

So much at stake

A CASE STUDY

The Collaborative Workout of the Women's Community Development Organization that Saved 87 Units of Supportive Housing in 12 Projects





1401 -1407 East 2nd St. & 216 N. 14th Ave East. Provides 21 family and single units of transitional housing.

Purpose of this report

The intent of this report is to describe the phases of growth of a Minnesota nonprofit housing development organization with a cutting-edge vision. This organization experienced phenomenal growth and had remarkable impact in its early years, but faced many daunting mid-life challenges and eventually experienced a gradual but persistent decline in its capacity and ability to remain solvent and fulfill its mission.

After years of award-winning accomplishments mixed with operational challenges, this dynamic organization underwent a painful but exemplary workout process that involved the organization's key leaders, its historical funders, and numerous community stakeholders. The final result was an orderly transfer of its assets to a more financially sound nonprofit housing organization and continued mission impact on the lives of hundreds of vulnerable women and children. In total, twelve unique housing developments dedicated to meeting the needs of underserved women and children were preserved. The organization's greatest asset — affordable housing with services — was successfully stabilized and preserved through a collaborative process that engaged a broad base of funders, public officials, community leaders, and members of the organization's staff and board.

It is common to hear about lessons learned from successful experiences, but less common to hear the invaluable lessons that come out of unwelcome change, instability or even the dissolution of a once dynamic organization. This case study attempts to provide an overview of the remarkable growth, decline, carefully planned transition, and orderly transfer of the assets of one such organization.

This report also aims to provide some perspective on how nonprofits tend to evolve over time, the early and exciting phases of growth, the challenges of managing operations at full-scale, and certain early signs that indicate a housing nonprofit may be facing challenges and possibly faltering. By sharing the story of the Women's Community Development Organization (WCDO), the Greater Minnesota Housing Fund anticipates that the leadership of other housing organizations may recognize the early indications that extra help and expertise may be needed to manage change and achieve long-term stability. GMHF also wants to share these findings with other funders of nonprofit housing developers so funders can learn where and when to invest extra resources to strategically assist their grantees.



About the Greater Minnesota Housing Fund (GMHF)

Greater Minnesota Housing Fund (GMHF) was established in April 1996 in a joint effort of The McKnight Foundation and Blandin Foundation to address the urgent need for safe, decent and affordable housing in Greater Minnesota, which includes the 80 counties outside of the Twin Cities metropolitan area.

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WCDO'S MISSION

WCDO was established in 1986 with the vision of offering services that assist women and children who are experiencing violence, homelessness and chronic poverty and to create an environment that strengthens a woman's belief in her ability to influence the direction of her life.

The vision of the Women's Community Development Organization (WCDO)

From its earliest days, the Women's Community Development Organization, (WCDO), formerly known as Women's Transitional Housing Coalition, Inc., was an agent of social change. The Duluth, Minnesota-based organization was dedicated to serving women in need. Battered women, victims of sexual exploitation or abuse, teenage mothers, women who needed to complete their education, women who needed a path to build their career skills, women who, more than anything, needed a roof over their heads from which to be safe and begin to build a new life.

WCDO's founders channeled their impressive leadership skills and poured their passion energies into the mission of saving and changing the lives of vulnerable women and children. They secured safe houses and other secure transitional housing where women could stay for up to 18 months. Through comprehensive programming they gave their clients a new foundation upon which to build, including: counseling on parenting, legal assistance in custody disputes, recovery from addiction, job readiness training, on-the-job experience in the construction trades, assistance in creating new "life plans" and completing their education and getting a permanent job.

WCDO's work attracted widespread political support and enlightened new partnerships with law enforcement, as well as significant funding resources, ardent volunteers and a dedicated staff and board. In many ways WCDO was the heart of the women's movement in Duluth. With homeless and runaway youth at startling levels, WCDO's mission was timely and the organization rose to meet the need. WCDO made inroads into the social sector as well; they worked closely with public officials to improve relations among their clients and the police, medical personnel and social service providers.

Clients, funders, and peers agreed; WCDO was on the cutting-edge of social service delivery, and they were effective. They pursued social change and institutions responded. They had the ability to lead and had a passion for organizing.

In 2002, Greater Minnesota Housing Fund (GMHF) took its board of directors to WCDO for a site visit in Duluth, and by all accounts it was a very moving experience. A client of WCDO's, a 14-year-old girl with an infant, spoke to the assembled board members. She presented her personal goals for her child and for herself, outlining her educational objectives and her career aspirations. Board members were moved, and more importantly, impressed. It was a powerful expression of the extent to which WCDO could improve the lives of their constituents.

This site visit was pivotal in shaping GMHF's decision to begin to fund permanent, supportive housing projects throughout Minnesota. Since witnessing the powerful effects WCDO and organizations like it could have on

the lives of homeless families, GMHF went on to invest over \$32 million in permanent gap funding and predevelopment loans to 52 different developments, resulting in 883 new units of supportive housing with services.

WCDO founders and its subsequent leaders excelled at designing strategies and realigning their own services and programs as well as those in the public agencies it and its clients needed to work with. These innovations were viewed as breakthroughs and created real systems change. But as time went on, it became apparent that the work of building innovative programs and advocating for much-needed systems change, and even real estate development, was fundamentally different than the challenges of property management, asset management, reporting and compliance. These latter tasks required strong internal systems and more consistent management. A transition was needed to employ more formal policies and procedures, more guidelines and rules for when to be flexible with clients and when to require greater accountability. Job responsibilities needed redefining, expenses and revenues needed to be stabilized, and the frequency of leadership changes among both board and staff needed to be addressed.



