MERGER CASE STUDY

Merger between Economic Opportunity Council of Suffolk, Inc. (EOC) and Suffolk Network on Adolescent Pregnancy, Inc. (SNAP)

This case study is based on CAPLAW's interview with Adrian Fassett, President/Chief Executive Officer of Economic Opportunity Council of Suffolk, Inc. (EOC) in Patchogue, New York, as well as a review of EOC's website and its IRS Form 990.

Economic Opportunity Council of Suffolk, Inc.

Economic Opportunity Council of Suffolk, Inc. (EOC) is a 501(c)(3) Community Action Agency (CAA) with annual revenue of approximately $9 million and about 200 employees. EOC provides the following services to low-income people in Suffolk County, on Long Island, New York:

- Family development services to help clients: improve job skills; secure higher paying, more fulfilling employment; effectively manage conflicts between family and job demands; master budgeting skills; and strengthen family relationships
- Housing services, including: affordable housing development; down payment and closing cost assistance to eligible first time homebuyers; homeownership counseling; mortgage counseling for homeowners who are having difficulty maintaining their mortgage; and reverse mortgage counseling for seniors
- Child care services at two centers and at Suffolk County Family Court
- Youth and adolescent programs – including adolescent pregnancy prevention, parenting programs for adolescent parents, a middle school after-school program, and a program that helps at-risk youth prepare for and graduate from college
- HIV/AIDS case management, prevention and outreach
- Services for people with developmental disabilities, including: Medicaid and non-Medicaid service coordination; respite/recreation services; individual support services; community habilitation services; and group day habilitation services
- Community-based community revitalization and crime prevention services funded by the U.S. Department of Justice's Weed and Seed Program

Suffolk Network on Adolescent Pregnancy, Inc. (SNAP)

Suffolk Network on Adolescent Pregnancy, Inc. (SNAP) was a 501(c)(3) organization that focused exclusively on adolescent pregnancy prevention programs in Suffolk County, NY. Prior to the merger, it had annual revenue of approximately $1.5 million and 21 employees. The merger was completed in March 2011. After the merger, EOC hired most of SNAP's staff, including its executive director. SNAP is now a division of EOC. One SNAP board member – the board chair – joined the EOC board. SNAP ceased to exist as a separate corporation.

Reasons for the Merger

According to EOC's president/CEO Adrian Fassett, SNAP was having a difficult time financially because it only provided a single type of service – adolescent pregnancy prevention. SNAP was experiencing cash flow problems and, on occasion, problems making payroll. Although SNAP probably could have survived on its own, the SNAP board felt that it would be beneficial to find a merger partner before the organization was in such dire straits that it had to merge or dissolve.

The EOC board viewed the potential merger as an opportunity for EOC to broaden its services and outreach into the public schools in Suffolk County, where SNAP operated well-respected programs. In addition, at the outset, the EOC board believed that SNAP had a $260,000 surplus and that the merger would improve EOC's overall financial condition. "[W]e thought that, financially, it wouldn't put a stress on us," says Mr. Fassett.

"Programmatically, it just made sense; it fit. It was a gap in services that [EOC] had that [the merger] would fulfill."

How Merger Talks Were Initiated

According to Adrian Fassett, who was a SNAP board member at the time, the SNAP board "had talked with some other potential partners and it didn't work out. I never brought up my agency since I thought it was a conflict of interest because I was a board member. And then I was approached by the board chair and [SNAP's executive director] about a possible merger." He notes that the two organizations were familiar with each other because they had worked together over the years and because of his service on the SNAP board.

Both organizations' boards met to discuss whether they wanted to explore the possibility of merging further. Mr. Fassett resigned from the SNAP board to eliminate the conflict of interest between his role as a SNAP board member and as the president/CEO of the organization with which SNAP was considering merging.

The Merger Process

Board Resolutions After initial merger discussions, the boards each met separately and voted to explore the possibility of merging, including conducting due diligence and forming a merger committee with representatives from both organizations. Later, after due diligence and resolution of outstanding issues by the merger committee, each board voted to complete the merger.

