

The Five Things Every Reserve Fund Needs

Exclusively for Nonprofit Organizations

Everyone will at some point face unexpected costs. Nonprofit organizations are no exception. Although, having sufficient reserve funds can solve these unexpected timing issues. Sufficient reserve funds can also allow an organization to invest in new programs, expand the organization's own reach, fund innovation within or outside of the organization, test out new development ideas, or grow internally. Ultimately, having sufficient reserve funds makes a nonprofit a potential future investor, in either itself or other ventures.

But it is not enough to just have the funds available. In this challenging economy, have the peace of mind that your organization is taking the right approach when it comes to its reserve funds. This means having *at least* the following:

- **Structure** - As one of the most important aspects to any reserve fund and the fiduciaries involved, your organization must have structure. An investment policy statement is an excellent way to implement this necessary structure. An investment policy statement can define the purpose, objectives, and guidelines for investing reserve funds, while also summarizing the reserve fund's investment strategy and outlining the requisite duties and responsibilities of all parties. It can also address not only how to preserve the reserve funds, but how funds can be spent in the future. Finally, the process of implementing an investment policy statement makes structure a decision that includes the entire Board. You need to minimize unnecessary risk and liability, and an investment policy statement can help.
- **Balance** - Generally speaking, investors have certain responsibilities in handling their investments. These responsibilities include maximizing your organization's returns while maintaining acceptable risk. But this is easier said than done. Appropriately balancing invested funds allows you to disregard unimportant elements and conflicting pieces of information that can keep your organization from its goals. Disregarding unimportant elements and conflicting pieces of information also helps prevent Boards from making decisions based on the emotions of fear or greed. Decisions such as those often generate results that would not be in your organization's best interest.
- **Liquidity** - Reserve funds are commonly referred to as "rainy day" funds. A "rainy day" could include the sudden loss of a funding source, unexpected delays in grants or revenue, or a

decrease in special event revenue. These “rainy day” funds are needed when unexpected costs arise, not on a predetermined timeline. And when unexpected costs arise, reserve funds cannot help your organization if you cannot access them when needed. Resolve your rainy days as soon as possible by maintaining appropriate liquidity in your organization’s reserve funds.

- **Cost Efficiency** - Organizations must control expenses as efficiently as possible. Controlling expenses efficiently means managing them prudently in relation to the organization’s assets, its purposes, and its time horizon. Accomplishing this means receiving as much value as possible from your advisor, investments, and custodian. The prudence of utilizing such expertise means it is important to understand the value your organization is receiving through each respective cost.
- **Communication** – Communication related to the reserve funds should be both internal and external. Internally, it is critical to keep the necessary parties aware of key topics. Key topics that could warrant communications with internal parties include the overall investment strategy, the effectiveness of the strategy, and the performance of the reserve funds. External communication is just as critical. Communication between necessary internal parties and external parties, such as your organization’s advisors, should be done regularly. It should also include regular reporting customized to accommodate your organization’s required recipients, internal filing process, and chain of communication.

The accelerating change and uncertainty in today’s world requires nonprofit organizations to be proactive, flexible, and financially prepared. Maintaining sufficient reserves enables nonprofits to maintain long-term financial health, while providing stability and continuity in the near future. Ensuring the reserve fund’s sufficiency promotes the success of your organization, and these five factors are the beginning.

Questions? Let us help you. Contact us today.

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