The National Council of Nonprofits, the largest network of nonprofits in the country, submits the following comments regarding the Federal Reserve’s proposed Nonprofit Organization Loan programs – the Nonprofit Organization New Loan Facility (NONLF) and the Nonprofit Organization Extended Loan Facility (NOELF). Our network of more than 25,000 organizations – charitable nonprofits, faith-based groups, and foundations – is committed to promoting positive policy solutions that will enable organizations to advance their missions in their communities and, in particular, to promote COVID-19 relief and recovery. It is with this public policy perspective that we offer these comments.

The proposals on which we comment must be understood within the greater context. Unemployment news across the country is horrific. Forty-million Americans have lost their jobs due to the coronavirus pandemic, with another 1.5 million new claims in the week ending June 13. The nonprofit community is not immune from this crisis; data from Johns Hopkins University estimate that 1.6 million nonprofit jobs have been lost in the last three months. This translates to 13 percent of jobs in the nation’s third largest industry. Without appropriate federal assistance, many organizations on which Americans rely are not likely to survive, creating further pain for the public and strains on the economy due to unmet needs.

We applaud the Federal Reserve for recognizing the importance of the work of the nonprofit sector as demonstrated in the Chairman’s statement, "Nonprofit organizations are critical parts of our economy, employing millions of people, providing essential services to communities, and supporting innovation and the development of a highly skilled workforce... and we are working to help them through this difficult time." Moreover, we welcome the addition of Nonprofit Organization Loan programs to the options available to promote nonprofit sustainability. We anticipate few charitable organizations will seek these loans, however, because there currently is no provision that makes the loans forgivable. Even for those willing to consider applying for a Nonprofit Organization Loan, there are other impediments that we address in these comments.

1. Loan Forgiveness is Critical to Nonprofit Sustainability

A fundamental feature of nonprofit economics has long been that nonprofit boards are averse to taking on loans to cover operating expenses. Unlike for-profit businesses, charitable organizations typically rely on support from the community to fund their operations. For the foreseeable future, charitable organizations are likely to see exponential growth in demand for their services while resources – whether charitable, foundation, or corporate donations, or government grants and contracts – are not expected to recover, much less rise to meet the growing challenges. For these reasons, the best, and perhaps only, workable solution for charitable organizations of all sizes is to secure grants or forgivable loans to fund operations during and emerging from the pandemic.

We understand that staff of the Federal Reserve is of the opinion that providing loan forgiveness is not an authority the independent agency possesses. We ask that this narrow view of legal authority...
be re-examined and, if confirmed, that the Federal Reserve publish the analysis for the public and Congress to review. If it turns out that legislative clarification is needed, we ask Congress to ensure that charitable nonprofits of all sizes have access to loan forgiveness, not just those eligible for Paycheck Protection Program loans via the CARES Act.

**Recommendation:** The Federal Reserve, either on its own or working with Congress, must recognize the extent to which the public and economy rely on the vital services nonprofits provide to communities and the economy by creating a forgivable loan program.

**2. Limitation of 50-Employee Minimum Should Be Removed**

The term sheet for the proposed nonprofit loan facility imposes a size minimum that is not imposed in the Main Street New, Priority, or Expanded Loan Facilities for for-profit businesses. There is no explanation why the Federal Reserve is proposing that nonprofits with fewer than 50 employees should not be eligible for Main Street loans for which their small business counterparts of equal size could secure lending support.

Many of the nonprofits in our network are on the frontlines of this pandemic, working with fewer than 50 employees to address immediate and growing needs. Indeed, 97 percent of nonprofits have budgets of less than $5 million annually, 92 percent operate with less than $1 million a year, and 88 percent spend less than $500,000 annually for their work. The “typical” nonprofit is community-based, serving local needs. Arbitrarily excluding these vital organizations from important loan programs would not only cut out the vast majority of nonprofits, but also harm the people who would no longer be served by those nonprofits.

