

**Underwriting the Non-Profit Organization**  
**National Community Development Lending School**  
**March 25-28, 2012**  
**Seattle, WA**

**INTRODUCTION**

Non-profit organizations are critical to community development success, whether in affordable housing, economic development, community service or neighborhood revitalization. This course walks you through the basics of community development lending, the important role played by non-profit organizations and what makes them different from a financial perspective. The course covers issues such as governance, management, programmatic considerations and the fundamentals of financial analysis including ratio analysis and appraisal gap. Learn to interpret financial statements to support your internal presentation and have a better conversation with your non-profit customer. Through the use of a real case study, you will have a greater understanding of how to assess management, operations and financial condition, while learning what questions to ask. Get behind the numbers and learn to be an effective advocate for the non-profit organization.

**OBJECTIVES**

As a result of this course, you will:

- Enhance your understanding of non-profit organizations
- Distinguish non-profit versus for-profit financial statements
- Understand qualitative and quantitative factors to be considered
- Understand the structure and source of repayment for common types of loans
- Understand why subsidies are needed

**INSTRUCTOR**

Cathy Niederberger  
Managing Director, Community Development Banking  
PNC Bank  
249 Fifth Avenue  
Pittsburgh, PA 15222  
Phone: (412) 762-8333  
E-mail: [cathy.niederberger@pnc.com](mailto:cathy.niederberger@pnc.com)

---

**2012 National Community Lending School**  
 Underwriting the Non-Profit Organization  
 New Orleans, LA

---

**AGENDA – MARCH 26 or 27, 2012 (Monday Afternoon or Tuesday Morning)**

<b>TIME</b>	<b>TIME</b>	<b>MINUTES</b>	<b>TOPIC</b>
1:30	1:40	10	<ul style="list-style-type: none"> <li>• Introductions</li> <li>• Background of class participants</li> <li>• Ground rules</li> </ul>
1:40	1:45	5	<ul style="list-style-type: none"> <li>• Course outline and objectives</li> </ul>
1:45	1:55	10	<ul style="list-style-type: none"> <li>• Role of Community Development Lender</li> </ul>
1:55	2:05	10	<ul style="list-style-type: none"> <li>• CD Non-Profits and 501©(3) status</li> </ul>
2:05	2:10	5	<ul style="list-style-type: none"> <li>• Types of Loan Requests</li> </ul>
2:10	2:20	10	<ul style="list-style-type: none"> <li>• Qualitative Analysis</li> </ul>
2:20	2:30	10	<ul style="list-style-type: none"> <li>• About the Financial Statements</li> </ul>
2:30	3:00	30	<ul style="list-style-type: none"> <li>• Quantitative Analysis</li> </ul>
3:00	3:15	15	<ul style="list-style-type: none"> <li>• Break</li> </ul>
3:15	3:25	10	<ul style="list-style-type: none"> <li>• Pt. 1: Case Study Prescreen Reading</li> </ul>
3:25	3:55	30	<ul style="list-style-type: none"> <li>• Pt. 2: Read (10), Calculate (10) and Class Review (10) Financial Highlights</li> </ul>
3:55	4:25	30	<ul style="list-style-type: none"> <li>• Small Group Analysis of Request</li> </ul>
4:25	4:45	20	<ul style="list-style-type: none"> <li>• Loan Presentations/Recommendations</li> </ul>
4:45	5:00	15	<ul style="list-style-type: none"> <li>• Summary and Closing/Questions</li> </ul>

## **GLOSSARY OF TERMS AND DEFINITIONS**

**Non-Profit Organization:** Defined by nature of its tax exempt status and legal entity status; does not mean the organization does not make a profit.

**Loan-to-value ratio:** A percentage calculated by dividing the amount borrowed by the price or appraised value of the asset to be purchased; the higher the LTV, the less cash a borrower is required to pay as down payment.

**Loan-to-cost ratio:** A percentage calculated by dividing the amount borrowed by the total cost to develop the project.

**Appraised value:** An estimate of a property's fair market value.

**Hard costs:** Included in hard costs are all of the costs for the visible improvements, line items like grading, excavation, concrete, framing, electrical, carpentry, roofing, and landscaping. Another way to describe hard costs is the "brick and mortar" expenses.

