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STRATEGIC RESTRUCTURING: A *Tool for Improving Organizational Effectiveness*

Echoing across Pittsburgh's hillsides, for at least two decades, has been a call that this region's nonprofit organizations must achieve greater economies of scale. Fairly or unfairly, nonprofits have been challenged to reduce administrative costs, eliminate duplicative services, and seek collaborations with peer agencies. Indeed, in February 2001, The Forbes Funds advanced this call by hosting a Leadership Roundtable featuring James Austin, the John G. McLean Professor of Business Administration at the Harvard University School of Business Administration, who presented numerous case studies and examples of strategic alliances and provided practical, down-to-earth strategies for local nonprofit staff and trustees. In 2003, The Forbes Funds commissioned David La Piana, Michaela Hayes, and Natasha Terk of San Francisco-based La Piana Associates, Inc., arguably the nation's leading resource on strategic restructuring for nonprofits, to examine the lessons learned from mergers, alliances, and joint ventures involving local nonprofits. In cooperation with The Forbes Funds, La Piana, Hayes, and Terk conducted case studies of ten agencies located across Pittsburgh.

WHAT IS STRATEGIC RESTRUCTURING?

Strategic restructuring—mergers, alliances, joint ventures, and other forms of strategic partnerships—is a tool used by nonprofit organizations that seek to improve their organizational effectiveness. It is used across the country and even more so in certain urban areas—such as Pittsburgh—where the number of nonprofit organizations grew dramatically in the past decade. These environments are laden with challenging dynamics, including increased competition for funding and other resources, such as qualified staff. Times of economic downturn exacerbate this situation. Strategic restructuring can offer organizations in crisis—due, for example, to shortfalls in funding, increased competition, or departure of an executive director—a means of survival or a way to assure continued advancement of mission. Of broader interest is the use of this tool to improve organizational effectiveness in general.

HOW COMMON IS IT?

Strategic restructuring is not new in the sector, as revealed in findings from previous research and demonstrated by some of the organizations included in the study sample. However, there is an increasing awareness of this tool, due to various factors. These include an increased focus in the sector on organizational effectiveness, in part motivated by foundation interest in improving the effectiveness of grantmaking. This is exemplified by the emergence, in 1998, of Grantmakers for Effective Organizations (GEO)—a grantmaking affinity group that works to improve both nonprofit and philanthropic effectiveness. Strategic restructuring is a promising tool for achieving this outcome.

During the past five years, the amount of information on, and interest in, strategic restructuring has increased dramatically. Contributing to this is the Strategic Solutions project, an initiative funded by three California-based foundations: the James Irvine, William and Flora Hewlett, and David and Lucile Packard foundations.¹ Since 1998, this project, managed by La Piana Associates,



Envisioning Pittsburgh's nonprofit sector as innovative, informed, and engaged, The Forbes Funds advance capacity-building within and among the region's nonprofit organizations.

THE COPELAND FUND FOR NONPROFIT MANAGEMENT

The mission of The Copeland Fund for Nonprofit Management is to strengthen the management and policymaking capacity of nonprofit human service organizations to serve better the needs of their communities.

- Management Enhancement Grants
- Emergency Grants
- Cohort (Professional Development) Grants

THE TROPMAN FUND FOR NONPROFIT RESEARCH

The mission of The Tropman Fund for Nonprofit Research is to support applied research on strategic issues that are likely to have profound effects on nonprofit management and governance, especially among human service and community development organizations.

- Applied Research Projects
- Annual Research Conference

THE WISHART FUND FOR NONPROFIT LEADERSHIP

The mission of The Wishart Fund for Nonprofit Leadership is to encourage pioneering nonprofit leadership by promoting public learning and discussion about issues critical to ethical and effective management, as well as by celebrating exemplary practices.

