

June 22, 2020

The Honorable Steven Mnuchin
Secretary of the Treasury
Main Treasury
1500 Pennsylvania Avenue, N.W.
Washington, DC 20220

The Honorable Jerome Powell
Chair of the Board of Governors
The Federal Reserve
20th St. and Constitution Avenue, N.W.
Washington, DC 20551

RE: Comments on Nonprofit Organization New Loan Facility Term Sheet and Nonprofit Organization Expanded Loan Facility Term Sheet

Dear Secretary Mnuchin and Chairman Powell:

On behalf of our nearly 5,000 member hospitals, health systems and other health care organizations, our clinician partners — including more than 270,000 affiliated physicians, 2 million nurses and other caregivers — and the 43,000 health care leaders who belong to our professional membership groups, the American Hospital Association (AHA) appreciates the opportunity to comment on the proposed Nonprofit Organization New Loan Facility Term Sheet and proposed Nonprofit Organization Expanded Loan Facility Term Sheet (together, the “Term Sheets”) posted for comment by the Federal Reserve on June 15. We appreciate the efforts of the Department of the Treasury and the Federal Reserve to create and outline new credit facilities to assist numerous business sectors, now including the nonprofit sector, in surviving the health care and financial crises instigated by the COVID-19 pandemic.

Our comments are focused on increasing the possibility that hospitals around the country can make use of this potentially vital loan facility and on easing the daunting conditions imposed on hospitals in the midst of a public health crisis with devastating financial effects.

As noted in AHA’s letters on [April 3](#) and [April 12](#), access by health care organizations to the low-cost loans described under Section 4003(b)(4) of the Coronavirus Aid, Relief, and Economic Security (CARES) Act is an essential component of federal support for hospitals, especially nonprofit hospitals, which provide a substantial measure of health care in this country. Many hospitals are reeling financially from lost revenues and increased expenses incurred from being on the front line of fighting the pandemic. The Federal Reserve facilities outlined in the Term Sheets have the



potential to satisfy loan assistance needs for health care organizations ineligible for Paycheck Protection Program (PPP) loans or for which PPP loan maximums are insufficient. We appreciate that the Federal Reserve and Treasury are committed to a separate variant of the Main Street Lending Program for nonprofit organizations and your previous statements in that regard. In order to ensure the utility of the loan assistance outlined in the Term Sheets, we submit for your consideration the following comments so that this critically-necessary loan facility will be available to as many hospitals in need of such assistance as possible.

1. Eligibility of Public Hospitals

Public hospitals operated by states, counties or cities are involved in the battle against COVID-19, and are essential to the viability of the economies of their geographic locations, as are for-profit and nonprofit hospitals. Due to the size and other requirements of the Municipal Liquidity Facility described in the applicable Term Sheet posted by the Federal Reserve on April 9 and amended on June 3, the Fed's municipal liquidity facility is not directly available to public hospitals, and indirect availability, much less timely indirect availability, also is doubtful given the complexities of intermediated financings. These separate enterprises of state, county or local government should not be precluded from assistance under any of the Fed facilities developed for this crisis. The proposed Term Sheets restrict eligibility to 501(c)(3) and 501(c)(19) organizations, but footnote two states that other forms of organizations may be considered for inclusion as a nonprofit organization under the facilities described in the Term Sheets at the discretion of the Federal Reserve. The AHA urges Treasury and the Federal Reserve to exercise such discretion and specify that public hospitals described in section 501(c)(3) are considered to be exempt from taxation under section 501(a) regardless of whether they have now or have ever had an Internal Revenue Service (IRS) determination letter and are eligible under these loan facilities if the remaining eligibility criteria are satisfied.¹

2. Specific Eligibility Criteria

- **Requirement of borrower existence since Jan. 1, 2015.** The Term Sheets condition borrower eligibility on the borrower's existence prior to Jan. 1, 2015,

¹ On May 3, the Treasury Department issued Question and Answer 42 (Q/A 42) providing further guidance on when a public hospital will be considered a section 501(c)(3) nonprofit organization for purposes of the Paycheck Protection Program. Q/A 42 says in part, "The Administrator will treat a nonprofit hospital exempt from taxation under section 115 of the Internal Revenue Code as meeting the definition of 'nonprofit organization' under section 1102 of the CARES Act if the hospital reasonably determines, in a written record maintained by the hospital, that it is an organization described in section 501(c)(3) of the Internal Revenue Code and is therefore within a category of organization that is exempt from taxation under section 501(a)."

and continuous operation since that date. This apparent seasoning requirement could cause the numerous health care organizations and other nonprofits formed on or after Jan. 1, 2015, to be ineligible for this critical federal loan assistance. Nonprofit health care is a sector in which realignment has been prolific over the past five years and has often resulted in the creation of new subsidiaries, affiliates and stand-alone entities to house the continued operation of acquired enterprises that likely had a long prior operating history. Moreover, this requirement that the borrower be in existence prior to Jan. 1, 2015, stands in marked contrast to the analogous requirement under the Main Street Lending Program for for-profit businesses, which are required to be in existence prior to March 13, 2020, thereby rendering ineligible only borrowers formed with knowledge of the pandemic. Given this background, the requirement that nonprofit borrowers be in existence for approximately five and a half years appears to serve no salutary purpose other than to restrict access to the Federal Reserve facilities by nonprofits. The requirement should be eliminated or the date should be changed to March 13, 2020, consistent with the treatment of other similar entities.