1802 E. 2nd **Street.**Provides 26 units of affordable housing for women and children.

A brief history of Women's Community Development Organization

Passionate leaders with a bold agenda

In 1986 a group of visionary women founded Women's Transitional Housing Coalition, renamed Women's Community Development Organization (WCDO) in 2004, with the mission "to create an environment that strengthens a woman's belief in her ability to influence the direction of her own life," by providing safe, decent and affordable housing, program services and advocacy services to achieve her goals.

The goal of WCDO was to provide the housing and services homeless women needed to stabilize their own lives and the lives of their children, to develop self-sufficiency skills, and engage with the larger community through education and employment. WCDO's principles of community building, participation in the social and economic environment and the economic empowerment of women infused WCDO's programs, its advocacy and its service delivery. These empowerment values also permeated the organization's staff management, board governance and property management practices.

The founders of WCDO who themselves brought extensive nonprofit service and management experience, also deeply understood the population they served, having worked extensively with women in Duluth who had been victims of abuse, were homeless, or were at risk of homelessness.

High impact and profound early accomplishments

WCDO's founders assessed the availability of housing in the community for their constituents and found it completely lacking in several ways: existing scattered-site housing was inadequate and lacked services; it was often unsafe and less than secure; it was not clustered in a way that fostered a sense of community among residents, and it did not provide for the residents to have a voice. WCDO made the decision to wade into the property development arena themselves. After two years of grassroots organizing, project planning and fundraising, they opened Duluth's first women's transitional housing project in March 1988. The project provided 21 units of much-needed supportive housing for very poor and underserved women and children.

Thus, WCDO was born out of a strong mission and dedication to serve a specific underserved population. WCDO was known for occasionally strident advocacy which at times created tensions between WCDO and other nonprofits, its service providers, the city of Duluth, and even the Duluth Housing and Redevelopment Agency (HRA). This is not uncommon for advocacy organizations seeking to create change and rebalance social equity. While it is more common in the advocacy realm, it is less common in community development organizations seeking to form ongoing community partnerships. This is one example of how WCDO blended its advocacy role with its community development agenda, and it was common for these dual roles to create challenges for WCDO, and its many new partners and allies.

Organizational growing pains, internal limitations, emerging challenges
Before WCDO's first decade was out, the organization began to struggle to
manage its growing agenda and operations. The organization's financial
management and reporting policies and project management systems had not
kept pace with its increasingly complex operations. Cash flow and fiscal
management problems began to surface.

Moving into property development had helped the organization grow significantly and to achieve their mission, enabling them to provide the supportive housing their stakeholders needed, but it posed new challenges as well. The income generated by development fees had quickly become incorporated into their business model. WCDO was on the path to becoming development fee dependent without the professional capacity to pursue consistent new real estate projects, or sufficiently manage their own growing portfolio of rental properties. And the dynamic of being fully committed to protecting their clients from repeat homelessness while simultaneously conducting good property management—collecting rent in a timely manner—put a strain on the organization's finances and staff.

In 1996, its 10th year, WCDO's co-directors recommended that the organization take an 18-month break from further new housing development project activity "to get our house in order" and rethink its real estate development business model, its overall organizational structure, its program priorities and its financial condition. WCDO chose to commit itself to a three-year organizational improvement and program assessment facilitated by organizational consultants, and funded by a statewide housing intermediary.

The organizational assessment produced a powerful menu of recommended improvements at WCDO, including changes to board governance, developing more rigorous business planning, adding staff capacity, implementing more diligent property management, and instituting stronger financial management and accounting systems. Once the recommendations were digested by the board and staff, WCDO took immediate steps to address the recommendations, beginning with creating a new strategic plan, developing a new property management business plan, and upgrading its accounting systems and staff. However, as time went on, WCDO did not completely implement several of the improvements, and it did not initiate other improvements recommended.

During this period of increasing management and operating stress within the organization, WCDO experienced an exodus of its founding staff leadership and board members. By its 12th year in 1998, all of the founding directors had left the board of directors. The two founding staff departed within a year of each other. Both were gone by 1999, leaving WCDO with the need to replace all of its original leadership at a time when several key management improvements were recognized as immediately necessary. Over the next two years, WCDO hired and lost two more executive directors. Management instability now compounded other operational and financial problems.

Expanding WCDO's agenda in pursuit of organizational renewal

In the organization's 15th year (2001), WCDO's founding director returned to put together and manage a major new program, called Women In Construction Training Program. This new program addressed one of WCDO's empowerment goals—job training that would directly lead to living-wage employment opportunities for disadvantaged women, the organization's principal constituency. The program became a driver and partner in the organization's business development strategy. Women In Construction-trained female construction crews were successfully employed in all of the organization's real estate development projects through 2005, when the last of WCDO's rental developments came online. WCTP became a wholly-owned subsidiary of WCDO.

By this time, WCDO owned and operated 12 development properties, including 21 units of transitional housing, 20 permanent supportive housing units and 52 permanent affordable units for a total of 93 housing units. WCDO did not realize a net revenue increase from its expanded real estate development efforts due to certain losses on at two projects jointly developed with WCTP, but its impact had expanded to reach more women with more housing, services and invaluable job training.

In 2004, WCDO transferred the Women in Construction Training and construction company subsidiary to a new 501(c)(3) entity created and run by its former director. WCDO received much public recognition for its housing development innovations, training programs and human services via several awards for exemplary achievement between 2003 and 2005. While the new working relationship with the construction training subsidiary and its own former director was complementary and productive, WCDO was not able to reestablish the original strong base of internal development capacity it originally had. For the next two years, WCDO wrestled with property management and maintenance of its rental housing, and undertook no new development.

Grappling with decline, negotiating a collaborative workout

As WCDO approached its 22nd anniversary in 2008, its third executive director in three years resigned. WCDO had been faltering financially and operating in crisis mode on several fronts for two years, and the Board of Directors had begun to take direct control of key administrative responsibilities and exercise more direct oversight. The loss of WCDO's latest executive director provoked a clear leadership crisis and was the tipping point for the organization and the Board's response.

