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Some Pointers For Stressed And Distressed Charitable Orgs

By **James Vincequerra and Gerard Catalanello** (February 15, 2018, 12:26 PM EST)

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There is speculation that one unintended consequence of the recently passed Tax Cuts and Jobs Act is that there will be less charitable giving in 2018 and beyond.[1] While the newly passed tax law does not change in any material way the deductibility of charitable donations, the thinking is that the near doubling of the standard deduction for individuals will indirectly result in a disincentive to charitable giving for those taxpayers who will no longer itemize their deductions.[2] While the more dire predictions may be overblown, it is only sensible for the directors and administrators of not-for-profit charitable organizations to consider the potential for a statistically significant reduction in donations for 2018 and beyond, and plan accordingly.

What to Do and When to Do It

If you are involved in the management of an NFP that relies on donations to meet any portion of its annual operating expenses, now is the time to be proactive and get ahead of problems before they happen.

It is always good practice to stay in regular contact with your donors to keep them invested in the mission of the company. Typically, NFPs are good about outreach to major donors who write the big checks and less diligent about the donors that make smaller donations, even though those smaller donations, when aggregated, often make up a large percentage of the annual receipts. If the speculation about tax reform’s impact is even marginally correct, absent some initiative, a lot of smaller NFPs will start to disappear. The best way to minimize this effect is to keep donors engaged and concerned about the mission. Regular communication and outreach to donors and potential donors is absolutely critical.

Unfortunately, fundraising is hard work, and even with a concerted effort to keep these donors engaged, many NFPs may see their budgets squeezed by less giving. If that is the case, NFP administrators will need to take a hard look at restructuring operations to reduce costs at least until donations rebound.

Restructuring Operations

It is a good idea for NFPs to make a concerted effort to regularly analyze operations for inefficiencies, using existing management, friends of the NFP with complimentary skill sets and, when necessary, outside professionals. Leases, staffing, supply contracts and debt facilities should all be periodically reviewed to ascertain whether or not they still meet institutional needs and have not become a burden or an outsized expense. If they have, renegotiation of those agreements/obligations should be initiated right away. Our experience has been that contract counterparties more often than not are sympathetic to NFP budget constraints and will at least be receptive to a frank and open discussion about the economic difficulties a charitable institution is experiencing and reasonable proposals on how they might help to ease the strain.

In addition to looking inward for potential efficiencies, prudent administrators will also look to potential combinations with other NFPs that share a similar mission. The economies of an NFP combination, if executed properly, can be just as significant as those in the for-profit world. While NFPs may have to contend with additional regulatory oversight for such combinations in certain circumstances (the Charities Bureau of the New York attorney general's office would be one oversight agency in New York), the transaction costs of such a combination are a small price to pay if significant administrative and operational efficiencies can be achieved so that the mission can continue. This is often a difficult conversation to have with the management of well-established NFPs that have become well-recognized institutions in their home cities and towns, but ultimately it is the success of the charitable mission, and not the institutional brand, that should be the guidepost by which charitable directors make these decisions.

When NFP clients are confronted with economic strain or potential combinations, we often advise the board to establish a special subcommittee of directors and other "friends" of the company whose skill set may be more attuned to contract renegotiations and corporate restructuring. The level of engagement by the board and the professionals it chooses to retain can, in close cases, mean the difference between survival and failure for many thinly capitalized NFPs. We are frequently surprised by the number of people willing to donate not only substantial sums of money but significant amounts of their time and energy to causes that are dear to them. This is a critical resource for distressed NFPs and one that more often than not goes untapped.

Know the Law

NFPs and other charitable organizations often have very specific rules directing their governance and operations that are different from those that govern for-profit companies. A good working knowledge of and compliance with the legal and regulatory framework that the NFP survives under is critical. As a case in point, in 2010 New York passed the New York Prudent Management of Institutional Funds Act, or NYPMIFA, which significantly changed the landscape of rules governing how NFPs utilize their endowments. NYPMIFA was passed in response to the financial pressure that many NFPs felt as a result of the economic downturn in 2008-2009, but it may prove to be just as useful to distressed NFPs today. It is also very useful for NFPs to maintain good working relationships with the city and/or state regulators whose job it is to monitor them. While certain NFPs may be regulated by numerous governmental departments (nursing homes and assisted living facilities being two of the most heavily regulated), maintaining good lines of communication with the staff at these departments can be critical when an NFP needs to move quickly through a regulatory review process for an approval necessary to survive.

Moreover, directors of a not for profit must be mindful that they are fiduciaries charged with protecting and preserving the stated mission of the company, as opposed to directors of a for-profit who are typically seated with a mandate to increase value for shareholders and other stakeholders. The difference in discharging one's duty as a board member of a not for profit compared with a for-profit is quite significant when the company is under serious financial distress and survival of the mission is jeopardized.

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[1] Chris Gates, Nonprofits Are the Unintended Victims of the New Tax Bill, TheHill.com (Dec. 29, 2017, 11:00 AM), http://thehill.com/opinion/finance/366773-nonprofits-are-the-unintended-victims-of-new-tax-bill; Dan Cardinali, Kill the Tax Reform Bill, IndependentSector.com (Dec. 15, 2017), https://independentsector.org/news-post/kill-tax-reform-bill/.

[2] Joseph Rosenberg, Phillip Stallworth, The House Tax Bill Is Not Very Charitable to Nonprofits, The Tax Poli

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