An Introduction to Debt & Financing for Colorado Primary Care Clinics

Presented by

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September 28, 2016

The Colorado Health Foundation™

Agenda

Introduction

Considering a Loan?

- What types of loans are available?
- What do lenders look for from potential borrowers?
- What should you expect from a lender?

Q&A

Overview:
Nonprofit Finance Fund® (NFF)

NFF, a nonprofit 501(c)(3), envisions a world where capital and expertise come together to create a more just and vibrant society. We unlock the potential of mission-driven organizations through tailored investments, strategic advice, and accessible insights.

- 1000+ customized financial consultations
- Hundreds of partnerships and publications advancing financial awareness and friendlier funding practices for nonprofits

Since 1982, NFF has offered innovative financing solutions, provided loans for working capital and facilities, and leveraged New Market Tax Credits to stimulate private investment in low income communities.

- Over $370 million in loans
- Over $230 million in NMTC
- Over $1.5 billion in capital leveraged for nonprofits
- $30MM in re-grants

NFF is "…arguably the most influential voice in the ongoing effort to reshape thinking and practice about nonprofit capitalization."

-The Nonprofit Times

Colorado Primary Care Clinics – Adapting to a Changing Environment

Nonprofit Finance Fund

Medicaid Expansion

Shift to an Integrated Approach to Patient Care

Moving Towards Outcomes-based Payment Models

Trends Identified from Analysis of Financial and Patient-Related Data

Growing budgets from Medicaid expansion and growing balance sheets from facility projects

Full cost coverage remains a challenge, in spite of improving surpluses

Facility-intensive capital structures

Modest liquidity / flexibility within a changing environment

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Why Do Nonprofits Borrow?

Operational Support

- Seasonal Needs
- Cash Timing Gaps Related to Funding
- Day-to-Day Operating Cash Needs

Financing an Asset

- Facility Acquisition, Construction, Renovations
- Equipment Purchase

Organizational Growth or Expansion

- Predevelopment Planning
- Growth Capital
- Temporary Support

Types of Loans Available

Working Capital Loans: financing for short- and medium-term operating needs

- Line of Credit (LOC)
- Bridge Loan
- Growth-Related Loans
- Equipment Loans

Facility Loans: financing for medium- to long-term facility needs

- Construction/Renovation/Leasehold Improvements/
- Acquisition/Permanent
- Predevelopment

Cash Flow Quiz

True or false…

1. Deficits can cause cash flow challenges. **TRUE**

2. If an organization has a cash flow challenge, it must be the result of a deficit. **FALSE**

3. An organization's year-end balance sheets will tell me if they faced cash flow challenges during the year. **FALSE**

4. Cash flow challenges = bad management. **FALSE**

Working Capital Loans:
Lines of Credit (Revolving)

- Finance a short- to medium-term cash need
- Typically finance current assets (A/R, inventory)
- Monthly interest payments
- Repayment is generally from operating cash flow
- Generally secured by A/R or other business assets
- Clean-up period

Working Capital Loans: Bridge Loans

- Used to bridge timing gap between an organization's need to pay expenses and receipt of payment, generally in a lump sum from a specific source:
  - Government contract
  - Foundation or Corporate grant
  - Seasonal events
- Principal repayment is required upon receipt of funds from the funder
- Monthly interest payments are required, generally from the organization's operating cash flow
- Typically secured by pledge, contract or award

Working Capital Loans:
Loans for Growth and Expansion

- Primary Care Clinics may identify opportunities for additional programs, expansion of existing programs, or new ventures

- Provides funds for hiring additional or upgrading staff, and/or supporting operations until stabilized

- Interest is paid monthly; principal repayment may be timed to match the organization's projected growth benchmarks

Working Capital Loans: Equipment Loans

- Financing equipment may be necessary for the organization's growth and/or operations (e.g. medical equipment acquisition and upgrades, electronic health record systems, other IT systems, etc.)
- Principal and interest payments are made monthly to fully repay the loan over the term, generally the useful life of the equipment
- Typically secured by the underlying asset
- Financing is an alternative to leasing
- Repayment is from cash flow