**Recommendation:** The Nonprofit Organization Loan programs must be revised to remove the 50-employee floor.

**3. The Proposal to Limit Loans to Mid-Size Nonprofits with Less than 30 Percent of Revenue from Donations Disqualifies Many in the Charitable Sector**

The National Council of Nonprofits strenuously objects to the proposed loan qualification criteria that organizations must have revenues from donations that are less than 30 percent of 2019 revenues. Perhaps the Federal Reserve is unaware that its proposed disqualifier flips other federal law on its head: to retain tax-exempt status under Section 501(c)(3) of the Internal Revenue Code, charitable nonprofits must meet a “public support” test showing they receive at least a third of their revenues via contributions from the general public, contributions or grants from other public charities, or from governmental agencies. If a charitable nonprofit fails to do so, then it carries the added burden of providing additional facts and circumstances to prove that it is a publicly supported organization. One hand of the federal government – Congress, Treasury, and the IRS – currently tells nonprofits we need to have contributions of more than 33.3 percent, while the Federal Reserve proposes to limit loans to those that receive less than 30 percent of their revenues from donations.

As currently written, the draft term sheets for the two nonprofit loan programs favor large institutions with established “business” operations that generate fee-for-service revenues. That may work for nonprofit hospitals, colleges, and universities, but it will not work for most charitable organizations that are serving the greatest needs in their local communities during and after the pandemic.

Right now, communities are relying on frontline nonprofits of all sizes to address immediate needs. The local shelter, food bank, Meals on Wheels, community outreach, and faith and cultural institutions normally rely on a mix of donations, pay-what-you-can payments, grants, and contracts to fund operations. Every organization in every community is unique; its mix of revenues is determined
by the value that the community places on the services, values, and impact that each nonprofit provides. Any reliance on an arbitrary threshold for charitable donations would exclude a large share of well-run nonprofits that will survive the pandemic with sufficient federal support.

Just one example is needed to demonstrate the disconnect between the proposed cap on eligibility and the economic and legal realities that charitable nonprofit face. The informational tax return that most charitable nonprofits fill out each year – the Form 990 – requires nonprofits to list different forms of revenue. The IRS treats certain work performed by nonprofits under written agreements with governments as donations. Specifically, Form 990, Part VIII Statement of Revenue provides the line item “h. Government grants (contracts)” as the place where some organizations – notably human service providers – disclose as much as 90 percent of their revenues as contributions, even though they are earned via written agreements with governments to provide specific services to the public. See generally IRS Instructions for Schedule A (Form 990 or 990-EZ) – Public Charity Status and Public Support.1 Surely, the Federal Reserve does not intend to discriminate against the subsector of the charitable nonprofit community dedicated to helping people cope with the COVID-19 pandemic.

From the foregoing, it should be clear that the Federal Reserve has chosen a false proxy for nonprofit stability or an indicator of the ability of organizations to repay loans.

**Recommendation:** Eliminate the requirement that no more than 30 percent of an organization’s 2019 revenues come from donations.

### 4. The Proposed Loan Terms Should Be Made More Favorable for Charitable Organizations

The draft Nonprofit Loan Facility term sheets impose certain liquidity, asset, and reserve requirements that are not required in Main Street New Loan Facilities available to for-profit businesses. While recognizing the differences between nonprofit and for-profit economics, the Federal Reserve proposals impose unfair and unsustainable terms on charitable entities.

Nonprofit organizations typically provide services with low profit margins. Indeed, social service organizations report an average aggregate margin of 1.5 percent. According to a recent report by Seachange Capital Partners, the median social services nonprofit has a margin of 1.0 percent, receives 3.6 percent of its revenue from philanthropy (including investment income), has total financial assets (including endowments and other assets that are subject to legal restrictions) equal to 1.9 months of expenses, and operating reserves of less than one month of expenses. Less than 20 percent of large nonprofits have 6 months or more of operating reserves, a widely accepted standard for “financial strength” for nonprofits. Social services organizations are the most fragile, with fewer than 10 percent reaching this standard.

