# A Qualitative Research of Mergers in Non-profit Sector

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**Abstract**

*The vast majority of people perceive mergers as being done by businesses to increasing the value of shareholders, strengthening operations and increasing profit as well as improving services, products and value for their consumers. Mergers can be used by non-profit organizations (NPOs) as a way to increase community service to share limited resources and engage assets including willingness. Even if it hasn't been widely implemented in the past, the number of NPOs taking into account such a commitment is increasing. The merger procedure of non-profit organizations is very similar to that of for-profit organizations, both in terms of process steps and factors to be tracked, such as synergies, cost savings, or other benefits. The paper is based on a qualitative research of the main issues related to the merger of non-profit organizations.*

**Key words:** mergers, non-profit organizations, synergy.
**J.E.L. Classification:** A10, M20

## 1. Introduction

Non-profit organizations have drawn attention in recent years due to the widespread "state crises". This has manifested in the last two decades in all parts of the world. In northern Europe, the non-profit sector has come to grips with the questioning of traditional policies of social protection. In the southern, central and eastern European countries, highlighting the non-profit sector has been marked by a permanent concern for the environmental degradation that continues to threaten the health and safety of people everywhere. In addition to stimulating support for market-driven economic policies, this questioning of the state has again brought attention and made new hopes for civil society organizations operating in most societies around the world (Salamon and Anheier 1997).

The non-profit sector, also known as a voluntary economy or social economy, civil society, third sector, non-profit or charitable sector, influences national and global economies, regardless of its title (Schmid, 1995).

Failure theories suggest that non-profit organizations survive in a space where government and free markets fail (Weisbrod, 1997). According to this philosophy, NPOs provide goods and services to society that are not profitable for businesses and which are underfunded by government agencies due to political realities. (McCormick, 2001).

The emergence of the non-profit sector supported the idea that neither the public nor the private sector cannot cover all the needs that exist within society (Brinkerhoff and Brinkerhoff, 2002, p.4)

The non-profit organizations are treated as non-governmental entities established "as a form of charity which doesn't seek profit for owners and whose principal purpose is the provision of public services or the defense of a cause. Therefore, they are considered to be private organizations, but aimed to fulfill public or quasi-public goals" (Vlăsceanu, 1996, p.19).

In terms of efficiency, the association of several economic entities shows that their effectiveness is greater than the effectiveness of each individual. Specifically, the value of the firm A summed up with the value of the firm B taken separately have a lower value than the combined value, the value after the merger (Sherman, 2010).

Merger operations are one of the external growth mechanisms through which businesses can better meet the purpose for which they are set up (Georgescu and Chiriac, 2013). Broadly, the merger refers to two companies that come together to become one (Sherman, 2010).

Specifically, a merger is a combination of two or more companies in which the assets and liabilities of the target firm are absorbed by the acquired firm. Although, the acquiring firm may be a significantly different organization after the merger, it retains its original identity (Sherman, 2010). Aldrich (2008) believes that firms can merge either by absorbing one another, and in this case we are talking about an acquiring firm and a target firm (one that will cease to exist) or a merger where two or more organizations will cease to exist to form a new one. Some authors believe that by merging an organization can buy another one (Singer and Yankey 1991). Often, in literature and practice, the merger term is associated with the acquisition one. Mergers refer to joining two or more organizations to establish a new organization, and the acquisition refers to the absorption of one organization by another (Ansoff and McDonnell, 1988; Golensky and DeRuiter, 1999).

There are three types of mergers between companies: horizontal, vertical, and conglomerate (The Economist Dictionary). A horizontal merger takes place when two companies are in a competitive position and offer the same services in the same geographic region. Vertical mergers are combinations of companies that have a buyer-seller relationship and are not competing with one another. Conglomerate mergers take place when companies are not competing and do not have a buyer-seller relationship, offering different products on different markets, with the goal of diversifying activity with minimal risk (Gaughan, 2010).

Finally, it is important to underline that in a successful merger, the organizations involved will negotiate a structure that is mutually beneficial and helps all parties to achieve their goals (Cartwright and Cooper, 1993).

## 2. Aspects of mergers in non-profit organization

**Defining**

Government funding to social service agencies has been on the decline in recent years (Xiao-cong and Ming-Chao, 2004), and this trend has been exacerbated by the economic downturn (Guidestar, 2009). A recession was officially declared at the end of 2007, but many states began to feel the effects of the economic downturn before 2007. This situation has affected, in the same time, the collection of funds at the non-profit organizations. The low level of resources gathered by NPOs as well as the diminishing of the funds received from the state budget forced the actors of non-profit sector to collaborate each other in order to achieve the social goal for which they were set up. More than that, non-profit organizations have been forced to merge in order to stabilize funding and to cope with changes in the economic climate. Such changes are often stimulated by new legislation and fluctuations in government funding (Golensky and DeRuiter, 1999).