Types of Loans Available

Working Capital Loans: financing for short- and medium-term operating needs

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Facility Loans: financing for medium- to long-term facility needs

- Construction/Renovation/Leasehold Improvements
- Acquisition/Permanent
- Pre-development

Facility Loans: Construction, Renovation, Leasehold Improvement

- New construction or renovation of owned real estate or leasehold improvements

- May convert to (or be repaid by) permanent financing

- Construction-loan term is based on timeline of project
- Interest paid monthly during construction

- Typically secured by the property

- Loan is disbursed as construction progresses

- Cost overruns, construction delays pose a risk

Facility Loans:
Acquisition/Permanent Loans

- Medium- or long-term financing for the purchase of a facility, or
- May be used to refinance an existing loan (e.g. construction loan)
- Usually collateralized by the underlying asset
- Monthly principal and interest payments required often based on an amortization (10 to 20 years) may be longer than the loan term/maturity
- Repayment from cash flow

Facility Loans: Predevelopment

- Some lenders may provide predevelopment loans to cover costs related to assessing viability of a project and inform decision-making before moving forward
  - Eligible costs include: architectural plans, structural engineering inspections, environmental assessments

What's the Right Loan?
Matching the Loan to the Need

A social service agency receiving significant revenue from the government; but frequently, payment from the government agency is delayed…

Working Capital

Line of Credit

Bridge Loan

A successful and popular community center with overcrowded programs and facilities, is *considering* expanding or buying a new, larger space…

Facility

Predevelopment

A health clinic starting construction on a new, larger facility. While they have secured grant funding, it won't be available for 6-9 months…

Working Capital

Bridge loan

What's the Right Loan? Matching the Loan to the Need

An experienced health care center in a low-income neighborhood is undergoing a major transformation: building an entirely new, large facility to serve more clients…

Facility

Predevelopment
Construction
Mortgage/term loan

A charter school for K-12 needs a significant upgrade of its computers and printers…

Working Capital

Equipment loan

A small performing arts center is growing out of its space. After a thorough internal assessment, they've decided that they are ready to add a small wing to the building and make some renovations…

Facility

Predevelopment
Construction
Mortgage/term loan

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What Do Lenders Look For?

Management and Governance

Financial strength

Planning and Reporting

Repayment sources

Management and Governance

- Strong, stable, experienced management team
- Management team balances programmatic and financial expertise
- Well-developed infrastructure to support operations; including staff, systems, procedures, checks and balances
- Engaged board of directors operates independently from management, performs fiscal oversight
- Board members with diverse, relevant professional backgrounds support and supplement staff expertise

Financial Strength

- Demonstrated history of consistent, unrestricted operating surpluses
- Diversified, reliable, sustainable revenue sources
- Cash flow sufficient to support operations and service debt
- Positive cash balance from year to year
- Enough cash to reinvest, as needed, in facility or other infrastructure costs
- Established reserves for unanticipated events and maintenance

Planning and Reporting

- Timely, accurate reporting and analysis of financial results by management and board
- Consistent accounting practice; reliable, timely internal financial statements
- Timely audits and financial statements
- If Planning for growth, change, or facility projects
  - Internal support: Staff, board, management are aligned
  - Viability: Project scope, size, and goals are reasonable and measurable; funding sources identified
  - Business plans aim for long-term sustainability
    - includes analysis of program and financial strategies, multi-year projections; adjustments made as needed
  - Evaluate competition, user demand, relevance

Repayment Sources

- Demonstrated consistent, unrestricted-operating surpluses sufficient to support operations and service debt (principal and interest payments)
- Repayment sources are available and budgeted by funder
- Repayment sources are committed and confirmed

Beginning the Conversation: Underwriting Considerations

Character

- Strength and tenure of senior management and board
- Reputation in the community and with other stakeholders

Conditions

- What is the condition of the local market?
- What is the condition of the local, state and national economies?