Due Diligence Because he had resigned from the SNAP board, Adrian Fassett could not describe the due diligence process SNAP used. He reports, however, that "[EOC] went through [SNAP's] audit reports, financial statements. We talked to their funding sources. We visited their programs. We spoke with other community partners... [W]e were very familiar with them, so there was a lot we knew about the organization already."

Merger Committee "Then we started discussing what the merger would look like if it did take place – would we keep all their staff, would we keep their executive director, those type of things," Mr. Fassett explains. The SNAP and EOC boards formed a merger committee which included some SNAP board members, some EOC board members, and executive staff from each organization. The merger committee's goal was to iron out issues in areas such as governance, staffing, policies and procedures, personnel policies, and employee benefits. "We were able to do that smoothly ... in one meeting," he notes.

Government Grants and Contracts Of transferring SNAP's government grants and contracts and getting funding source approval, Mr. Fassett observes, "That was actually the easiest part. We got approval from all government funding agencies before the state [i.e., the New York Attorney General, the New York Supreme Court and the New York Department of State] approved the merger ... The funding sources were the easiest issue, and we thought it would be a big deal. We had no problem with any of them." "One of the reasons for that," he explains, "is that we had a prior relationship with [SNAP's] funding sources already. They knew our agency and our work, too. So that was simple, we had not one problem with a funding source."

Communication Throughout the merger process, both organizations communicated regularly with their staff. "Internally, both agencies had agency-wide meetings with their staff to explain what they were doing, and we had updates every three months with our staff," Adrian Fassett recalls. "On the outside it was pretty well known ... that we were contemplating [the merger] ... it was in the paper," he says. "Then when the merger was completed,

we had a big community dinner and night out where we invited politicians, other community-based organizations [and] partners."

Working with Professionals EOC worked with an attorney and its accounting firm on the merger. The attorney drafted the plan of merger and filed the certificate of merger with the state to effectuate the transaction. EOC's accounting firm worked with EOC to ensure that SNAP's books were in order and were transitioned over properly to EOC's financial software system.

Merger Costs The primary expense associated with the merger was about $15,000 in legal fees, which was paid out of SNAP's unrestricted surplus funds. EOC's accounting firm worked on a pro bono basis.

Integration of the Two Organizations

Much of the work of integrating the two organizations actually took place before the merger was finalized. Adrian Fassett explains that "physically, programmatically, and financially, we did the integration before the merger actually became effective." The integration was overseen by a transition team, consisting of EOC's management team plus SNAP's former executive director and finance director.

Board Composition EOC made one seat on its board available for one of SNAP's board members. SNAP designated its board chair to serve on the EOC board.

Staffing EOC took on all but two of SNAP's employees. It hired SNAP's executive director, who had founded SNAP and is well-respected and well-connected in Suffolk County, to manage its SNAP division. It also brought on SNAP's fiscal staff to augment EOC's finance department, as well as most of SNAP's program staff. Despite the pre-merger integration of most aspects of SNAP into EOC, SNAP's employees were not brought onto EOC's payroll until the merger was finalized.

While he was a board member of SNAP, Adrian Fassett had made recommendations to SNAP regarding its employee benefits based on EOC's benefit plans. Thus, SNAP's benefit plans were similar to EOC's and administered by the same company and moving SNAP's employees onto EOC's benefit plans proved relatively simple.

Facilities and Equipment SNAP was able to negotiate out of its leases for facilities and equipment with no penalty based on the fact that it would be merging into EOC. Before the merger was complete, SNAP staff moved out of SNAP's facilities and into EOC's.

Finances EOC began integrating SNAP's financial data into its accounting software prior to the merger. This task was made easier by the fact that SNAP used the same accounting software as EOC, based on a recommendation Adrian Fassett had made years earlier in his capacity as a SNAP board member. Initially, SNAP was treated as a separate entity in EOC's accounting system. Eventually, however, SNAP's finances were integrated into EOC's as a separate division of EOC. SNAP had a $50,000 line of credit secured by its receivables, which was transferred to EOC.