At this point, the WCDO Board took several steps to establish operational stability:

- It secured experienced interim executive leadership;
- It initiated a new level of collaboration and transparency with its primary funders; and
- It invited all community stakeholders to come to the table to jointly identify a mutually agreeable workout plan.

At this point, one clear option in the minds of the WCDO Board was that WCDO might not survive as an organization, but that WCDO's assets and programs could be assumed by another community-based institution and thus continue to serve WCDO's low-income women constituency.

As a result of this constructive posture by WCDO's Board leadership, WCDO played an ongoing, active and constructive role in shaping the final outcome — an outcome that preserved its affordable housing and its services, while conducting an orderly, responsible winding down of its affairs. After 24 years in business, WCDO transferred its assets, along with current service contracts and funding, to Center City Housing Corporation on March 31, 2010, and formally dissolved the WCDO organization in May.

Timeline of WCDO's Phases of Growth and Decline

1985

A Compelling New Vision to Serve & Empower the Underserved

Organization forms (as Women's Transitional Housing) to nurture and serve the housing and related needs of Dulutharea women and young mothers.

Organization actively pursues development of transitional housing and provides extensive women's advocacy, education and training opportunities.

Funders respond eagerly to support the mission and help build the organization. Operations grow significantly in this phase.

1990

Innovative New Programs & Strategies with Profound Impacts

Organization opens Duluth's first transitional housing project (25 units) targeted to assist women in crisis.

Staff leadership and advocacy-oriented staff rise to the challenge of developing innovative transitional & supportive housing projects at a greater scale.

Further housing units planned, developed and begin operations.

1995

High Growth, Management Challenges, Reassessment

Organization continues to expand its development and management activities as operations grow.

Organizational challenges mount, intentional 18-month break from development to reassess development activities and restructure.

Organization engages in intensive 3-year organizational improvement program.

All founding board and staff members have left by 1999. New board members are recruited, and staff leadership is promoted from within.

2000

Renewal: New Strategies, New Name, New Leadership

Organization creates new program to employ and train women in construction, launched by founder of WCDO.

Female crews trained by the organization work in all real estate projects developed during this phase.

A total of 12 projects are now developed with 91 units under management by the organization, including training and programming for residents.

Organization is rebranded from Women's
Transitional Housing
(WTH) to Women's
Community Development
Organization (WCDO).

Organization receives awards for its work.

2005

2010

Decline, Stakeholder Collaboration, Orderly Transfer of Assets

Organization purchases 26unit building with complex reporting and regulations that exceed staff capacity.

Transition to outside property management occurs without sufficient organizational planning.

Frequent executive director turnover; WCDO's board of directors takes control of organization.

Workout Team assists interim WCDO leadership to plan transfer of assets.

RFP issued, seeking compatible organization to take on the portfolio of properties.

Two profitable housing properties are sold to help finance the workout.

WCDO's assets successfully transferred to Center City Housing Corporation (CCHC).



Alicia's Place, located at 315 N. 2nd Ave. W. Provides 11 efficiency units for homeless women.

Organizational challenges and lessons learned

The written proceedings of the 1998 National Building Durable CDCs Conference, sponsored by Local Initiatives Support Corporation (LISC), state that the kinds of crises that ultimately jeopardize an organization's survival "are cumulative affairs in which individual problems, no one of which is fatal, gradually gain mass and momentum until the available forces for remedy are too little, too late."

The experience of WCDO exemplifies this notion of cumulative effect. Following are some of the key challenges in the organization's history. It is impossible to know if one problem contributed more to the organization's gradual decline and ultimate demise than another. It is important to note that none of the problems are unique to WCDO. In fact, all of the lessons learned are important principles for nonprofit boards and management to be alert to throughout the life of any community organization.

CHALLENGE: CHANGES IN LEADERSHIP

Repeated changes in board and staff leadership and diminishing board engagement

The WCDO founders and early executive staff brought key expertise and experience relevant to the organization's mission and operations. These founders played a major role in defining the original values of the organization, developing its operating principles and establishing its initial programs and priorities. They fostered a culture of empowerment and commitment to including representation of women being served by WCDO on the Board.

The two founding employees operated as co-directors, jointly conducting fundraising, project development, advocacy, and designing programs. Having multiple directors made sense in a duo-mission-based organization, focusing on both safe, decent supportive housing and the empowerment of women and children. As a result of their combined insight and innovation they enjoyed the full confidence of the board of directors. The co-director and later the 3-person team management leadership structures worked well while there was both effective, skilled leadership combined with equally strong board oversight.

However, over time, this board confidence evolved into a more passive board which was not provided with adequate board development or knowledge of the business to effectively govern. The board's passive role was compounded by repeated turnover of executive staff. This organizational instability gradually became a cultural norm which over time had a slow but devastating effect on the organization's finances, staff morale, board commitment, and ultimately hurt WCDO's ability to continue to have an impact in the community.

CCHC PERSPECTIVE

"The community support from funders was remarkable toward stabilizing the program and portfolio. Likewise the tenacity of Warren Hanson during financial negotiations supporting CCHC's acquisition and operations was unbelievable." -Rick Klun, Executive Director, Center City

Housing Corp. (CCHC)

After its first creative and highly productive years, a weak Board of Directors began to undermine performance. A once-active and involved board deferred its responsibilities to monitor programs and outcomes to the staff. When the board did take action, it was reactive rather than strategic. When the founding board first began to experience the departure of colleagues, WCDO aggressively recruited replacements that would maintain and enhance board expertise. But by the time the final founding board member departed, the organization was not positioned with a strong replacement board, it had no plan for ensuring a strong board composition, nor was there a succession plan for its executives. Succeeding boards did not re-establish the proactive, strategic role of the founding board, and successive executive co-directors, all promoted from within, were less seasoned than those they replaced, without the experience needed to overcome the extreme management and finance challenges that WCDO would inevitably confront.