**Soft costs:** Soft costs include the architect's fees, the engineering reports and fees, the appraisal fee, the toxic report fee, any government fees - including the plan check fee, the cost of the building permit, any assessments, and any sewer and water hook-up fees - plus the financial costs, such as construction period interest and loan fees.

**Section 8 Subsidy:** HUD makes up the difference between what a low- or very low-income household can afford and the fair market rent for an adequate housing unit. Eligible tenants must pay 30 percent of adjusted income. Section 8 housing must meet certain standards of safety and sanitation, and rents for these units must fall within the range of fair market rents as determined by HUD. This rental assistance may be used in existing housing, new construction, and moderately or substantially rehabilitated units.

**HUD Community Development Block Grant Program (CDBG):** The uniquely flexible CDBGs provide a variety of loan and grant programs in different cities. Under this program, funds are allocated to local governments to finance a wide range of housing, community development and economic development activities. Priority projects and funding allocations are determined by the local unit of government.

**HUD Home Investment Partnerships Program (HOME):** The HOME program provides funds directly to states and local governments (known as participation jurisdictions (PJs) to address a broad range of affordable housing needs. It encourages public-private partnerships by providing incentives to for-profit and non-profit developers to produce housing for low-income households. HOME provides funding and general guidelines to the PJs and empowers them to design and tailor affordable housing strategies to address local needs and housing conditions.

**United States Dept. of Agriculture Rural Development Community Facility Guaranteed Loan:** This program guarantees loans made to finance essential community facilities such as day care centers, hospitals, schools, clinics, roads and fire halls. Applicants can be public bodies, Indian tribes, cooperatives, or other non-profit organizations.

**Community Development Financial Institutions:** Mission-driven financial institutions that provide financial products and services to people and communities underserved by traditional

financial institutions. CDFIs include a broad range of institution types such as community development banks, community development credit unions, community development loan funds, community development venture capital funds and micro enterprise loan funds.

**Community Development Financial Institutions (CDFI) Fund:** The CDFI Fund provides investments and awards to community development financial institutions (CDFIs) and banks through the CDFI program and the Bank Enterprise Awards (BEA) program. Located within the Treasury Department, the Fund made its first awards in 1996.

**Federal Empowerment Zones/Enterprise Communities:** The Empowerment Zones/Enterprise Communities Initiative (EZ/EC) provides tax incentives, performance grants, and loans to designated distressed areas to stimulate economic activity and to create jobs.

**Federal Home Loan Bank System:** The twelve district Federal Home Loan Banks (FHLB) administer two affordable housing programs for financial institutions that are members of the FHLB System. The programs are designed to encourage member banks to participate in affordable housing efforts in their communities.

**Affordable Housing Program (AHP):** This Federal Home Loan Bank program provides direct grants for affordable housing that are used in conjunction with other sources of funds, such as the Community Investment Program (see below), low income housing tax credits and other federal, state and local programs. Funds are used to finance the purchase, construction and rehabilitation of rental or owner-occupied housing for very low- and moderate-income individuals.

**Community Investment (Advance) Program (CIP):** The Federal Home Loan Bank provides advances at the member bank's cost of funds to serve as an incentive to members to provide loans for community development activities in the following categories:


- Affordable home ownership opportunities for first-time home buyers and low and moderate-income persons or families
- Economic development opportunities through residential and community revitalization programs
- Affordable rental opportunities and
- Construction loans

**Program Related Investment:** PRIs by charitable foundations are an alternative to traditional grant making. Instead of a cash transfer without repayment (grant), PRIs convert the grant into an alternative investment instrument such as a loan guarantee, interest subsidy or equity investment. A key attribute of the PRI is its flexibility, which means it can be structured to effectively address different types of financing gaps.

