



The Case for Reserves

Cooper Foundation

The Bernard and Audre Rapoport Foundation

Waco Foundation

As donors and contributors to many of the nonprofits that serve McLennan County, and as engaged members of the larger regional and national philanthropic community, we recognize the state of the nonprofit sector is changing. The demand for services remains constant (and in some cases has increased) while the amount of resources available to meet those needs is in flux. A reduction in government support combined with a continual increase in the number of nonprofits created to do good work (a process made easier by the IRS's new application process), has increased the level of competition for philanthropic dollars.

It is in this environment that nonprofits must meet the challenge of not only doing good work, but funding it. Today the work of raising support, which is to be done by board and staff, is on-going. Best practices call for the work of raising funds to be both present and future minded - the job of raising money should not end once the funds for the annual budget are secured.

Just as it is considered good practice for individuals and families to set aside funds for a rainy day, their child's education, future travel or retirement, many foundations consider it good practice for nonprofits to set aside reserves. Specifically, it is important for the board of a nonprofit to establish, monitor, and protect a specific set of funds to prepare for unforeseen circumstances and emergencies that naturally arise when conducting business. We believe that ensuring your ability to serve the community, and more specifically, your target population years from now, means thinking about your nonprofit's financial future today. We understand that many nonprofits and their donors may be challenged by (or even averse to) the notion that nonprofits should set aside money for tomorrow when great needs still exist today, but we encourage nonprofit leaders (as board and staff), that as they grapple through that issue, they should keep in mind the value strong financial health can add to their work and impact today.

Having stability in operations, and more specifically, in one's financial management, increases your ability to:


- Attract donors who are looking to ensure their gifts and investments have the potential for long lasting impact;
- Attract and retain the well qualified and skilled staff needed to run programs, deliver services and manage the nonprofits overall work;
- Expand much needed programs and/or services;
- Hire adequate staff as need and opportunity arises in order to help minimize burnout; and
- Weather fluctuations in grant funding that are the result of the ever increasing competition for grant funds.

The Nonprofit Finance Fund, a nonprofit organization and community development financial institution, provides education and support to nonprofits throughout the country on financial management and the issue of capitalization. While they recognize that each nonprofit's situation may vary, the Nonprofit Finance Fund, based on its experiences and research, has found that three to six months liquidity offers most nonprofits the ability to cover emergency situations, while six months or more of cash puts nonprofits in the ideal position to not only address emergencies, but also weather fluctuations in the economy and plan for future expansions, direction changes, staffing, etc. Ultimately, every nonprofit must find a reserve formula that works best for their circumstances and needs. As they do, they can rest assured that contrary to what they may have heard, the IRS will not penalize them for ending the year with a surplus.

For a number of organizations, a cash reserve is just a starting place. For those whose field of work is indefinite (for example, those who care for the elderly or provide the community with education services), the next step may be to create and/or grow an endowment. Because they are established to exist in perpetuity by allowing nonprofits to pull only from income once they have grown to an adequate size, endowments provide nonprofits with a steady stream of income that can be used for annual operating expenses, program or capital needs and more.

Throughout McLennan County and beyond, there are a number of nonprofit organizations experiencing financial sustainability challenges because the business model under which many of them were developed and continue to operate, leaves them in a perpetual state of need. For many nonprofits, achieving sustainability and ensuring mission completion in this new economic climate calls for moving away from the 'crisis to crisis' model of fundraising and adopting a different set of practices. Establishing and maintaining a reserve lends to your nonprofit's ability to ensure its legacy is not lost. We encourage you to consider growing your reserve today.

If you are interested in learning more about importance of nonprofit reserves, check out Grant Thornton's article: [Maintaining Sufficient Reserves to Protect Your Not-For-Profit Organization](#).



Building a reserve fund can be a slow and arduous process. The first step is to learn how to talk to your donors about the importance of having a reserve (the Foundation can help with this process). Once you have tackled that hurdle, you should consider implementing any or all of the following strategies to progress your effort:

- Maximize in-kind gifts for day to day operations as well as special events and programs;
- Set and keep the goal of not passing deficit based budgets;
- Build a cushion into your nonprofit's annual budget;
- Add a 'reserves' line item into your nonprofit's annual budget and actively seek donations for it;
- Work with current donors to secure non-cash or planned gifts that can be put towards a reserve;
- Establish a policy whereby any unanticipated gift (or a percentage of it) is automatically set aside for the future. To learn more about reserve policies, check out:
 - The Nonprofit Assistance Fund's statement on reserves and access their Nonprofit Reserves and Policy Examples [here](#); or
 - Colorado Nonprofit Association's Operating Reserve and Investment Policy.