In addition to these board issues, the organization began to experience chronic staff turnover. Two founding staff left the organization, departing within a year of each other. They were initially replaced by one of WCDO's long-serving program staff, and eventually by another member of the operations staff. Several years later, three executive directors resigned over four years. WCDO conducted at least one executive search over the years but never hired a director from outside the organization.

When the organization was in its 20th year (late 2006), the last executive director was appointed, this time from the Board. A new Board president took over who was a former volunteer and a real estate professional. At this point the Board of Directors became more assertive and involved – seeking to actively manage the escalating problems and to conduct an orderly disposition of the organization's programs and physical assets if necessary.

Lessons learned:

- Strong, proactive boards and executive leadership are critical components to long-term organizational health.
- Leadership changes are a trigger for organizational instability and an early indicator for impending financial instability and crisis.²



Red flags: Inadequate executive compensation, staff burnout, and a lack of leadership transition planning. ³

 Development and retention of qualified staff is critical for organizational sustainability.



Red flag: Expansion or shift in programming without a shift in staff capacity.

• Departure of founder(s) provides an opportunity for the organization to consider opportunities to merge with another entity.



Red flag: Insufficient attention to leadership transition in face of departure of founder(s).

CHALLENGE: FINANCES

Lack of fiscal management and adequate reporting systems

Before WCDO's first decade was out, cash flow and fiscal management problems had surfaced. WCDO's financial management and reporting policies and systems did not keep up with the organization's increasingly complex operations; revenues and expenses related to its properties were reported as line items on the organization's general operating statement. Consequently, the Board was not receiving a clear picture of the financial position of the organization or a property-by-property view of the portfolio's performance. Supportive services and program delivery received operating support, and while developer fees were earned as the portfolio grew, they did not fully cover actual expenses. A combination of revenue timing issues, inaccurate accounting, slim operating margins, and late-payment penalties weakened WCDO's financial position.

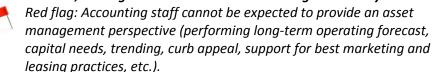
FROM THE FIELD

"Although financial statements are rarely the starting point for problems, poor financial reporting and a lack of internal controls can lead to a downward spiral that can be difficult to correct."

—Nichols, Spencer and Trinh, p.7 One of the common themes in the research on struggling community development corporations is weaknesses in financial reporting and analysis. A study of failed CDCs reveals a lack of clear, helpful internal financial statements and lack of detail on performance by business line or entity, which make it difficult to identify cash-generating and cash-draining activities.⁴

Lessons learned:

- Establish an accurate and transparent financial reporting system to ensure informed decision-making, accountability and internal controls.
 - Red flag: Commingled funds; cash-basis accounting.
- Complex operations require sophisticated financial statements reviewed by a critical board. Board members should be selected for their skillsets, and finance should be one of them, particularly nonprofit finance. All board members should know and be regularly reminded of their fiduciary responsibilities; this can be achieved through board member orientation.
 - Red flag: No source for comparative data on similar properties and tenant populations run by other organizations (including Technical Assistance and other available help).
- Loss of accounting staff puts organizations at risk for financial reporting delays and weak internal controls. Property management staff turnover can prevent an organization from conducting basic, competent property management, which will affect occupancy levels, rental income, safety and security and building conditions—all of which will have profound impacts on residents, the organization and the surrounding community.⁵



CHALLENGE: LACK OF CAPACITY

Expanded real estate development and social service programming without the capacity to absorb these efforts

Responding to the need for permanent affordable housing for women completing their program, and to secure development fee income, WCDO began developing housing without services for women ready to move on from the supportive environment of the transitional housing program. This move doubled the organization's portfolio in less than ten years. These developments provided permanent affordable housing without the supports and advocacy of the Transitional Housing Program. With this expansion, WCDO began to look increasingly like a traditional developer.

Several years later, the organization added a major new program, the Women in Construction Company training program. By 2005, WCDO owned and operated 91 housing units in 12 properties including transitional housing, permanent supportive housing units and permanent affordable units.

WCDO's expansion coincided with the onset of the economic downturn that challenged the entire community development industry, and its chronic problems escalated. Its most recent developments, which included 20 units of permanent supportive housing, further challenged WCDO's already-struggling property management and program delivery systems. Taking on the Endion School property in late 2004 challenged the organization's operations. The reporting and financial requirements of the complex amortizing first mortgage and the extensive federal regulations relating to the Section 8 HAP contract for the site contributed to their fiscal and operational struggles.

Lessons learned:

- Program expansion requires a careful evaluation of the short and longterm financial costs, benefits and risks.
 - Red flag: "Following the money" and its requirements can lead to an organization living hand to mouth.
- Ensure the organization has proper staffing and strategy before growing the business or adding new business lines.⁶
 - Red flag: Is the new program a true innovation to the field? The more an organization is trying to be first in, the more it will require a cushion of resources, in the form of staff, cash and time.
- Stepping outside of the organization's core competencies increases organizational risk.
 - Red flag: What's new can tend to be more interesting to staff. Is infrastructure suffering because the energy is drawn to the newest thing?
- Changing market conditions and increased competition for funding resources can present insurmountable problems for some community development organizations.⁷
 - Red flag: Optimism and idealism can cloud judgment about feasibility.

 Gut instincts should not be relied upon if outside expertise is available.