# Underwriting the Non-Profit Organization

2012 National Community Development Lending School  
Cathy Niederberger  
PNC Bank

---




---

---

---

---

---

---

---


---

## Traditional versus Community Development Lender

**Introduction - Role of the Community Development Banker**

- **Traditional Lender**
  - Business credit policies
  - Measurable goals
  - Relatively easier- to- book deals
- **Community Development Lender**
  - CD lending credit policies
  - Measurable goals
  - Involved early
  - Identifies potential partners
  - Layers of financing, Longer cycle
  - Manages internal expectations

2




---

---

---

---

---

---

---

---

## What are “typical” Community Development Non-Profits?

- Community Development Corporations
- Social Services
- Arts and Culture
- Child or Elder Care
- Education
- Health Care
- Community Development Financial Institutions
- Religious Organizations

3




---

---

---

---

---

---

---

---

## What is a "501 (c)(3)"?

### Internal Revenue Code Section

- To qualify for tax exempt status the non-profit organization must:
  - Be organized and operated exclusively for religious, educational, scientific, or other charitable purposes
  - Not have earnings benefit of any interest
  - Not have any substantial activity that attempts to influence legislation
  - Not participate or intervene in political campaigns
  - Not engage in illegal activities or violate fundamental public policy



4

---

---

---

---

---

---

---

---

## What are typical loan requests?

- Predevelopment
- Construction Loans
- Lines of Credit
- Bridge Financing
- Term Loans
- Standby Letters of Credit

Any of these loans should be analyzed from a qualitative and quantitative perspective.



5

---

---

---

---

---

---

---

---

## Analyzing the loan request

### What is included in the qualitative analysis?

- Type of organization
- Mission or affiliation, formation and history
- Leadership including key management, staff, Board of Directors
- Infrastructure (legal, accounting, systems)
- Programming, activities, tracking results and community impact
- Membership demographics
- By-laws
- Reputation
- Critical issues



6

---

---

---

---

---

---

---

---

## Other Qualitative Considerations

Assess the external risk based on the type of NPO:

- Economic
- Political
- Regulatory
- Reputational
- Other



7

---

---

---

---

---

---

---

---

## What is different about not-for-profit accounting?

- Earning a profit is not the primary mission
- The "equity" section is different
- Most Generally Accepted Accounting Principles (GAAP) apply
- There are some special accounting principles for NPOs
  
- Required Financial Statements include:
  - Statement of Financial Position
  - Statement of Activities
  - Statement of Cash Flows
  
- Comparison of for-profit and non-profit statements



8

---

---

---

---

---

---

---

---

## Quantitative Analysis

Assess the internal risk based on the type of NPO and how it manages its finances.

- Revenue Structure (reliance on key funders, capital campaigns, reimbursements)
- Expense Structure
- Capital Structure
- Collateral Valuation
- Liquidity
- Leverage
- Coverage



9

---

---

---

---

---

---

---

---

## Now back to you:

### What is the risk tolerance at your institution?

- Each financial institution has a unique risk culture and tolerance
- Learn the credit process at your institution
- Advocate for a CDL policy if none exists

10



---

---

---

---

---

---

---

---

## Steps to analyzing the community development loan

- Review loan request
- Perform credit analysis
  - a) Make loan without assistance
  - or
  - b) Identify gaps and continue to pursue
  - or
  - c) Deny the loan request
- If the above decision is 'b', encourage borrower to match the loan request to government, civic or foundation programs
- Re-analyze credit
  - Deny loan
  - Finance project

11



---

---

---

---

---

---

---

---

## Examples of why a loan may not be approved

### Credit Analysis Outcomes:

- Gaps without solutions
- Unacceptable credit risk
- Inadequate return
- Unacceptable profitability
- Unacceptable interest rate risk
- Inadequate management ability
  - Difficult to compensate for this!

12



---

---

---

---

---

---


---

---



Questions?

13



---

---

---

---

---

---


---

---

Case Study: House of Soul

*Your Bank has been asked to provide a \$500,000 unsecured line of credit to a local community-based organization. Please review the attached write-up and determine whether this is something you would like to pursue. If not, why not? If so, are you willing to grant this loan based on the information provided? Do you need additional information? If so, what other information will you request?*

14



---

---

---

---

---

---

---

---

**2012 National Community Development Lending School**

**Course: Lending to Not-for-Profit Organizations**

**Case Study: House of Soul**

**Loan Request: \$500,000 Line of Credit**

***Part 1:***

***Your Bank has been asked to provide a \$500,000 unsecured line of credit to a local community-based organization. Please review the attached write-up and determine whether this is something you would like to pursue. If not, why not? If so, are you willing to grant this loan based on the information provided? Do you need additional information? If so, what other information will you request?***

## House of Soul

### Background

House of Soul is a nonprofit (501 (c)(3)), community-based organization. House of Soul was founded in 1972 by ten concerned, transplanted Puerto Rican parents who sought to find hope for their children and their community in the aftermath of the 1968 Orlando riots. From the beginning, House of Soul made an effort to assist community residents within a culturally sensitive framework. House of Soul's mission, then and today, is to provide for the well being of low and moderate-income families by helping them break the financial and emotional hold of poverty and fostering their self-sufficiency.