The statistics above should not be viewed as an indictment of the efficiencies or management policies of nonprofits. Governments routinely hire nonprofits to deliver services to the public. Indeed, as seen previously, nonprofits delivering social services often earn the vast majority of their revenues pursuant to written agreements with governments (sometimes labeled as grants, other times as

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1 The IRS Instructions warn (at page 9, column 1) about the complexities of making these determinations: “Contributions are sometimes difficult to distinguish from such gross receipts — the label on the agreement [between the government entity and the nonprofit] isn't controlling. ... See Regulations section 1.509(a)-3(g). Refer to the instructions for Form 990, Part VIII, lines 1e and 2, for more examples addressing the distinction between government payments that are contributions and government payments that are gross receipts from activities related to the organization's tax-exempt purpose or function.” (Emphasis added.)
contracts). Yet, governments seldom pay the full costs of providing those services, a fact documented by numerous studies, including several commissioned or conducted by the National Council of Nonprofits. This systematic underpayment to nonprofits forces them to spend money and time to raise donations from the public – something for which the Federal Reserves’ proposed loan terms would essentially penalize nonprofits providing human services during the pandemic and subsequent recovery. Compounding the harm, nonprofits doing government grant/contract work often experience cash-flow challenges because governments usually reimburse nonprofits only after the work has been completed and then often with significant delays in payment.

**Recommendation:** Recognizing the unique nature of nonprofit operations and their importance in continuing to provide vital services as partners on the front lines of the COVID-19 crisis, we urge the Federal Reserve to eliminate borrower requirements 7 (liquidity) and 8 (debt ratio). If this is not possible, then we ask that the requirements be lessened significantly to reflect the economic realities of nonprofit operations, for example by requiring only 30 days cash on hand, and reducing the loan origination ratio from 65 percent to 40 percent.

**Recommendation:** We are also concerned that certain eligible loan features are too onerous for nonprofit organizations and are less favorable than those offered in other government programs. Specifically, the interest rate of LIBOR plus 300 basis points is significantly higher than that offered for Paycheck Protection Program (“PPP”) Loans (1.0%) and that for Economic Injury Disaster Loans (2.75%). In addition, the imposition of loan origination and service fees adds unacceptable costs under the Nonprofit Organization Loan Facility. Finally, the notion that nonprofits would face a 70 percent balloon payment at the end of the fifth year of the loan would scare away many nonprofit board members. Nonprofits with existing loans with balloon payments are usually provided an opportunity to renegotiate such loans at prevailing market rates.

We urge that the loan terms including interest rate and balloon payments be revisited and recommend the lowest permissible rate, such as the 0.5 percent rate initially proposed for PPP loans. In addition, we urge some flexibility in the balloon payment requirement to afford the opportunity for renegotiation. If the 5-year amortization were extended to 7 years, this could lessen the balloon payment. We request that the borrower have access to engage with derivatives (change to a fixed rate) without the minimum swap requirements.

5. The Ratio of Adjusted 2019 Earnings before “EBIDA” Should Be Revised

In the “Draft for Public Consultation,” for both the Nonprofit Organization New Loan Facility and the Nonprofit Organization Expanded Loan Facility, one of the eligibility criteria for borrowers is that they must have “a ratio of adjusted 2019 earnings before interest, depreciation, and amortization (“EBIDA”) to unrestricted 2019 operating revenue, greater than or equal to 5%.” (#6) In the context of nonprofit operations, this threshold is too high and would make many, if not most, nonprofits ineligible based on these criteria alone, which seems written more in the context of for-profit businesses as opposed to nonprofit organizations.

It may certainly be prudent and necessary to have a positive ratio of adjusted earnings; however, nonprofits generally operate on small margins out of necessity and to fulfill their missions rather than sit on excess surpluses. Moreover, at times, a nonprofit may have a planned and manageable deficit as part of a strategic plan—a negative ratio at one isolated point is not always an indication of instability.

Furthermore, the footnotes for criteria #6 clarify that “The Eligible Lender should calculate operating revenue as unrestricted operating revenue, excluding funds committed to be spent on capital....”
Many nonprofits have “restricted revenue” through grants and contracts built into their operating budgets. Excluding this revenue would compound the problem of meeting the 5 percent ratio. Although it would be sensible to exclude contributions raised for a “capital campaign,” excluding other capital funds included in an annual budget for maintenance and planned upgrades would further decrease the required ratio.