- Ensure rigorous evaluation of new divisions, operations and programs using financial tools.
 - Red flag: Procrastination is the risk indicator. What has to be delayed in order to serve new programs?
- Be aware of these factors that are sometimes associated with rapid expansion of community development organizations:
 - 1) Taking on non-real estate ventures that are outside the organization's core competencies,
 - 2) Having an unclear financial picture that obscures true program costs,
 - 3) Extreme emphasis on maximizing developer's fees, and
 - 4) Lack of belief that the CDC could fail.8

CHALLENGE: BALANCE MISSION AND BUSINESS

Balancing the pursuit of high mission impact while maintaining good business practices

In many ways, WCDO staff and board members never viewed the organization as a real estate developer. The organization employed a holistic and shared responsibility approach to its work. Development and property management operations were integrated with its administrative and program delivery operations. This inevitably led to tensions between client-focused mission work and sound business practices. This was especially apparent in the organization's struggles with property management. Early on, advocates found themselves tasked with property management responsibilities that compromised their roles and weakened their relationships with residents. WCDO's staff was not equipped by training or experience to manage the increased property management responsibilities; tenant selection, rent collection, vacancies/turnover, and maintenance functions were unevenly staffed.

The addition of 20 units of permanent supportive housing further challenged WCDO's already struggling property management and program delivery systems. Residents with severe chronic mental health and substance issues, and who had experienced long-term homelessness, taxed the capacity of WCDO's advocates. WCDO's consensus-driven management and chronic staff turnover problems left the organization without clear lines of authority and accountability, and some employees felt unsupported and unable to manage crisis situations of residents.

The integrated nature of WCDO's work put staff in a compromising position. They discovered firsthand how difficult it can be to achieve the "double bottom line" of nonprofit housing mission and asset management.

Lessons learned:

- Nonprofit housing requires balancing mission with sound property
 management. If the goal is to be flexible with resident needs and
 emergencies, special funds must be set up and margins must be managed
 to accommodate built-in losses.
- Adding property management requires careful planning, organizational capacity and expertise.



Red flags: Deciding to self-manage for the additional income, without going through an assessment of pros and cons and the checks and balances lost;

Poor curb appeal and lax marketing and leasing efforts lead to unnecessary vacancy loss;

Fear of noncompliance (determining appropriate rent at restricted levels) leads to putting a hold on leasing activity.

- Ensure effective tenant screening practices and clear guidelines for tenant eviction to avoid deterioration of the properties and increased vacancies.
 - Red flag: Verbal rent payment plans with resident with chronic extensions, no written payment plan policy.
- Clearly differentiate between property management and advocacy roles, to conform to established and well-understood practices of both the property management industry and service providers' profession.
 - Red flag: Lack of written resident policies in general can lead to lack of separation of duties which allows some staff to hold the hard line while other staff can provide services and advocate role.
- Recognize that tensions between property management and housing services may be inevitable, even when different organizations or departments within an organization carry out these functions, but they still must be addressed.⁹



Red flag: Who is answering questions for residents? Is there a chain of command and roles and responsibilities that are clearly defined and adhered to?

CHALLENGE: ORGANIZATIONAL CULTURE

Confrontational organizational culture and strained relationships lead to unintentional isolation

The passion and commitment to the mission that served WCDO well early on became a source of isolation and avoidance in later years. WCDO was, at the core, a social justice organization. WCDO was willing to take a confrontational approach to sensitive issues in the community and maintained a commitment to addressing racism and advocating for low-income women and children and people of color.

WCDO's outspoken commitment to systems change, which outsiders viewed as strident behavior, created tension both within and outside the organization. Internal management struggles sometimes spilled beyond WCDO and left the organization at odds with neighbors. Over time, it became difficult for community stakeholders to ask questions. The organization's attempts at

mitigating negative publicity through the media further damaged some community and political relationships.

When the organization reached a crisis point in 2008, a highly qualified nonprofit professional with over 20 years of nonprofit management experience was hired as Interim Executive Director. In addition to addressing immediate operating needs, the new Executive Director immediately began reaching out to stakeholders. The Board engaged the larger Duluth stakeholder community in a frank discussion of WCDO's situation and its prospects. These discussions yielded indications of a strong interest in the preservation of the housing and services, but no support or solution for WCDO. The appeal to the community and opening the lines of communication did, however, open the door to consideration of a collaborative role for the funding community in ensuring the preservation of these critical housing resources.

Lessons learned:

Housing organizations can't operate in isolation; good relationships are essential for organizational sustainability.



🖊 Red flag: Frayed relationships with government agencies or other funders compound problems for already-struggling organizations by reducing or eliminating future funding opportunities and removing leniency or special help related to compliance issues. 10

Collaboration with other organizations needs to come earlier than the workout phase. Joint ventures could have been pursued at the time when new projects and programs were added. High-performing nonprofits forge high-impact partnerships with government, private sector, nonprofit and civic institutions. These partnerships allow nonprofit housing organizations to form complex business relationships and partnerships to more effectively leverage resources. 11



Red flag: Inability to interact with other providers, funders and government without strife can undermine an organization's ability to function.

Keys to successful stakeholder intervention

The WCDO workout process required a willingness for all stakeholders—community representatives, funders, lenders—to be open to whatever might come next for the organization. Though the team initially gathered to see what could be done to salvage the organization and keep it moving forward, they soon came to the realization that it was too late. Though they felt the loss as much as anyone, they were in the difficult position of closing WCDO's doors while preserving the housing and services. Here are the key principles the Workout Team pursued as they considered WCDO's future.

KEY: INFORMATION GATHERING

Understand property management operations and portfolio records.

At WCDO, a number of properties were bundled together as a group. This made it difficult to identify the source of any problems. An important step in this case was to conduct a pro forma on each property to get an accurate picture of how each property was performing. Not all of the properties in the portfolio were in a precarious operating position. Conducting pro formas for each property enabled the team to identify and address operating problems for each property and get the properties in position for transfer. At the end of this process, the properties were unbundled so that each property stood, operationally, on its own.