- Leadership Roundtables
- The Frieda Shapira Medal
- Alfred W. Wishart, Jr., Award for Excellence in Nonprofit Management

has focused its efforts on increasing the sector's awareness and understanding of strategic restructuring. The large and increasing number of articles on strategic restructuring in both sector-specific publications, as well as in the popular press, is indication of increased interest in, and use of, this tool for improving organizational effectiveness. In the past year, the interest has spiked, due in part to the economic downturn and the resulting financial difficulties that nonprofits are facing.

WHAT IS THE ROLE OF STRATEGIC RESTRUCTURING IN PITTSBURGH?

The nonprofit sector in Pittsburgh shares many of the challenges faced by nonprofits throughout the country. Reduced government and foundation funding is placing great pressure on the sector, which has experienced a proliferation of new nonprofits during the past decade, thus increasing the competition for a smaller pool of funds. This is certainly the case in Pittsburgh. Further exacerbating this situation is Pittsburgh's weak economy and resulting broad-based job losses. The result has been an increased need and demand for services, especially in the health and human services subsectors which serve as a "safety net."

The impact of these trends is evidenced in increased competition among nonprofits and also from for-profit entities. This is most acute in the health and human services subsectors. For-profits have entered this market seeking to expand their base through government contracts, including those focused on bringing managed care to federal and state-funded programs, such as Medicaid, and to county-funded programs.

As the Pittsburgh nonprofit sector, and particularly the foundations that support it, strives to address these interrelated challenges, it will be important to provide leaders more information about strategies available to improve the effectiveness of their organizations. Among these, strategic restructuring has shown great promise. However, in order to make the best use of this tool, nonprofit leaders need to understand:

- When strategic restructuring is an appropriate strategy (i.e., for what situations);
- What outcomes are reasonable to expect;
- What form of strategic restructuring is best for the organizations involved; and
- How to increase the likelihood of achieving the desired outcomes.

Similarly, foundations, concerned about improving the effectiveness of the nonprofits they support, can benefit from this information as well. For all involved, having clear and realistic expectations of the potential outcomes is perhaps most important.

HOW EFFECTIVE IS STRATEGIC RESTRUCTURING?

While there is a growing body of knowledge about the factors that support effective negotiation and integration of strategic partnerships, much less is known about the actual outcomes nonprofits experience and how these compare to their expected outcomes, prior to the strategic restructuring. The Forbes Funds commissioned La Piana Associates to address these questions,

specifically as they relate to the health and human services subsectors in the Pittsburgh nonprofit community.

STUDY METHODOLOGY

Strategic restructuring, especially in its more complex form of corporate integration (e.g., mergers, joint ventures), typically spans a multi-year period from pre-negotiation discussions through negotiations and integration. Further, while there has been an increase in activity related to strategic restructuring in the sector, within any subsector (e.g., human services), and within any given geographic area, there are a finite number of such partnerships developing at any one point in time. For these reasons, La Piana Associates used a retrospective case study approach to investigate the research questions. This involved in-depth interviews with the leadership of ten nonprofit organizations identified as study participants by The Forbes Funds. Separate interviews were conducted with two leaders from each organization, the executive director, and a board member (typically, the board chair). This allowed comparison of responses and provided different perspectives on the process and outcomes.

The study participants represented a variety of types of strategic restructuring, spanning the partnership continuum from strategic alliances—administrative consolidation and joint programming—through corporate integration—joint venture, management services organization, parent subsidiary, and merger. (See Figure 1: The Partnership Matrix.) Not only did the types of strategic restructuring differ, but these organizations also differed along many other dimensions. Through the in-depth interviews, La Piana Associates gathered both qualitative and quantitative data that would provide measures of change in organizational effectiveness. La Piana Associates then sought to determine whether these could be attributed to the strategic restructuring.

WHY DO NONPROFITS PURSUE STRATEGIC RESTRUCTURING?