Mergers between NPOs can be viewed as formal alliances used to capitalize on the strengths of organization’s competitors while also making the merged organization more attracting to funders by decreasing replication of services, increasing the ability to serve more clients efficiently, and reducing overhead expenses (Inspiration Corporation, 2006). Mergers are seen as a viable option when non-profit organizations experience increased transition costs from uncertainty in service demands, client needs, and funding (The Boston Foundation, 2009). Progressively, more NPOs have merged together as a way to address declining funding, increased competition for scarce financial resources, and expanding demand for services (Golensky and DeRuiter, 1999).

Mergers are often described as a last solution for survival in the face of intense resource competition (Singer and Yankey, 1991; Golensky and DeRuiter, 1999). More than that, mergers can be used as a strategic option by all parties not simply to grow or survive but to accomplish specific mission goals and increase impact (Cortez et al., 2009).

In Romania, the legal regulation states that the merger is done by absorbing a foundation by another one or by merging two or more foundation to form a new. Forwards, the decision to merge shall be adopted if at least two thirds of the total number of members of the management body agrees. Reorganization of non-profit organizations in a federation must not be confused with merger, because NPOs constituting in a federation retain their own legal personality, including patrimony (Ordinance 26/2000).

**Benefits and limits**

The main reason for mergers is economic uncertainty, market fluctuations, lack of resources and dependence on common sources of financing (Bastien, 1987). Economic and political uncertainty forces organizations to combine so they can ensure a steady stream of resources that they need to survive. The activity carried out together can allow merging organizations to achieve synergies such as economic synergies, financial and technological ones that help to strengthen their position on the market. (Cortez et al., 2009; Singer and Yankey, 1991; Jenkins, 2000).

Mergers aim achieving economic benefits, economies of scale, greater spread and market recognition (Kanter and Seggerman, 1986; Gaughan, 2010).

Singer and Yankey (1991) identified several reasons that may lead to collaboration or merger. Two of these reasons are increasing efficiency of the organization's activities and the ability of building a monopolistic position based on a common vision. Cowin and Moore (1996) in their study confirmed these findings. Schmid (1995) identified as additional reasons, the potential for spreading general spending, achieving scale economies, opportunities to increase lending capacity, and geographical and sectoral expansion. In case of for-profit entities, the main rationale reasons for achieving merger are the future economic benefits, while for non-profit organizations, managers may be interested in identifying an additional impulse that would lead them to merger (Cowin and Moore, 1996).

Jenkins (2000) identifies five benefits of non-profit organizations mergers highlighted bellow.

*a. Efficiency Gains through Economies of Scale*

The merger of two or more non-profit organizations into one often leads to considerable efficiency gains through economies of scale. The new organization is able to deliver services more efficiently by reducing administrative costs, development costs, and/or overhead expenses. Economies of scale are later achieved through the efficient allocation of labor and resources. A well-trained and motivated staff is an influent factor to success, both in the for-profit and non-profit sector. In case of organizations seeking to focus on the effective use of technological innovation, human capital, and personnel issues, mergers may provide a means to gain sufficient scale to address such problems efficiently.

Strategic mergers can provide NPOs the means to achieve minimal level of staff size, fiscal resources, and expertise to develop the organizational capacity to undertake and to sustain constructive and sophisticated evaluation initiatives, staff development and training programs, and to harness the advantages of modern technology.

*b. Efficiency Gains Through Economies of Integration*

Mergers can help NPOs taking advantage of vertical integration, known as the combination of distinct related processes or services within the borders of a single organization concerning the improvement of the delivery of client services and developing of their social goals. The majority of these services can be provided by multiple NPOs, but a fragmented system is inefficient and often difficult and frustrating for clients. Mergers in NPOs may lead to better coordination, linked services, or co-location which, in turn, will likely lead to a higher level of service, treatment, and benefit for the client.

*c. Salvaged Public Resources*

Permanent concern for the citizens' social interest is the reason why NPOs have advantageous tax treatment. When the resources of the NPOs are effectively used, the local community and society have major benefits. The public interest is not fulfilled when a failing non-profit organization struggles to maintain its corporate existence and imprudently expends scarce resources that might have been better used by another organization achieving the same or similar mission. Those valuable public resources are permanently forsaken.