A second component to the information gathering was to locate all loan documents and grant agreements for each property. A common problem with workouts is the lack of documentation of critical property information. In the case of WCDO, a consultant working on the project called all funders and gathered all documents pertaining to each property. This provided a more complete picture of which organizations had money in each property, loan information, and the terms of existing grant agreements.

KEY: DELIBERATE LEADERSHIP CHANGE

Plan for and anticipate a transfer of control in leadership to a buyer organization during the final stage of workout.

The recognition by a struggling nonprofit housing organization that it is not able to hold on to its properties is a difficult, yet important part of the successful disposal of property. Doing so allows for a transfer of leadership and the ability to leave behind a legacy through a successful transfer and preservation of affordable housing properties. In the WCDO case, the executive leadership team was pragmatic, recognizing that the organization would not be able to hold on to the properties. WCDO took the lead (with Workout Team assistance) on the development of a comprehensive RFP process, focused on identifying a strong organization with a compatible mission and the capacity to take on the portfolio of properties. The process included letters of invitation to several selected organizations and two complete submissions. WCDO's process included a final review by funders of their ranking, before WCDO made its final decision. Center

City Housing Corporation, a local organization with the experience and mission match, was selected as the buyer through this process.

A deliberate transfer of leadership took place once it was determined that Center City would be taking on WCDO's properties. Center City's Executive Director then became the leader and drove the timeline. The Workout Team, which had managed the transition to this point, shifted its role from lead agent to supporter of CCHC's efforts. WCDO's role in the project was minimized at this time. The Workout Team continued to involve many of the funders needed to make decisions about approving property and mortgage transfers and recapitalization.

Throughout this period, interim staff at WCDO were supported with an investment of approximately \$125,000 from GMHF to ensure the organization would continue to function and provide case management until the workout was complete. It was unusual for any funder to support 100 percent of operations during a time of such instability, but as an intermediary, GMHF had the flexibility to do so, and to take a leadership role in the Workout Team process. Minnesota Housing's support at this time was likewise critical toward ensuring that scarce funding resources and WCDO's vital housing stock not disappear.

KEY: CAPITAL NEEDS ASSESSMENT

Understand how properties are operating.

In a workout process, it is essential that the buyer conduct a thorough assessment of capital needs, rental assistance, tenants and their needs, funding resources, operating budget and service funding. In the WCDO case, the Workout Team conducted a quick and less complex assessment to gather information about each property. WCDO and Center City negotiated an agreement that provided the framework for the transfer process, during which Center City could complete the due diligence and the capital needs assessment necessary to determine the viability of the portfolio and negotiate its purchase of the WCDO properties. A skilled property management group was brought in to stabilize the properties and provide added assurance to funders that a workout could be successful.

Center City also submitted a request to Greater Minnesota Housing Fund for approval of a predevelopment loan to support its due diligence activities. Its preliminary research and due diligence convinced Center City that a more thorough effort was essential, would be time and staff intensive and require asset management consulting and legal assistance. The Workout Team and WCDO had made progress in sorting out and analyzing much of the information needed for an evaluation of the portfolio and its viability, but a complete financial picture was not yet in place, and many questions remained to be addressed. With Greater Minnesota Housing Fund's approval of this request, all of the workout partners were able to continue their aggressive efforts to move the transfer process forward.

It was critically important to all members of the Workout Team, and most particularly to funders, that the portfolio be improved prior to transfer and projected to be successful. No one wanted Center City to be saddled with a failing portfolio that could potentially destabilize the organization and its own investments.

In this situation, the buyer took on debt and did not pay cash for the buildings. This is common, though the assumption of existing and new debt is not a given. Sometimes individual properties can be sold to generate cash to pay debt. WCDO pursued the sale of two properties that were not included in the "exclusivity agreement" and used the proceeds to settle a portion of its outstanding debt. They recapitalized the new portfolio with most of the money raised going to property improvements with a 10-15 year life cycle. While the rehabilitation and recapitalization plan was, overall, less than ideal, it was deemed sufficient by the Workout Team, particularly as some of the properties were eligible for more funding in 5-10 years.



Duluth 5-Plex, located at 218-228 N. 14th Ave. E.Provides 5 affordable family rental units.

Navigating the workout process

The lessons learned from the successful transfer of properties described in this report suggest there are a number of key steps to take to ensure success in workout situations.

- 1. Principals must ask for help. One of the factors of a successful workout is whether or not the organization asks for help and seeks resources in time for stakeholders to provide meaningful help. A proactive appeal to the community and open lines of communication pave the way for funders to have a collaborative role to help ensure the preservation of critical housing resources. The workout period is a time to air all of the organization's 'dirty laundry,' something organizations experiencing financial crises can be reluctant to do.
- 2. Convene all stakeholders. Bring together a group of stakeholders with interest in the mission, funding, program, policy, and political roots of the organization. These stakeholders value the preservation of the housing and programs the organization has developed. Convening invested stakeholders helps chart a path toward the workout of a common goal—the preservation of affordable housing and services.
- 3. Keep the process moving forward. Time is of the essence in the workout process. It is a high urgency situation for funders, sellers, buyers, cities and HRAs. All the players will need to commit extraordinary energy and time to get the work done. The project team needs to establish benchmarks and a timeline to keep everyone on task. Most benchmarks need to be completed on or even before their deadline. If complications arise, the team can adjust the deadlines, while still making progress on other decisions and tasks.
- 4. Engaging a buyer/transfer using a clearly defined process. Develop a comprehensive process to recruit, evaluate and select a buyer organization. Accept only complete submissions from experienced organizations. Review and rank the submissions that focus on mission compatibility and demonstrate capacity and experience in areas critical to the organization's portfolio, and seek feedback from funders, to select an appropriate organization to receive the assets.
- **5. Gather all critical files and documents.** Locate all documents and grant agreements for each property pertaining to each property in the workout. This provides a more complete picture of what organizations have money in each property, loan information, and the terms of existing grant agreements.