One objective of this study was to learn to what extent the Pittsburgh nonprofit sector is the same as, or different from, other similar urban areas throughout the country. Prior research studies—both La Piana Associates' studies and those of other researchers—as well as La Piana Associates' field experience have found that the reasons for pursuing strategic restructuring generally fall into a few key categories. These are to:

- Increase efficiency—in particular, to reduce administrative expenses;
- Serve the community (stakeholders) better by offering more and/or an expanded continuum of services;
- Respond to increased competition (e.g., for clients and/or funding); and
- Address leadership challenges (e.g., the departure of a skilled ED, or a "burned-out" board).

SUCCESS FACTORS AND CHALLENGES IN STRATEGIC RESTRUCTURING

Strategic restructuring is not easy. It requires dedication, time, focus, and patience—all in addition to the day-to-day management and operation of the organization. While it can reduce

expenditures, it also often requires *new* expenditures. Even in consolidation of administrative functions, where the potential for reducing expenses is greatest, there are expenses involved, such as new and/or expanded IT capabilities to handle the increased volume of transactions (i.e., more clients, more services delivered). Over a period of time, increased volume and the associated revenues may counterbalance the additional expenses.

Research studies and first-hand experience reveal several factors that make it more likely that a strategic restructuring will achieve its objectives. These include:

- Having a “champion”—someone in a leadership position who acts as a cheerleader of sorts for the partnership;
- Positive experiences and relationships—past positive experience with collaboration/ partnership, especially between the organizations involved, to help build the trust that is so crucial to a successful partnership;
- Honest, frequent, and clear communication;
- Positive board/ED relations and the absence of internal conflict;
- Risk taking/growth orientation; and
- Focus on mission—being able to keep the ultimate objective in sight and rallying staff and board to this shared vision.

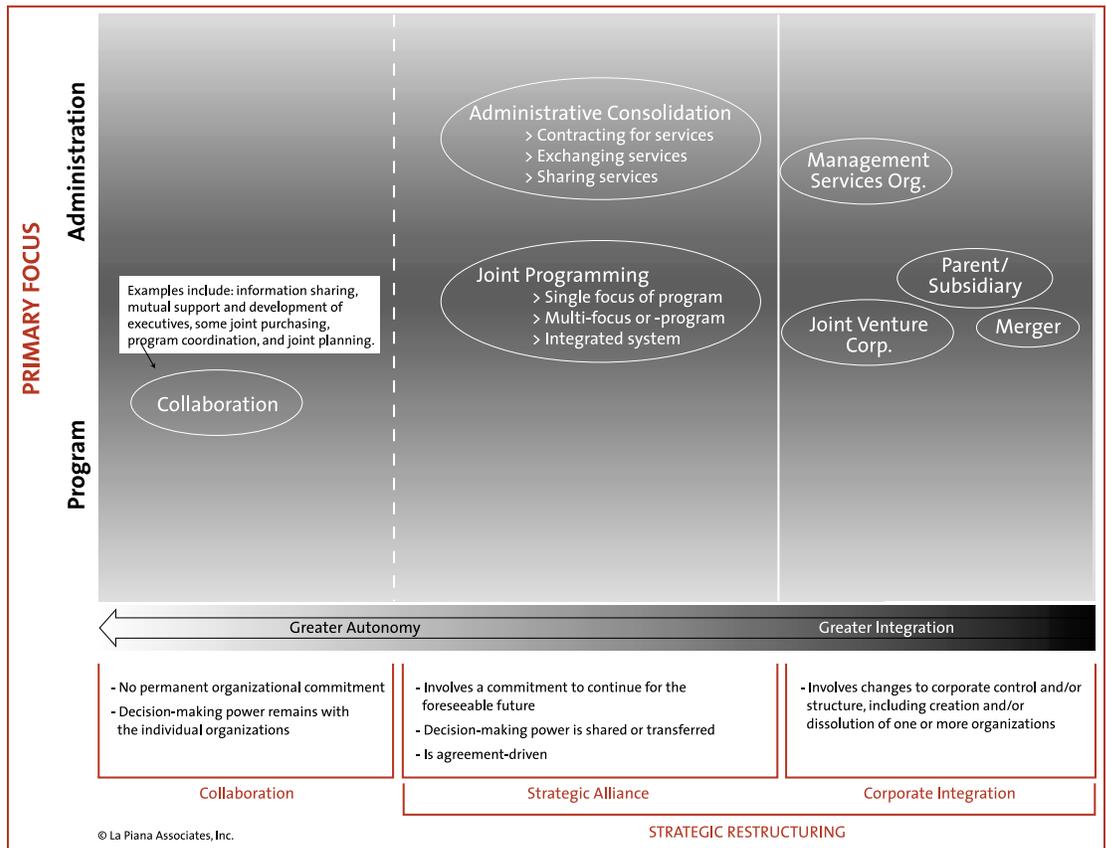
These success factors help organizations overcome the key challenges that arise, including:

- Autonomy concerns—fear of losing individual autonomy, “ego” issues, and lack of trust; and
- Conflicting organizational cultures²—While it pervades all aspects of an organization, organizational culture is not always something of which those outside of an organization (or even those inside it) are consciously aware. Often differences in organizational culture do not become apparent until the implementation phase of strategic restructuring when staffs begin working together.

EXPECTED OUTCOMES: OBJECTIVES OF STUDY PARTICIPANTS

In undertaking strategic restructuring, the Pittsburgh nonprofits participating in this study sought to achieve a range of objectives related to organizational effectiveness. These varied by organization and included:

FIGURE 1: The Partnership Matrix



- Reducing competition for donors;
- Reducing competition from for-profits;
- Meeting an unmet community need—e.g., providing needed services where no one else was offering them;
- Sustaining a needed program—e.g., helping to maintain the services of an organization on the brink of closure;
- Offering a continuum of services—e.g., partnering so services could be coordinated in a manner that would be beneficial as well as transparent to clients;
- Reducing administrative expenses;
- Enhancing IT capacity;
- Offering a better benefit package to employees; and
- Increasing visibility and reach.

ACTUAL OUTCOMES: STUDY FINDINGS

In general, study participants felt their strategic restructuring had been successful in improving their organization’s effectiveness. While (a) the degree of success varied, (b) the time to implement the strategic restructuring fully was often longer than anticipated, and (c) the specific success factors were not entirely what was originally expected, study participants were able to point to specific indicators of success, including:

- Improved services and service delivery—This was the most frequently cited outcome;
- Decreased costs—This was also a frequently cited outcome. In particular, specific administrative costs decreased for many of the study participants;
- Decreased competition, increased market awareness, and improved (more competitive) market position;

- Improved organizational infrastructure, including enhanced capabilities in marketing and IT, and better healthcare and other benefits for staff; and
- Increased ability to recruit staff, volunteers, and board members.

SUCCESS FACTORS FOR STUDY PARTICIPANTS

Among the factors contributing to the study participants' success were:

- Careful, thorough planning;
- Patience and flexibility;
- Good relationships and trust between the partners;
- Funder support (in all stages)—both encouragement and funding;
- Shared vision and focus on mission;
- Board involvement and support;
- Strong leadership that kept people motivated and focused on the shared mission and desired outcomes;
- Early agreements about leadership—e.g., who would be the executive director; and
- Outside expertise—Although the participants tended not to use outside consultants, those that did felt that this had been helpful.

A few factors were specific to the Pittsburgh community:

- Funder support—Several interviewees mentioned that, during the mid to late 1990s, funders in Pittsburgh were encouraging nonprofits to collaborate.
- Close-knit nonprofit community, particularly in the human services subsector—One commonly cited success factor in strategic restructuring is previous relationships (e.g., collaboration, peer networks) between nonprofits. Leaders in Pittsburgh's health and human services subsectors tend to know or know about each other.
- Threat of for-profits entering the market—During the 1990s, many of the nonprofit leaders in the health and human services subsectors faced a common threat in the form of for-profit entities. This threat made nonprofits more inclined to work together.