**Recommendation:** The 5 percent requirement should be reduced to zero, if not eliminated. In addition, a statement of explanation of a deficit should be allowed so that a negative ratio does not mean automatic ineligibility for a nonprofit borrower. Finally, further clarification on the calculation methodology — in the context of nonprofit operating budgets — is needed in regard to both restricted funding from grants in annual operating budgets, as well as capital funds for improvements that are part of an annual operating budget. This clarification would allow noted revenues to remain in calculation to ease the restriction and not further restrict eligibility.

6. **“Reasonable Efforts” Regarding Employee Retention Require Further Clarification**

Most charitable nonprofits can only advance their missions through the committed service of individuals dedicated to improving the lives of people in their communities. It is in everyone’s interest – our communities, our employees, and the missions of nonprofits – that the nonprofit workforce returns to pre-pandemic levels and that organizations and their employees continue to contribute to the wellbeing of individuals, communities, and the U.S. economy.

As explained more fully in a June 18 National Council of Nonprofits article, the description of “Retaining Employees” in the draft for public comment requires refinement if the Federal Reserve expects nonprofits to take advantage of this facility. Specifically, before seeking loans, nonprofits need to know what is meant by “reasonable efforts,” “maintain its payroll,” and “retain its employees,” as well as better understanding of the scope of the “time the eligible loan is outstanding.” We ask that the final regulatory and contractual materials include these clarifications:

**Recommendations:**

- **“Reasonable efforts”** should be interpreted in the totality of the circumstances, taking into consideration not only the general economic environment in the community or communities in which the borrower operates, but also factors such as workforce, fundraising ability, revenue-generating activities, and overall demand for the services and programs the organization provides. One option would be to add the qualifier “mission-based” before “reasonable efforts.”

- We presume the terms “maintain its payroll” and “retain its employees” are included in the description to parallel the loan forgiveness provisions of the Paycheck Protection Program, but without the rigid application of the mandates in the CARES Act. We ask the Federal Reserve to make clear that nonprofits participating in the Main Street loan program generally should endeavor to pay staff at the same or increased income levels and should act in good faith to keep staffing levels (measured on the basis of full-time equivalents) at the same or increased levels, both for the duration of the loan. It is also important that the loan documents expressly state that the employee retention provision begins on the date that loan funding is received by the borrower rather than at an earlier date.

- The need for **Safe Harbors:** Congress and the Administration have seen as the pandemic unfolded that initial presumptions about its depth and duration were flawed. In both legislation and administrative guidance, policymakers have established clear rules acknowledging that economic and health conditions in parts of the country may make it very
difficult or impossible for employers to rehire staff and that these conditions can improve and worsen over time. Therefore, we ask that the Federal Reserve clearly state that nonprofit borrowers will not be penalized under the employee retention provision for the decision of employees to decline offers of rehire, or for those who are fired for cause, voluntarily resign, or voluntarily request a reduced schedule during the time that the loan is outstanding.

7. Additional Recommendations and Requests for Clarification

Finally, the National Council of Nonprofits respectfully requests that the Federal Reserve clarify the following issues before finalizing the Nonprofit Organization Loan programs:

- **Endowment**: What resources should be included in endowment calculations? Does it include restricted endowments? Does it extend to include cash on hand?
- **Collateral**: Flexibility on collateral is requested. The loan should be available with no more than 50 percent Loan to Value (LTV) if collateral is needed.
- **Other Debts**: The proposal requires that borrowers “refrain from repaying the principal balance of, or paying any interest on, any debt until the Eligible Loan is repaid in full, unless the debt or interest payment is mandatory and due.” We request that this exclude lines of credit and other debt that are assumed to provide financial liquidity related to the impact of COVID-19.

The National Council of Nonprofits appreciates this opportunity to provide public comments. Our networks of charitable organizations stand ready to answer questions, offer additional insights, and provide follow-up research to assist the Federal Reserve to develop Nonprofit Organization Loan programs that address the immediate needs of charitable nonprofits on the frontlines of providing relief and recovery during this national crisis.

Respectfully submitted,

[Signature]

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