House of Soul is committed to providing families with a comprehensive network of culturally sensitive services. It offers more than 20 programs, which include counseling, child care, education, mentoring, job training and placement, homelessness prevention, energy conservation, leadership development, community economic development, and housing. House of Soul's staff of more than 100 full-time employees works to create an atmosphere of hope and optimism within a framework of community building. House of Soul's focus on the family and the community is reflected in its programs. Within House of Soul's day care program (one of the organization's longest and most comprehensive programs), children of diverse backgrounds enjoy family table- style meals, learn, and play within an environment that respects and teaches the value of diversity. In addition, House of Soul's welfare-to-work program, which employs a job placement officer, was contracted by the city to provide job search services to residents.

House of Soul, which serves over 12,000 families annually, founded the first bilingual, bicultural day care center in Florida over 25 years ago. Over 100 children are enrolled in the year-long program annually. The population served by House of Soul reflects the ethnically diverse population of the South Ward of Orlando, which is 45 percent Puerto Rican, 20 percent Black and 10 to 15 percent Hispanic, other than Puerto Ricans. House of Soul is supported by a combination of city, state, county, private and federal funding.

House of Soul's programs and services are available to people of all ages. They take a holistic approach to development of the whole self. Programs range from parenting workshops to inter-generational programs, and from foreclosure prevention services to programs to make people's homes more energy efficient. Their goal is for all residents to maximize their quality of life.

**Community Programs include the following:**

### Housing:

Low income home energy assistance, weatherization, senior citizen heating and cooling program, lead education outreach and comprehensive housing counseling.

### Real Estate Development:

Affordable Housing & Economic Development -Since 1988, House of Soul via its affiliate, HOS Development Corporation has built and sold more than 150 units of affordable housing, providing homeownership and rental income opportunities to 100 families.

Comprehensive Neighborhood Revitalization - House of Soul is engaged in a model comprehensive neighborhood revitalization program that is focused in the Lower Seventh Avenue section of Orlando. The Lower Seventh Avenue Community Plan developed with broad participation by a variety of stakeholders provides guidance for the City of Orlando, residents, business interests, non-profit and other stakeholder activities.

### Adult Development:

Hispanic women resource center; ESL civic classes; ESL classes; immigration assistance; prisoner re-entry services; computer resource center; computer literacy classes; homelessness prevention program; workforce learning link; GED testing; welfare to work initiative.

### Youth, Family & Health:

Early Childhood education; family success center; after school and summer enrichment program; Orlando youth leadership program; youth empowerment services; domestic violence intervention; h.i.v. intervention services; h.i.v. and s.t.d. prevention

### **Leadership and Management:**

House of Soul has a 16-member Board of Directors comprised of business representatives entrenched in the community. These individuals represent a variety of organizations including financial, education, high tech, legal, cultural, social and civic institutions.

The daily operations are conducted by the key management team as follows:

John Florio – Executive Director

Roberto Emanuele – Chief Financial Officer

Stephanie Cipriani – VP of Programming

John Florio has been the Executive Director of House of Soul since 1998. Mr. Florio is involved in local, citywide and state initiatives and works with local, regional and state committees, task forces coalitions and associations. He is a board member of Leadership Orlando and the Orlando Community Development Network as well as a member of the Master Plan Working Group, and other Orlando, state and national groups. Before joining House of Soul, Mr. Florio's career spanned 30 years of service in housing and community development activities both domestically and internationally.

Mr. Emanuele has been with the organization for five years and joined House of Soul from another not-for-profit organization. He has an undergraduate degree in accounting from the University of Texas at Austin and received his MBA from Penn State University.

Ms. Cipriani joined House of Soul in 2009. She was previously employed as a CRA Officer at a local financial institution.