Merger Benefits

There have been both programmatic and financial benefits to EOC from the merger, according to Adrian Fassett. First, it has enabled EOC to expand its programs and outreach into the public schools in its service area. SNAP brought to the merger its "well-respected programs in all the school districts in the community," he notes. As a result, he says, EOC has been able to "bring in some additional resources into our programs. And the schools have opened up new partnerships, so it has worked well." He provides the following example: "Through our adolescent pregnancy prevention programs, we do assessments of families and make referrals to our family development program … [T]hat [has] helped us as far as growing our family development program, and it [has been] a tremendous asset to the program … the school superintendents really love[] that piece of it. It was a value-added bonus there." Second, the merger has provided additional funding and finance staff for EOC.

Presumably, the merger has also benefited SNAP by enabling it to continue its programs within an organization that has a broader range of programs and is more financially secure.

Overall, Adrian Fassett says of the merger that "It has been very successful. And with funding issues and the way money is now, that $1.5 million dollars really helped out my agency and the programs are wonderful."

Merger Challenges

There were three main challenges to the merger. First, SNAP's surplus turned out to be smaller than EOC had originally thought. Second, it took longer than anticipated to obtain approval of the merger from the state. And, third, integrating the two organizations' cultures took more effort than anticipated.

A closer examination of SNAP's books revealed that SNAP had a surplus of only about $72,000 and not $260,000. Adrian Fassett explains that "Once we had agreed to go ahead with the merger and the train had left the station and was going down the track, we had started combining our operations before the merger." "When we started combining their books onto our books," he recalls, "we found out their auditing firm had made a $90,000 mistake. So their $260,000 surplus was not really $260,000. Then we found another misstatement, so it came out that their surplus was only about $72,000. But at that point it was past the point of no return."

Another hurdle was the fact that the state was slow to approve the merger. In New York, mergers of nonprofits formed for charitable purposes must be approved by the Attorney General, the New York Supreme Court, and the New York Department of State; funding sources or licensing agencies whose approval or consent is required must also sign-off on the transaction. One thing that slowed the approval process, according to Mr. Fassett, was the fact that an attorney from the state "picked up that … my agency had started doing childcare and …we didn't have the right certification with the state in terms of nonprofit status. So we had to re-file our status for our nonprofit standing before they could go ahead and approve the merger."

"The most challenging issue we faced was corporate culture," Adrian Fassett recalls. "SNAP was a predominantly Caucasian organization with all Caucasian management, and my agency was a predominantly minority agency with all minority management. Their corporate culture was totally different, more laid back." He observes that "it took a good year and a half, almost two years to get this culture thing worked out."

Lessons Learned

Merging with an organization with which your CAA already has a solid relationship facilitates the process – from initiating merger talks through integration.

Communicate with the funding sources of both organizations early and often during the merger process.

Conduct thorough due diligence, especially financial due diligence, before beginning to integrate the two organizations. It is important to get a complete and accurate picture of a merger partner's financial position, especially whether it has any hidden liabilities such as unpaid payroll taxes or outstanding legal claims, before getting "past the point of no return."

Before merging, have an attorney check that both organizations are up-to-date on all of their corporate, tax and other legal filings and that those filings have been done correctly.

Most importantly, don't underestimate the importance of organizational culture. "Cultural integration begins with cultural awareness and sensitivity – and fostering these should be an important element of the entire merger process, from assessment and negotiations through integration," merger consultants LaPiana Associates explain in *The Nonprofit Mergers Workbook Part II: Unifying the Organization after a Merger*. "No matter how successful other integration efforts may be, if issues around organizational culture are not considered and attended to, the merger will not achieve its potential."[1]

This case study was created by Community Action Program Legal Services, Inc. (CAPLAW). Visit us at www.caplaw.org.

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Footnote:

1. LaPiana Associates, Inc., *The Nonprofit Mergers Workbook Part II: Unifying the Organization after a Merger*, p. 79.