- **Impact of affiliations on eligibility.** The eligibility criteria specify that an eligible borrower must have no more than 15,000 employees or 2019 annual revenues no greater than \$5 billion. In addition, an eligible borrower must have an endowment of less than \$3 billion. The Term Sheets are silent on the applicability of affiliation principles in calculating employees, revenues and endowment. We reiterate, for the reasons discussed in AHA's April 3 letter, that a nonprofit applicant should be permitted to establish eligibility for the facilities described in the Term Sheets by reference to the number of employees of that entity, the revenues of that organization and the endowment of that organization, without regard to any affiliated entities.
- **Financial tests.** In contrast to the Main Street Lending Program facilities for for-profit businesses, which include no financial tests for borrower eligibility, the eligibility criteria under the Term Sheets require that nonprofit borrowers satisfy four separate financial tests: (i) 2019 revenues from donations must be less than 30% of total 2019 revenues; (ii) the ratio of adjusted 2019 earnings before interest, depreciation, and amortization (EBIDA) to unrestricted 2019 operating revenue must be greater than or equal to 5%; (iii) the ratio (expressed as a number of days) of liquid assets at the time of loan origination to average daily expenses over the previous year must be equal to or greater than 90 days; and (iv) at the time of loan origination, the ratio of unrestricted cash and investments to existing outstanding and undrawn available debt, plus the amount of any loan under the facility described in the Term Sheet, plus the amount of any Centers for Medicare & Medicaid Services (CMS) Accelerated and Advance Payments must be greater than 65%.

The AHA understands that the Main Street Lending Program facilities for for-profit businesses limited loan size to four times earnings before interest, taxes, depreciation, and amortization (EBITDA) or six times EBITDA, and that one of the primary reasons the Federal Reserve and Treasury decided to develop separate facilities for nonprofit organizations versus making nonprofit organizations eligible under the Main Street Lending Program facilities for for-profit businesses was concern that such EBITDA-based loan sizing limits might preclude nonprofits from obtaining any loans or adequately sized loans. Accordingly, the Term Sheets remove the EBITDA-based tests for loan sizing purposes and replace them with a loan limit of the lesser of average 2019 quarterly revenue or \$35 million. However, the multiple eligibility tests set forth in the Term Sheets are both quantitatively and qualitatively onerous and may disqualify many nonprofits, including nonprofit hospitals, even though they are sufficiently creditworthy to warrant the federal government's extension of credit in these difficult times.

For example, it must be emphasized that these are nonprofit organizations, and they operate at a low "profit" margin. A requirement of EBITDA to 2019 operating revenues of at least 5% effectively requires a 5% profit margin and would disqualify many if not most nonprofit hospitals. As another example, the 90 days liquidity test, as well as the uncommon (for nonprofit hospitals) liquid assets to debt test, are both based on the borrower's liquidity at the time of loan origination, i.e., in the midst of the pandemic that has given rise to the need to borrow, when liquidity has fallen to crippling low levels for many hospitals.

It is unclear why the Main Street Lending Program disregards a for-profit borrower's mid-pandemic financial status but conditions nonprofit borrowers' access to this important federal financial assistance on a demonstration of mid-pandemic liquidity. (The liquidity tests under the proposed Term Sheets are made even more onerous by including undrawn availability under lines of credit and CMS Accelerated and Advance Payments as debt for purposes of the liquid assets to debt test, thereby penalizing potential borrowers seeking these five-year loans for any unused working capital lines and for obtaining temporary and short-term working capital through the CMS program.) Conditioning eligibility on satisfaction of mid-pandemic liquidity tests will make the Main Street Lending Program inaccessible to many nonprofit borrowers and disfavors nonprofits for this critical federal assistance.

We request that the financial eligibility requirements be revised as follows: (i) nonprofit borrowers that can obtain the loans they seek by satisfying the four or six times EBITDA loan sizing limit should not be required to satisfy any of the financial eligibility tests (we would also suggest that the four or six times loan sizing limits, if applied, should be higher for non-profit borrowers in recognition that, in contrast to EBITDA, none of a non-profit borrower's EBITDA is used to pay taxes and therefore EBITDA can sustain more debt than the identical EBITDA amount); (ii) the 5% profitability test should be eliminated or substantially reduced; and (iii) any liquidity tests should be based on pre-

pandemic data and should not include, as debt, undrawn availability on lines of credit or CMS Accelerated and Advance Payments. The standard measure of financial health for non-profit hospitals is the debt service coverage ratio, and we would recommend that an average annual historic debt service coverage ratio of not more than 1.10 (excluding the proposed debt) and not less than 1.00 (including the new debt as though amortized over a 15-year period beginning on the first day of the historic period) be substituted for the other eligibility requirements, with the historic period being the three most recent fiscal years ending prior to March, 2020 and the coverage ratio being measured under a methodology consistent with the borrower's most recent debt agreement containing a coverage test. If a liquidity test is imposed in addition to a coverage test, it should be a traditional days cash on hand test calculated using liquid assets as of the most recent fiscal year ending prior to March, 2020 and average daily expenses over such most recent fiscal year. The liquid assets to debt test should not be applied to nonprofit hospitals.

