

January 11, 2021

TO: Board of Directors

FROM: Reserve Policy Task Force: Molly Myers, Treasurer and Task Force Chair, Mike Cooper, Board Chair; Lisa Gaffney, Vice President; Jonathan Tepper, Sonia Trask

RE: Reserve Policy Update

Background:

At the November 9, 2020 Board meeting, a Reserve Policy Task Force was created “to examine and provide recommendations regarding ArtStream’s Investment Policy and Reserve Policies.”

The Task Force was formed “to make recommendations to the Board regarding uses for the reserve fund, such as resource shortfall, defining a crisis situation, investment for new initiatives, how and why the reserve would be accessed and repaid, and whether to create an endowment fund to grow the asset base to generate income.”

Discussion of the following proposals will inform the Reserve Task Force’s next steps.

Proposal:

1. Approve the recommendation (attached) to establish an Operating Reserve Fund and an Opportunity Reserve Fund.
2. Establish a Finance Committee.
Proposal: The Finance Committee shall have at least three (3) members including the Treasurer. The Finance Committee shall coordinate the Board’s financial oversight responsibilities by recommending policy to the Board, overseeing staff interpretation of policy, and monitoring the implementation of financial policies. The Finance Committee shall oversee the investments and budget. The Finance Committee shall review and present the annual budget proposal to the Board. The Finance Committee shall meet no less than twice a year.
3. Resolve the open questions:
 - A. **Authority to use any of the reserve funds and procedure for the use of the funds**
Proposal: The Executive Director will submit a request to use any reserve fund to the Board Finance Committee. The request will include analysis of the reason for the use of the funds and the plan for repayment.
 - B. **Reporting and monitoring**
Proposal: The Executive Director is responsible for ensuring that the reserve funds are maintained and used only as adopted in this policy. The Executive Director shall ensure that the reserve funds are designated and noted in the financial statements.
 - C. **Review of the reserve policy and investment policy**

Proposal: The Finance Committee will review the reserve policy annually and the investment policy twice a year and report to the full board.

Rationale:

According to *BoardSource*,

The **Finance Committee** supports the board's responsibility for oversight of the organization's fiscal health. It recommends policies to the full board to safeguard the organization's assets, ensures the completeness and accuracy of its financial records, and oversees proper use of resources.

According to *BoardSource*,

Financial reserves act as a safeguard for rainy days and permit an organization to adjust to seasonal variances in expenses and income. Market forces, economic downturns, natural disasters, or other unexpected expenses cannot be controlled by nonprofit managers, but expenses related to them can — and should — be managed. Reserve funds allow an organization to continue activity when income falls unexpectedly, such as when clients are unable to pay their bills on time, when contributions decline substantially, or when a significant grant is not realized. These funds also allow an organization to seize an unprecedented opportunity, such as financing a new venture, making an advantageous capital purchase, or expanding a program at an opportune time.

Reserve funds usually come from the accumulated surpluses of the organization over time. The board, with input from staff, should establish a reserve policy that maintains an appropriate level for the organization, given its mission. Reserve funds are usually designated or allocated by the board as a way to ensure the long-term financial stability of the organization.

The *MD Nonprofits Standards for Excellence* recommendations include:

An organization should have 90 to 180 days of expendable net assets (reserves). If your organization lost all of its funding tomorrow, there should be enough in reserve to continue program operations for three to six months. Organizations also risk having reserves that are too large. Nonprofits are in the business to deliver services in furtherance of their mission, not to accumulate wealth.

Any decrease in unrestricted net assets should amount to no more than 20% of the net asset amount at the beginning of the fiscal year. Larger amounts indicate that the organization failed to react to shortfalls in revenue or overspending in a timely manner.

The Board has a responsibility to set policies ensuring that the organization's assets are protected. These policies, which are all required by the *Standards for Excellence: An Ethics and Accountability Code for the Nonprofit Sector* include but are not limited to:

- **Investment policies** that provide risk guidelines for the investment of the organization's funds and establish a process for reviewing investment performance.
- **Cash reserves** (unrestricted current net assets) that ensure that the organization will meet its financial obligations in a timely manner.

Attachment:

ArtStream Reserve Policy
D R A F T
January 11, 2021

Purpose of the reserve fund: To build and maintain an adequate level of unrestricted net assets to support the day-to-day operations in the event of unforeseen shortfalls; unexpected non-recurring expenses, and strategic initiatives.

Definition and Goals of the Funds

1. The Board of Directors defines the Operating Reserve Fund as the designated unrestricted fund. This fund is set-aside to stabilize the organization's finances by providing a cushion against unexpected events, loss of income, unbudgeted expenses, and temporary shortfall of operating funds.

The target minimum operating reserve fund is equal to four months of average recurring operating expenses, or \$160,000-\$175,000.

To be determined:

- Who has authority to access the funds?
- What is procedure for accessing the funds?
- What are the terms for re-funding the Operating Reserve Fund?

2. The Board of Directors defines the Opportunity Reserve Fund to provide for major unbudgeted expenditures, new programs, current program improvements, and facilities. The investment portfolio serves as the Opportunity Reserve Fund.

To be determined:

- Investment goals and benchmarks
- Who has the authority to access these funds?
- What is procedure for accessing the funds?
- What is the target for total assets in the investment portfolio?
- If investments grow beyond the target, how will strategic initiatives or growth opportunities be evaluated?
- When would assets be large enough to annually allocate a small percent to the operating account?

Accounting for the reserves – The Opportunity Reserve Fund will be recorded in the accounting system and financial statements. The Operating Reserve Funds will be available in cash or cash equivalents and maintained in a segregated account.

Funding for the Reserves - the Reserve Funds will be funded with surplus operating funds, and unrestricted donor gifts. The Board of Directors may direct that a specific source of revenue be set aside for operating reserves, i.e., special appeals, gifts, etc.

Repayment of the funds used – timeframe for repayment

When a request is made for use of the funds, the Executive Director will also present a plan for repayment.

Authority to use the any of the reserve funds and procedure for the use of the funds

The Executive Director will submit a request to use any reserve fund to the Board Finance Committee. The request will include analysis of the reason for the use of the funds and the plan for repayment. Possible reasons to use the reserve fund include ... unforeseen shortfalls; unexpected non-recurring expenses, and strategic initiatives.

Reporting and monitoring – The Executive Director is responsible for ensuring that the reserve funds are maintained and used only as adopted in this policy.

Executive Director shall ensure that the reserve funds are designated and noted in the financial statements.

Review of the reserve policy and investment policy – The finance committee will review the reserve policy annually and investment policy twice a year reporting to the full board.