Healthy Reserves Are No Accident
Hilda H. Polanco, Founder and Managing Director of FMA

If there is one lesson the nonprofit sector has learned in the past few years, it is the value of maintaining healthy reserves.

Whether to be used as a "rainy-day fund," to help smooth out transitions during turbulent times, or to leverage an opportunity in a strategic push, few will question the value of a strong balance sheet defined by ample, liquid unrestricted net assets.

But for executive directors and board members who are looking to grow their reserves, or rebuild them in light of recent history, getting there remains something of a conundrum.

While the approach will vary based on an organization's unique needs, there are a number of steps nonprofit managers can take to nurture growth in reserves in order to help establish long-term stability, as well as strategic relevance.

The biggest barrier to strategically creating a reserve is the perception that nonprofits should strive for an operating budget that balances.

Simply put, the key first step for building a reserve is to create a culture of generating revenue, and surpluses, within the organization.

The notion "as long as we have a balanced budget, we're fine" is anathema for planning for the future.

For organizations that do not have a reserve, balancing revenue and expenses to zero will ensure you never will; for those fortunate enough to have one, balanced budgets purely for the sake of balanced budgets threaten the reserves you do have.

To create that culture, however, management cannot act alone. It will need buy-in at the highest level (through having the board establish it as a priority) as well as the lowest (through staff who recognize and adopt the need for surpluses).

Once an organization has made the decision to create reserves, the budget is always the place to start.

As you already know, a strong budget should include all depreciation costs so your team does not get caught off guard by any necessary capital expenditures due to normal wear and tear.
Similarly, during the budget formulation process, inserting a line item to reflect "Current Year Contribution to Reserves" makes reserves generation a priority for resource allocation, demonstrating it is equally as important as raising revenues for supplies, personnel or occupancy.

Once the board has codified building the reserves into the framework of the budget, it becomes apparent to staff that this has become a key focus for the organization.

Likewise, while the philanthropic community is starting to largely embrace the need for building reserves, organizations that face any potential pushback from funders can overcome it by constructing an actual plan that helps make the case for building reserves in the long term.

**After leadership has removed potential barriers and chosen the processes in building reserves, organizations must make key decisions on what a reserve policy will look like.**

Thus, in creating reserves, there must be clarity in purpose. Management and the board must emphatically state when reserves should be accessible, and be able to answer simple questions such as "when is it a ‘rainy day’?" or "what constitutes an emergency?"

Deciding the purpose of reserves will depend greatly on each organization's goals.

The board can determine how much of its unrestricted net assets to make available for management to use as needed ("Operating Reserve"), how much to set aside for a rainy day ("Board Designated") and how much to earmark for a specific strategic goal ("Special Purpose").

*While an organization can certainly plan to maintain reserves in all three categories, it should see these funds as distinct, or else it may find the same pot of money is stretched too thin.*

**Creating reserves takes years of diligence. It won't happen overnight.**

If done thoughtfully, with a targeted goal through serious planning, however, it will undeniably help build an organization's fiscal strength for the long term.

Thus, only by embracing the proper attitude and steps can organizations move away from the immediate planning of what happens in the next 12 months to the long-term perspective of what happens in the next 12 years.

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