3. Loan Collateral

Many, if not most, nonprofit hospitals have outstanding bond debt or bank debt with bond indentures or loan agreements that restrict the incurrence of additional secured debt; unsecured debt is often subject to fewer constraints under applicable debt and lien incurrence covenants. The Term Sheets provide that an Eligible Loan is "a secured or unsecured" term loan, thereby leaving the decision on whether to require loan collateral to the particular lending institution that will retain a 5% interest in the loan. The Term Sheets also state that "Eligible Lenders are expected to conduct an assessment of each potential borrower's financial condition at the time of the potential borrower's application." Since the Federal Reserve, appropriately, is not requiring that the loans under these facilities be collateralized (unless the loan is an expansion of a pre-existing collateralized loan), it should eliminate the lending institution's option to require collateral if pre-existing debt instruments preclude such collateralization and should modify the Term Sheets to clarify, except where expressly required for an expanded loan, that nothing in the Term Sheets is intended to create any presumption that any loans should be made on a secured basis, and that lenders will incur no liability under the program for exercising their discretion to make eligible loans on an unsecured basis.

4. Interest Rate

The Term Sheets specify an adjustable interest rate on loans of LIBOR (1 or 3 month) plus 300 basis points. Section 4003(c)(3)(D)(i) of the CARES Act, which expressly mentions Federal Reserve direct loan facilities to nonprofit organizations, provides that the Treasury Secretary should endeavor that such direct loans be subject to an annualized interest rate that is not higher than 2% per annum. As reflected in provisions of the Internal Revenue Code that permit 501(c)(3)s to borrow at tax-exempt rates, the federal government has long acknowledged the importance of permitting such nonprofit

organizations to access capital at lower rates than those generally available to for-profit businesses. Particularly if the eligibility guidelines for nonprofit organizations remain more stringent than those for for-profit businesses under the Main Street Lending Program, which they should not (see Section 2.b. above), the 2% per annum interest rate cap targeted by Congress in the CARES Act should be implemented for loans to nonprofit organizations.

5. Prepayment Restrictions

The proposed Term Sheets provide that borrowers must commit to 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. The Term Sheets should be clarified, as has been done to a certain extent in the covenant documentation for the for-profit Main Street Lending Programs (the “For-Profit Covenants”), to permit prepayment of debt in connection with a refinancing. There is no reason to preclude nonprofit organizations from replacing, via prepayment, existing debt with other debt that has more favorable terms. The For-Profit Covenants permit refinancing of debt that matures within 90 days of the issuance of the refinancing debt, but that does not address the more common situation in which the refinanced debt is prepaid within 90 days of the issuance of the refinancing debt. And the 90-day limitation is prejudicial to nonprofit hospitals, as well as other borrowers of tax-exempt debt, as such debt is frequently refunded, with taxable debt or, if permitted by the Internal Revenue Code, with tax-exempt debt, more than 90 days prior to the date of prepayment or maturity. Similarly, nonprofit organizations should be permitted to pay down CMS Accelerated and Advance Payments, as well as working capital facilities, when money becomes available for such payments, instead of on the maturity date of the working capital facility or other mandatory repayment date. Such working capital facilities are intended as short-term financing until the borrower has sufficient funds to repay, and borrowers should not be forced to continue incurring unnecessary interest expense by delaying repayment until it is mandatory.

6. Compensation Restrictions

The Term Sheets apply the compensation restrictions in Section 4004 of the CARES Act to the loans described in the Term Sheets. For the reasons stated in our April 3 letter, AHA urges that the Secretary of the Treasury waive such requirements, as the CARES Act authorizes, in the case of “employees” providing medical services. As previously noted, given the national undersupply of medical professionals, hospitals and health systems receiving this type of federal loan should not be pitted against those that do not receive such loans and are able to compensate physicians and other medical personnel at market rates. At a minimum, guidance should clarify that borrowers may honor employment contracts executed prior to March 1, 2020, just as Section 4003 excludes from its restrictions compensation determined pursuant to a collective bargaining agreement entered into prior to March 1, 2020.

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Once again, we appreciate your leadership on these and so many other issues relating to this health, financial and societal crisis, and we look forward to continuing to work with you during this critical time to protect the health of our nation.

Sincerely,

/s/

Melinda Reid Hatton
General Counsel