*d. Enhanced Community Position*

Increasing the size and impact of an organization following a merger can lead to greater visibility and market recognition. A broader, more efficient non-profit organization often wields more clout, maintains political power, and lends a stronger voice which can permit the organization to influence government affairs, media relations, and public education initiatives. A merger may also provide a means to build a brand image or expand an existing platform (Jacobs, 2000).

*e. Incentives to Management*

Creating an environment where NPOs mergers take place more often may indirectly improve non-profit management. Some authors sustain that in the corporate sector, takeover activity drives managers to maximize shareholder wealth and increases "the pressure applied to managers to pursue projects that maximize market value" (Cook, 1987). Non-profit organizations, in many cases, have suffered as a result of inefficient management decisions in terms of adequate resource use or identifying innovative solutions to solve problems, or both. The decision to merge may lead to additional benefits for non-profit staff. In this respect, it is ensured that the activities they carry out create public value in order to avoid being viewed as a ripe takeover target or becoming a disposable of an employee in the event of a merger.

Cortez et al. (2009) identified the following types of strategic benefits that non-profits should seek: quality improvements in existing services; improved efficiency in existing services; increased funding; development of new skills; entry into new geographies.

Although, most studies show a high efficiency of mergers operations, empirical studies of NPOs mergers have revealed a high failure rate. Between 60% and 80% of the mergers were defined as organizational failures in achieving the expected results, cost efficiency, market control and diversification (Singer and Yankey, 1991; Pritchett, 1985; Kanter and Seggerman, 1986; Marks and Mirvis, 1986; Napier, 1989).

Failure to achieve economic stability and financial gains is often accompanied by personal disillusionment, which can lead executives and staff to leave the organization. This generates hostility as well as barriers in interpersonal communication, integration and productivity. Such disappointment also accelerates the failure of the merger (Paine and Power, 1984; Cartwright and Cooper, 1993).

Uniting different types cultures and the incapacity or lack of motivation to integrate new values and standards creates tensions and conflicts that can disrupt the merger process and even cause organizational failure (Wishard, 1985; Smircich, 1983; Mirvis, 1985).

A main disadvantage to a merger is that the surviving entity inherits all of the liabilities of the merged out entity and it is not easily possible to unwind the arrangement if it is later determined that the combination has not resulted in the benefits the parties expected. As a result, it is extremely important as part of the due diligence process to determine what assets and liabilities might be assumed by the surviving entity (Willard Boyd III, 2014).

## 3. Conclusions

The merger of two distinct organizational ideologies is problematic and creates conflicts at the structural and personal levels. The organizations with different goals encounter difficulties in accepting mutual ideologies. The inability or rejection of organizations to deal with issues related to the ideology and value of merging organizations may ultimately lead to the failure of a merger.

The success of a merger is, in a large extent, determined by the organization's ability to achieve structural integration and provide services to clients which can cover their needs. The merger of two organizations is not necessarily cost-effective, nor should it be associated with increased efficiency, effectiveness or performance. The merger directly contributes to increasing the number of organizational tasks and speeding up structural differentiation. Large organizations are experiencing functional difficulties, such as lack of flexibility and an inability to provide rapid answers to the various changes that may arise. Adopting a formal mechanical approach as a result of fast expansion is likely to cause functional problems that can be solved more effectively by a smaller organization, more flexible.

Finally, the merger should not be a purpose itself, but rather a means of achieving the objective of improving customer services. The fighting which continues to control strategic positions, resources and policy-making authority may cause merged organizations to deviate from their sustained goals. This poses a threat to the legitimacy of the organization and, ultimately, to its survival.

Further research is needed on the relevant factors for successful and unsuccessful mergers. Current literature provides leaders with guidance on human staff-related elements to adapt to change, also managing their own anxiety and confusion.

Non-profit mergers should be less frightful and stressful on a personal basis than for-profit mergers. While cutting costs and taking advantage of economies of scale are important, due to NPO's focus on mission there is usually no stated goal of downsizing staff or significant reduction in services. The factors that produce fear in those caught in for-profit mergers, such as loss of jobs, relocation, reduced pay, and less authority and responsibility in positions, are rarely a significant, direct result of a merger in NPOs.

In the present paper, based on a qualitative research, a number of advantages and disadvantages have been identified regarding the merger of non-profit organizations. We have noticed that some authors, based on conducted studies, believe that merger operations would lead to considerable benefits in terms of achieving the proposed goal, while other authors see the merger as a failure. In view of these assertions, we believe that it would be appropriate to analyze the merger projects carried out between these types of organizations. Analysis before and after the merger could lead to clearer results with regard to the subject concerned.

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