educated decisions about merging, and other social science researchers looking to better understand the internal workings of nonprofit mergers.

For more information

For more information about nonprofit mergers and realignments contact Judy Alnes, MAP for Nonprofits, at 651-632-7227. For more information about the merger research, contact Greg Owen, Wilder Research, at 651-280-2700.

Full research report available

A copy of the complete *“Success Factors in Nonprofit Mergers”* is available online at www.mapfor nonprofits.org and www.wilderresearch.org.



MAP for Nonprofits
2314 University Avenue, Suite 28
Saint Paul, Minnesota 55114
www.mapfor nonprofits.org



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451 Lexington Parkway North
Saint Paul, Minnesota 55104
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