Borrower owns and occupies several properties: 75 Park Avenue, Orlando, FL (Center I- Administration and Early Childhood Development); 76 Bush Avenue, Orlando, FL (Business Office); 39 Seventh Avenue, Orlando, FL (Center II -Personal Development Division & Hispanic Women's Resource Center); 208-216 - 1st Street , Orlando, FL (Center III); ; 595 North Sixth Street, Orlando, FL (Family Success Center II); 317 Petalland Avenue, Orlando, FL (Community & Economic Development and Community Improvement) and 600 Central Avenue, Kissimmee, FL (Kissimmee Home Energy Center; 23 Seventh Avenue, Orlando, FL (Youth, Family & Health Services and Family Success Center )

**Part 2:**

***The spreadsheets are based on the audited financial statements. The actual numbers are categorized into a common format used by the Credit Department.***

***Review the spreads and determine what seems significant to you.***

***Calculate the debt service coverage and leverage ratios using the 2010 numbers.***

NAICS (Industry) 813319 - Other Social Advocacy Organizations

## Stmnt Financial Position

	06/30/08 12 Months Audited	06/30/09 12 Months Audited	06/30/10 12 Months Audited
<b>Monetary Values in USD '000s</b>			
Cash & Cash Equivalents	859	957	324
Marketable Securities	30	30	30
<b>Cash and Equivalents</b>	<b>889</b>	<b>987</b>	<b>354</b>
Grants Receivable - Net CP	924	1,311	2,639
Due from Affiliate	344	354	486
<b>Accts/CP of Oth Receivables</b>	<b>1,268</b>	<b>1,665</b>	<b>3,125</b>
Prepaid Expenses - CP	129	136	216
<b>Operating Current Assets</b>	<b>129</b>	<b>136</b>	<b>216</b>
Other Non-Op Current Assets		44	
<b>Non-Operational Current Assets</b>		<b>44</b>	
<b>Total Current Assets</b>	<b>2,286</b>	<b>2,832</b>	<b>3,695</b>
Land	176	175	253
Buildings & Improvements	4,324	4,441	4,854
Furniture and Fixtures	155	189	197
Machinery & Equipment	218	292	430
Construction in Progress			235
Leasehold Improvements	6	23	23
Transportation Equipment	238	258	142
Other Fixed Assets	22		
<b>Gross Fixed Assets</b>	<b>5,139</b>	<b>5,378</b>	<b>6,134</b>
Accumulated Deprec (-)	1,675	1,828	1,507
<b>Net Fixed Assets</b>	<b>3,464</b>	<b>3,550</b>	<b>4,627</b>
Cash - Restricted		2	102
<b>Total Perm Restrctd Invest</b>		<b>2</b>	<b>102</b>
Other Non-Current Assets	29	1	106
<b>Total Other Non-Current Assets</b>	<b>29</b>	<b>1</b>	<b>106</b>
Intangibles - Other		5	5
Accumulated Amort (-)			1
<b>Net Intangibles</b>		<b>5</b>	<b>4</b>
<b>Total Non-Current Assets</b>	<b>3,493</b>	<b>3,558</b>	<b>4,839</b>
<b>Total Assets</b>	<b>5,779</b>	<b>6,390</b>	<b>8,534</b>
Notes Payable	2	3	101
<b>Notes Payable Short Term</b>	<b>2</b>	<b>3</b>	<b>101</b>
Current Maturities LTD	123	73	89
<b>Current Portion LTD</b>	<b>123</b>	<b>73</b>	<b>89</b>
<b>Short Term Debt</b>	<b>125</b>	<b>76</b>	<b>190</b>
Accounts Payable	130	112	376