FUNDER COMMENTS

"Since 1989,
Northland has made
20 grants totaling
over \$335,000 to
WCDO and Center
City Housing – wise
investments to
sustain and improve
critical services in our
region."

—Tom Renier, President,
Northland Foundation

- 6. Secure competent interim management. Maintain funding at a level that will keep current or interim leadership in place and the organization operating. Keeping the organization running with competent interim management is an essential part of negotiating the workout process. It stabilizes the organization's operations and services, keeps service contracts in place and avoids disruption to residents as the transition planning progresses.
- 7. Eliminate operating losses aggressively. Look carefully at operating costs and identify places to reduce operating expenses. Consider keeping only a skeleton staff in place during the workout period, such as a case manager, part-time Executive Director and bookkeeper. The board of directors may need to conduct extensive work as volunteers. Consider disposing of property to pay off property management debts.
- 8. No judgment, no blame. Workouts are high-stress situations and it is common to hear blame and judgments among the multiple stakeholders involved. This is counterproductive to the process. To create an environment that supports transparency, the seller organization must not feel judged by the organizations helping with the workout process. Conversely, the seller organization must not blame funders, staff members or other stakeholders. Avoid this pitfall by remaining grounded and focused on the larger goal of the workout process—to preserve housing for the families the organization serves.
- 9. Need for interim capital to bring in expertise, consultants. The buyer needs to have a complete understanding of the portfolio and the risk of taking on the additional properties. The buyer may seek predevelopment loans to bring in additional expertise to conduct a capital needs assessment. This step allows the buyer to feel more comfortable with the acquisition and ensure they are not inheriting a project that would put their other housing units at risk.
- 10. Be aware of existing funding requirements and compliance issues during transfer of properties. Gathering all loan documents and grant agreements for each property will provide a more complete picture of which organizations have money in each property and the terms of existing grant agreements. Having this information on hand will ensure that properties continue to meet funding requirements and will make the transfer and disposal process smoother.



Duluth TriPlex, located at 18 West 5th Street.Provides 3 family units of affordable housing.

Recognizing signs of trouble ahead

The challenges WCDO faced are not unique, nor are they particularly unusual. They included:

- 1) Staff/board instability
- 2) Financial troubles
- 3) Lack of capacity
- 4) Morale issues

These categories are discussed below in greater detail. These topic areas encompass the myriad issues that all nonprofits may face at one time or another in the course of their growth as an organization. No one indicator can clearly be identified as the straw that will break the camel's back or the clear sign that the organization is at risk of failing. However, the compounding effect of contending with many of these issues simultaneously can result in an irreversible downward spiral for a nonprofit.

Board members and executive leaders need to be aware of the warning signs that their nonprofit could be in trouble. Similarly, funders want to stay attuned to the prevalence of these concerns.

Many nonprofit organizations will surely recognize some of the challenges as they scan the list on the following page. Taken one at a time, these issues can be managed and overcome, and need not be insurmountable.

One of the proven key indicators of the need for heightened attention by both internal and external stakeholders is a change in the Executive Director, particularly the founder. While this may also provide opportunities for strategic realignment, stable leadership is most frequently an essential component to a successful organization. The departure of two or three executive directors in just a handful of years is a common indication of serious instability and is cited as a cause for concern more than any other factor.

The issues listed on the following page were not all necessarily experienced by WCDO. This list draws from their situation as well as from the literature on signs of a troubled nonprofit.

FROM THE FIELD

Morale may be reduced if staff must choose between an adherence to the mission and tough management decisions. One solution to this is serving fewer clients to keep the organization's finances sound.

- 1) Staff and board instability can take many forms. It may be the result of leadership changes, or a high turnover rate of staff or executive leadership. 12 Turnover may arise due to a combination of low pay and high stress. A challenging organizational culture, crisis management style, or a conflict-ridden environment may exacerbate tensions between key staff and board members, and can result in communication problems. If staff are not providing sufficient supporting materials or guidance, board members may become disengaged and inattentive, undermining the decision-making process. Board members may lose confidence in the organization, or burn out due to a high demand for their involvement in operational decisions. Understanding the reasons for staff and board turnover may reveal the need for mentoring, fundraising assistance, financial management training, or restructuring.
- 2) Financial instability may result from increased spending relating to expansion, loss of funds raised, mounting debt or payables, or dwindling reserves.¹³ The organization may not be expert at managing its finances, indicated by inadequate financial statements, and/or a lack of accounting staff capacity. There may be cash flow issues or anticipated grant or earned revenues may have gone unrealized. Expenses may be too high, suggesting the need for a leaner, less ambitious agenda. There should be an active board finance committee providing ongoing oversight of the finances of the organization.
- 3) Staff and board capacity issues can similarly plague an organization. These may stem from an expansion of operations without adequate staff. Inexperienced staff may have been hired and not provided the necessary training to fulfill critical functions. Conversely, excess facilities or staff should always be considered, as funding resources may have been eliminated and no longer be adequate. Boards need to ensure they hire a new executive director who is a leader, not just a manager. Attracting and retaining board members and ensuring that good governance is practiced is another area to examine in terms of board member qualifications, active committees, and regular board meetings with high quality reporting and board decision making.¹⁴
- 4) Morale issues may compound the problems noted above. Morale may be reduced if staff feel they must choose between an adherence to the values expressed in the mission and tough management decisions. One solution to this is serving fewer clients to keep the organization's finances sound. A crisis mentality may become the norm. Or there may simply be an avoidance of the issues at hand. Over time there may be a loss of confidence in the organization as it struggles to manage its day-to-day affairs. The organization may become insulated and withdrawn from the public, which may diminish its visibility and community support. Occasionally, unfavorable media can damage an organization's ability to attract and retain human and funding resources.¹⁵



Duluth TriPlex, located at 1431 East 2nd Street.Provides three units for homeless families.