Capacity/Cash Flow

- Ability to service the new debt as well as existing debt obligations
- Historical financials to understand why certain trends occurred
- What is the operational capacity of the organization? Does it have the right people, with the right skills, in the right roles?

Collateral

- What asset is available as repayment source in case the borrower can't repay the loan?
- What is loan to value of the asset?

Capital

- Borrower's net worth
- Borrower's own equity contribution into the project

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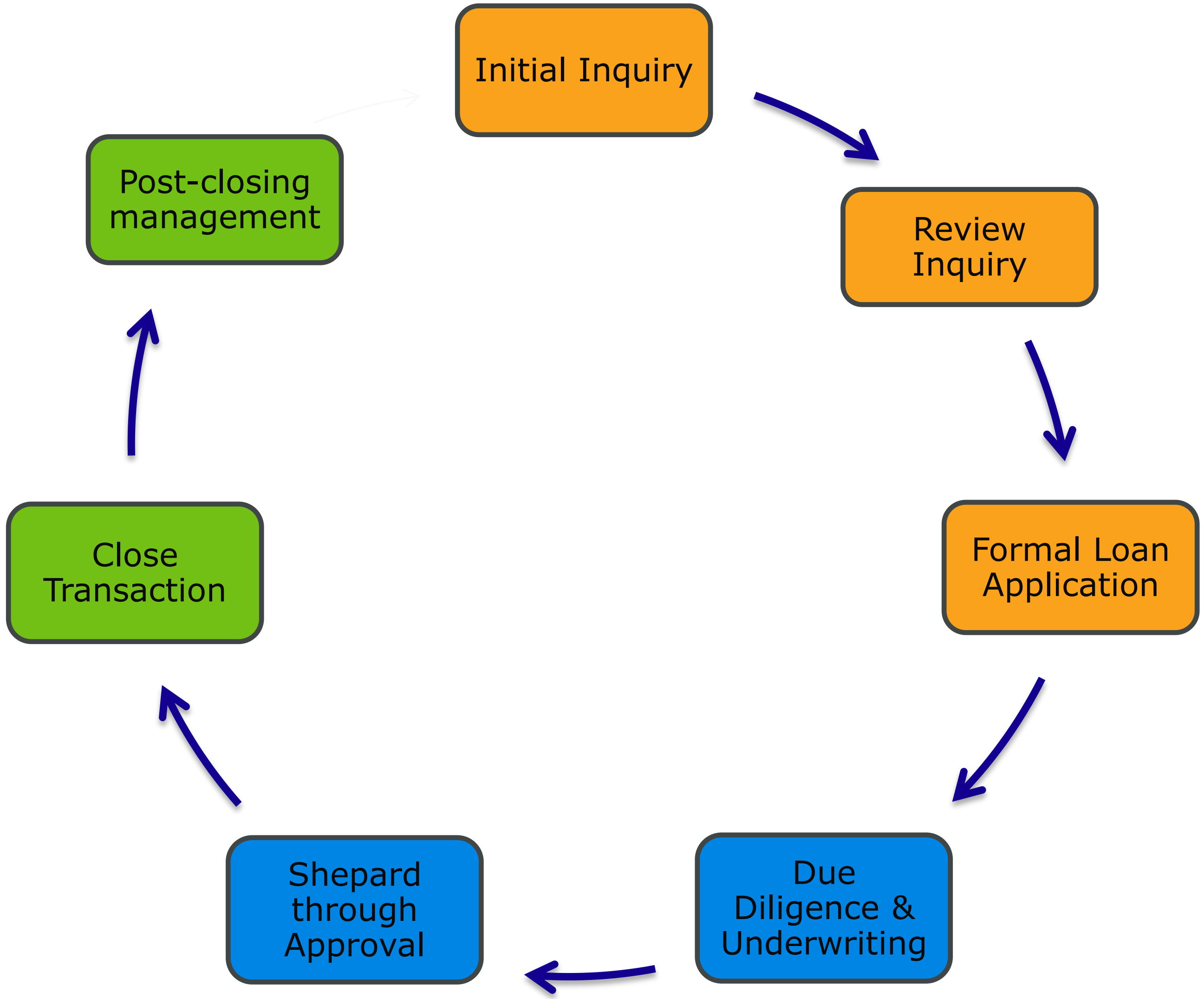
Beginning the Conversation: The Life Cycle of a Loan



Beginning the Conversation: What Will the Lender Ask For?