	06/30/08 12 Months Audited	06/30/09 12 Months Audited	06/30/10 12 Months Audited
<b>Monetary Values in USD '000s</b>			
Other Payables	1,162	1,161	1,932
<b>Total Operating Payables</b>	<b>1,292</b>	<b>1,273</b>	<b>2,308</b>
Other Benefits Payable - CP		4	
Other Accruals	840	720	800
Self Insurance - CP		343	390
<b>Total Accruals</b>	<b>840</b>	<b>1,067</b>	<b>1,190</b>
<b>Total Current Liabilities</b>	<b>2,257</b>	<b>2,416</b>	<b>3,688</b>
Long Term Debt	1,287	1,308	1,894
Notes Payable	16	11	6
Subordinated Debt	90	90	90
<b>Total Long Term Debt</b>	<b>1,393</b>	<b>1,409</b>	<b>1,990</b>
<b>Total Non-Current Liabilities</b>	<b>1,393</b>	<b>1,409</b>	<b>1,990</b>
<b>Total Liabilities</b>	<b>3,650</b>	<b>3,825</b>	<b>5,678</b>
Unrestricted	1,695	1,981	2,096
Unrestricted Board Designated		256	414
<b>Total Unrestricted Net Assets</b>	<b>1,695</b>	<b>2,237</b>	<b>2,510</b>
Temporarily Restricted	434	328	346
<b>Total Temp Restricted NA</b>	<b>434</b>	<b>328</b>	<b>346</b>
<b>Total Net Assets</b>	<b>2,129</b>	<b>2,565</b>	<b>2,856</b>
<b>Total Liabilities and Net Assets</b>	<b>5,779</b>	<b>6,390</b>	<b>8,534</b>



Stmt of Activity

	06/30/08 12 Months Audited	06/30/09 12 Months Audited	06/30/10 12 Months Audited
<b>Monetary Values in USD '000s</b>			
<b>Net Tuition &amp; Fees</b>	<b>0</b>	<b>0</b>	<b>0</b>
Fed Grants/Contr/Contrib	7,483	8,666	10,599
Private Grants & Contracts	1,693	1,757	2,448
Special Events Revenue	-	71	77
Program Fees	1,342	1,429	1,491
Other Rev/Gains/Support	281	258	309
<b>Net Unrestricted Revenues</b>	<b>10,799</b>	<b>12,181</b>	<b>14,924</b>
NA Release Restr (Oth than PP&E)	1,024	434	328
<b>Tot Unrestr Rev/Gains/Oth Sup</b>	<b>11,823</b>	<b>12,615</b>	<b>15,252</b>
Salary, Wages & Benefits	5,937	8,353	9,626
Rent/Lease Expense	-	359	377
Operation & Maintenance of Plant	72	-	-
General & Admin Expense	769	588	377
Programs	4,490	2,269	4,024
Professional Services	-	128	109
Insurance	-	76	85
Repair & Maintenance/Building Exp	-	32	31
Provisions for Bad Debt	34	1	-
Interest Expense	84	71	107
Depreciation Expense	160	194	241
<b>Total Operating Expenses</b>	<b>11,546</b>	<b>12,071</b>	<b>14,977</b>
<b>Operating Income (Loss)</b>	<b>277</b>	<b>544</b>	<b>275</b>
<b>Total Other Income (Expense)</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Excess (Deficit) Rev Over Exp</b>	<b>277</b>	<b>544</b>	<b>275</b>
Gain (Loss) on Disposition of Assets	(3)	(2)	(2)
<b>Total Other Adjustments</b>	<b>(3)</b>	<b>(2)</b>	<b>(2)</b>
<b>Incr(Decr) in Unrestrcd NA</b>	<b>274</b>	<b>542</b>	<b>273</b>
<b>Temporarily Restricted Funds</b>			
Contributions & Grants	779	328	346
<b>Total Temp Revenues</b>	<b>779</b>	<b>328</b>	<b>346</b>
Net Assets Released from Restr	1,024	434	328
<b>Total Temporarily Restrctcd Exp</b>	<b>1,024</b>	<b>434</b>	<b>328</b>
<b>Temporarily Restrctcd Inc (Loss)</b>	<b>(245)</b>	<b>(106)</b>	<b>18</b>
<b>Total Other Temp Restrctcd Adj</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Incr(Decr) Temp Restrctcd NA</b>	<b>(245)</b>	<b>(106)</b>	<b>18</b>
<b>Permanently Restricted Funds</b>			
<b>Total Perm Revenues</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Perm Restrctcd Inc (Loss)</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Total Other Perm Restrctcd Adj</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Incr(Decr) Perm Restrctcd NA</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Total Incr(Decr) in Net Assets</b>	<b>29</b>	<b>436</b>	<b>291</b>