Pursuing the cornerstones of strength and stability

Looking at nonprofits from the flip side, there are recommendations from the industry as to the qualities organizations should embrace in order to avoid a path toward decline. These recommendations come from authors who have studied nonprofits through their life cycles, and including stages of downsizing, merging, or closing.

It is vital to have and hew to a **current strategic plan** that tracks and anticipates sustainable growth for the organization.¹⁶ It is important that strategic plans be revisited to ensure they reflect and respond to changes in the needs of the community or the larger market. A turn in either direction requires a nonprofit's response. A large supply of housing can lead to high vacancy rates; meanwhile a robust housing market can price properties beyond the reach low-income households, creating a sudden demand for affordable housing.

Organizations must **strengthen their financial reporting and analysis**.¹⁷ This begins with strong staff capacity to effectively plan for the organization's future, raise adequate capital and manage its resources effectively. It is followed up with the board of directors' critical eye analyzing the financial statements and asking the hard questions.

Diversifying revenue streams is critical advice for all nonprofits.¹⁸ Over-reliance on a single funder or small set of funders leaves the organization vulnerable to shifting priorities of the funders. Similarly, significant one-time cash receipts,¹⁹ though welcome when they arrive, can mask underlying problems noted above under financial instability. Having sufficient operating support is important for healthy organizations. Early identification and removal of resource-draining projects will keep the organization in balance.²⁰

Another key to sustainable nonprofit practice is to **maintain open communication lines**, in good times and bad.²¹ Communicating within the organization, between the staff and the board, with clients of the housing units, with funders, with stakeholders who care about the mission and direction of the organization—maintaining all of these channels ensures transparency, openness, and trust. It enables the leadership to respond to programs quickly, should they develop, and keeps problems from becoming larger than they need to be. Consistent communication leads to better relationships with partners, peers, and funders—and contributes to the overall stability of the organization.

FROM THE FIELD

"Decline and dissolution are not considered an inevitable stage of an organization's life cycle but rather one of the routes an organization can find itself taking... An organization can face dissolution at any stage."

-Judy Sharken Simon, Fieldstone Alliance

Embracing the growth stages of a nonprofit

The course of WCDO is not unlike the path that other nonprofits have followed. A survey of the literature on the life cycle of nonprofits sheds some light on the common stages nonprofits pass through, from the kernel of an idea onward.

Various authors use different terms to describe the nonprofit life cycle, but there are strong commonalities across the ones surveyed for this report. They fall into five basic phases of growth, with a sixth phase relating to decline or dissolution that at least one author asserts should be treated through a separate lens. "Decline and dissolution are *not* considered an inevitable stage of an organization's life cycle but rather one of the routes an organization can find itself taking... An organization can face dissolution at any stage."²²

- 1) **The Idea Phase.** This is the time to "imagine and inspire," when the organization is establishing a vision, is still "formless" and exists only as an idea that is gaining momentum. Duration: 0-5 years. 25
- 2) The Startup Phase. The organization is now officially established, with nonprofit incorporation, and the beginnings of programming, management, staffing and/or volunteer base, funding, operations and a viable board of directors.²⁶ The organization is building capacity and solving operational problems.²⁷ Duration: 1-2 years.²⁸
- 3) **The Growth Phase.** The organization is establishing systems of accountability, with the need to grow on multiple fronts; staff and board are taking care of business while entertaining choices and challenges that come their way.²⁹ The driving question at this phase is "How can we build this to be viable?"³⁰ Challenges faced at this time may include competing visions, and situations where demand exceeds capacity.³¹ Duration: 2-5 years.³²
- 4) **The Maturity Phase.** This phase is a time of balancing growth with stability.³³ The goal during this phase is to continue to produce while sustaining the organization's momentum.³⁴ At least one author would include an additional phase just before maturing called "Peaking," during which time the organization experiences great success in all aspects of its operations, internal and external.³⁵ The board's role during this time is to assure the resiliency of the organization and to build the bench for future leadership transitions.³⁶ Duration: 7-30 years.³⁷
- 5) **The Renewal Phase.** The phase of renewal, in which the mission and business model are thoroughly reconsidered and sometimes dramatically altered, is spurred on by stagnation³⁸ and the need for reinvention.³⁹ The organization may feel compelled to renew itself due to changing market forces, industry shifts, or changes in cultural values and require a response from the nonprofit to keep it current and relevant. Depending on how dramatic the changes are that the nonprofit makes to its mission, programming, or structure, the organization may cycle back to an earlier stage.⁴⁰ Duration: 2-5 years.⁴¹

It is important to acknowledge that for some nonprofits, there will be a phase of decline and possible dissolution. That stage, not experienced by all nonprofits, is described here:

6) **The Decline Phase.** If stagnation has occurred and is not accompanied by a successful renewal effort, decline and shut-down may take place. ⁴² The key question at this time is: "Should we close?" ⁴³ The following factors are commonly occurring in organizations just prior to their closure: (a) loss of all or significant support; (b) "chasing dollars syndrome"; (c) sudden and dramatic expansion of services; (d) falling behind on financial obligations; (e) inability to meet service and financial projections; (f) departure of key board and staff. ⁴⁴ Duration: 1-2 years. ⁴⁵

Signs of trouble in housing nonprofits



Departure of founder or executive director
Rapid turnover of Board of Directors and/or staff
Tensions between staff and board
Dwindling resources
Inadequate financial statements
Rapid program expansion
Inexperienced staff
Blending of advocacy and property management roles
Negative press

Toolbox for funders to address decline



Provide conditional funding – support with intervention
Conduct heightened loan monitoring
Assist with strategic plan consulting
Maintain open lines of communication with grantees
Explore merger/transfer of assets options
Support interim management during workout process
Participate as member of workout team

Endnotes

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