CHALLENGES FOR STUDY PARTICIPANTS

The challenges that study participants experienced are similar to those that typically arise in strategic restructuring. These include:

- Changes in the external environment and changes in motivating factors—Threats, such as those posed by external competitors, often drive nonprofits together; if, however, the threat dissipates before the involved organizations have solidified their partnership, then there tends to be less motivation to continue.
- Delayed programmatic integration—Organizations have a tendency to stop working once they have negotiated the strategic restructuring. However, the most difficult work often lies ahead. If there is not follow-through, the organizations tend to be consumed in their day-to-day work, resulting in the strategic restructuring never being fully implemented or being significantly delayed. This was the situation for a few of the study participants.

- Operating in separate locations—The implementation process is much faster and smoother if the organizations are co-located. If they are not in the same building, having frequent face-to-face interaction is at least helpful. This lack of shared space and/or "face time" was challenging for several participants.
- Creating a unified organizational culture.
- Poor communication—Good communication is one of the most important factors in successful implementation of strategic restructuring. Lack of honest, frequent, and clear communication can create major problems and impede the implementation process, especially when the partnership involves multiple organizations in different locations.
- Lack of adequate systems to support the new entity.
- Internal changes, especially the departure of key leaders—Just as having a champion for the strategic restructuring is a success factor, not having one is a major challenge. Often, there are periods of significant uncertainty in the course of strategic restructuring. During these times, key leaders may leave the organization, causing further confusion and anxiety.
- Constrained resources—Strategic restructuring, while it can reduce expenditures, also requires the expenditure of resources.

SUMMARY

Overall, La Piana Associates found that the study participants achieved positive outcomes—in the form of improved organizational effectiveness—from their strategic restructuring efforts. Interestingly, study participants often embarked on strategic restructuring without having a complete understanding of the factors associated with success, nor of the challenges that they would encounter along the way, especially in the implementation phase. Given the positive outcomes that study participants experienced, the current challenges facing the sector, and the need for increased organizational effectiveness, nonprofits would benefit from having more information about strategic restructuring. This includes information about what to expect and tools to increase the potential for positive outcomes.

Funders can help make these resources available to nonprofits. However, they must tread a delicate line between providing information and support, and tipping the balance of power and making nonprofits feel they *must* undertake a given course of action because funding is dependent upon it. Of importance is the role a funder elects to play in providing information and practical support. Each foundation's approach will be dependent upon the foundation's general relationship with its grantees. Above all, foundations should themselves be aware of the information and tools that are available.

¹ Interested readers are encouraged to visit the Strategic Solutions web site (www.lapiana.org/ss/index.html) for information and other resources on strategic restructuring, including an extensive list of publications by researchers and practitioners throughout the country.

² Organizational culture encompasses the way people communicate with each other; the way they resolve conflict; and how they celebrate, reward, lead, manage, do their work, break down and assign work, and relate to each other. It is the core of the organization's belief system.

This TROPMAN REPORT is one of a series of briefing papers generated by The Tropman Fund for Nonprofit Research. TROPMAN REPORTS in this 2003 series are:

1. The Precarious Billion Dollar Sector: *Nonprofit Human Services in the Pittsburgh Metropolitan Area*
2. **Strategic Restructuring: A Tool for Improving Organizational Effectiveness**
3. Identifying Financing Opportunities for Pittsburgh-based Social Enterprises: *Challenges and Opportunities for Capitalizing Entrepreneurial Ventures*
4. Keeping Our Promise: *The Use of Modern Quality Assurance in Nonprofit Management*
5. The Challenge of Nonprofit Leadership: *A Comparative Study of Nonprofit Executives in the Pittsburgh Region*
6. When the Current Is Strong, Only the Big Fish Swim: *The 2002 Wage & Benefit Survey of Southwestern PA Nonprofits*
7. The Insurance Muddle: *Addressing Healthcare Costs for Nonprofit Sector Employees*
8. Diversity Within and Among Nonprofit Boards in Allegheny County, PA

To read the full text of this study, log onto The Forbes Funds' web site at www.forbesfunds.org.