Financial Info

- Audited financial statements
- Current year budget
- Year-to-date financial statements
- Existing debt and borrowing history
- Sources of repayment
- If repayment is from fundraising, fundraising plan

Org Info

- Strategy and business plan
- Annual report and brochure
- List and bios of board of directors, key staff
- List of major funders

Project Info

- **Facility Projects:**
- Project description, scope of work
- Project budget
- Operating Proforma
- Copies of lease, contract of sale, construction and architect's agreements

- **Working Capital Loans:**
- Copies of major executed contracts
- Monthly cash flow

Red & Yellow Flags

Lines of Credit:

- Proceeds are being used to finance gaps in funding versus bridging working capital needs
- One large drawdown shortly after loan closing that remains outstanding; should have frequent draws and payments throughout the year
- Few to no draws expected for the year, or need is smaller than loan request
- Prior LOC was termed out from previous financial institution
- Very tight debt-service coverage ratio

Facility Financing:

- Sources of project has not been committed or identified
- Weak project team with limited experience
- High loan-to-value
- Small contingency as compared to construction budget
- 1st time management taking on facility project
- No project consultant hired

General:

- Excessive management turnover
- Recent, major organizational change (i.e. merger)
- Consecutive operating deficits
- Minimal net assets
- Tight liquidity

Beginning the Conversation: What are Signs of a Good Lender?

- Do they understand your business?
- Are they willing to invest time in understanding your operating model to offer solutions tailored to your needs?
- Do they know your community and market?
- Do they have competitive terms for your marketplace?
- Is the application process reasonable in scope and time frame?

Assessing your Options: What Are the Types of Lenders?

- Banks – community, regional, national
- Community Development Financial Institutions (CDFIs)
- Governmental & Quasi-Governmental Agencies
- Foundations
- Other mission-based lenders

What If I'm Not Ready?

- **Complete a thorough internal assessment**: what are your vulnerabilities or the areas that need improvement in the four areas that lenders look at?

- Based on your analysis, **develop a work plan**, identifying the resources needed to fill those gaps:
  - Work with a management-support organization?
  - Engage staff and board?
  - Talk to your peers to share challenges & develop solutions?
  - Discuss with your funders; explore potential resources or external expertise?

- **Perform thorough financial analysis**: Implement controls, budget reporting, evaluate programs, profitability etc.

Example: Health Center Background

- ABC health center founded in the 1970's offers family-centered medical care regardless of the patients' ability to pay, to more than 11,000 patients annually
- Designated as a Federally Qualified Health Center (FQHC), ABC is the only facility in its county with the capacity to provide primary medical and dental services to the uninsured and under-insured.
- In addition to pediatric and adult primary care, ABC provides specialized medical programs, including
  - HIV/AIDS outreach,
  - regular visits to homeless shelters,
  - health education and HIV case management services to prison inmates, and
  - an adolescent health program focusing on the special health care needs of youths with high-risk behaviors.
- Strong management and project team with prior facility expansion experience
- Annual budget of $3.5MM with consistent surpluses

Example: Loan Request Overview

- $1.3MM for new construction of 10,000 square foot facility
  - $450k bridge loan
  - $850k construction / term loan (mortgage)
  - Borrower to contribute $300K of its own equity
- Sale of two properties as repayment source for the bridge loan
- Average debt service coverage ratio of 1.45x

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Thank you

To learn more about NFF, visit us at nonprofitfinancefund.org

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