FINANCIAL RESERVES POLICY

The purpose of this Financial Reserves Plan ("Plan") is to establish goals with respect to cash reserves of the combined organizations for the following categories:

1. Operating Reserves - 25% of annual operating expenses is recommended by United Way
2. Reserves to fund up-front costs for client expansion
3. Reserves for program expansion to enhance the types of services provided to clients
4. Capital Reserves to fund office expansion and equipment/software upgrades

Based on the accompanying analysis, the goals for reserves, current status and funding needs are as follows:

Goal	$ 9,900,000
Current Status	$ 2,700,000
Funding Need	$ 7,200,000

Once these goals have been adopted by the board of directors, then through the strategic planning process and annual budgeting process, policies and procedures can be put in place designed to achieve these goals and maintain the reserves.

BACKGROUND

The Federal budget continues to incur large deficits. The state of Missouri struggles each year to balance its budget. Many municipalities are experiencing financial difficulties. The economic recovery is moving slowly.

Approximately 95% of revenues supporting Easterseals Midwest's customers come from government funding. Only approximately 5% of budgeted revenues are received from private fund-raising sources. If the Federal or State governments cut funding in the future, the organization needs to be in a position to withstand those funding cuts by having sufficient reserves on hand to see it through the challenges.

Achieving the goals and maintaining the reserves established by this Plan will enable Easterseals Midwest to weather the storm of any unexpected decreases in revenues that could significantly disrupt the services provided to the customers.

While it may take a few years to achieve these goals, it is nonetheless important to establish the financial goals and review them periodically, especially during the time of the annual budget preparation and approval process.

In the spring of 2010, Grant-Thornton, one of the largest accounting organizations outside of the Big Four (Deloitte, Ernst & Young, KPMG and Pricewaterhouse), published a paper entitled,

"Maintaining sufficient reserves to protect your not-for-profit organization". The following are a few points from that report:

- Well-managed not-for-profit organizations should be generating surpluses.

- Adequate liquidity should be in place to avoid a cash crunch and disruption in operations.
- “Not-for-profit organizations that are reliant on only one source of funding, such as fundraising or government contracts, may require additional reserves to protect against a drastic reduction in such funding.”
- The size and complexity of the workforce may have an impact on the level of required reserves.
- Multiple-location operations may require more extensive reserves than single-site programs.
- Programs that require significant up-front investment or require the organization to match government funding or foundation grants may require higher reserves.

In developing a Financial Reserves Plan, it is also important that both the organizations’ Strategic Plan and Financial Reserves Plan support and complement one another.

Operating Reserves equal to a minimum of 25% of annual expenses are recommended. This amount was identified in the “Operating Reserve Policy Toolkit for Nonprofit Organizations” (First Edition, September 15, 2010) sponsored by the National Center for Charitable Statistics, Center on Nonprofits and Philanthropy at the Urban Institute, and United Way Worldwide. Link: http://www.nccs2.org/wiki/images/d/df/Operating_Reserves_Policy_Toolkit_1st_ED_2011-07-28.pdf

CURRENT RESERVES STATUS

Easterseals Midwest (as of December 31, 2012):

Operating Reserves (Board Designated Endowment) * $2.7 million

**As of December 31, 2012, the Easterseals Midwest investments balance totaled just under $4.7 million. Of that $4.7 million, $2.0 million is considered a “permanently restricted endowment” and is documented by a contract between Easterseals Midwest and the estate of the donor. After deducting the $2.0 million from the $4.7 million in investments, the remainder of $2.7 million is in a “Board Designated Endowment” or unrestricted and would be deemed Operating Reserves, since the board of directors has the right to vote on its investment and use.*

GOALS AND OBJECTIVES

1. OPERATING RESERVES

During United Way's review of Easterseals Midwest's operations, United Way pointed out that Easterseals Midwest's financial reserves are light and should be increased; they recommended that an amount equal to 25% of annual expenses be set aside in an operating reserve.

Budgeted Expenses:	
FY-13	$39.0 million
FY-14	
Anticipated increase – one percent (1%)	.4 million
Anticipated FY-14 Revenues	$39.4 million
Operating Reserves Goal:	
25% of budgeted expenses (FY-14 $39.4 million)	**$9.9 million**
Current Status:	
$2.7 million Easterseals Midwest	$ 2.7 million
Fundraising Need:	**$ 7.2 million**

Keep in mind that 25% of expenses should be considered a minimum goal, as this would provide funds for only four months of operating revenues. Given the dependency (95%) on governmental funding, it would not be unreasonable to establish an Operating Reserve objective of six months (50% of annual revenues).

It should be pointed out that in order to maintain a 25% Operating Reserve once achieved, it will be necessary include a line item in the annual operating budget to fund the Operating Reserve account equivalent to 25% of the projected increases in expenses over the former year.

- **NOTE REGARDING SPENDING LIMIT POLICY:** Keep in mind the board-approved "draw down" from Operating Reserves in accordance with Easterseals Midwest's Spending Limit Policy. This policy permits up to 5% of the total Operating Reserves to be withdrawn from reserves to cover annual operations. The practice during FY-13 was to draw 4% of the Operating Reserves for operations.

  The Spending Limit Policy should be reviewed. If client needs can be met without utilizing funds from the reserves, consideration should be given to abandoning the practice of drawing from Operating Reserves pursuant to the Spending Limit Policy until such time as the Operating Reserves Goal is achieved and maintained on an annual basis.

2. UP-FRONT COST OF CLIENT EXPANSION

With 95% of revenues from government-funded programs and with those payments being received approximately 90 days “in arrears”, almost every expansion in the number of clients served by Easterseals Midwest results in a sustained increase in the overall accounts payable. On average, it costs approximately $1,600/month to serve one customer. To add 20 customers, the sustained increase in accounts receivable is approximately $96,000 (20 customers x 3 months x $1,600/month = $96,000).

Reserve Goal:

Sufficient for expansion of 20 clients $96,000

Current Status:

No funds are presently set aside for this purpose.

Shortfall: $96,000

3. PROGRAM EXPANSION:

The quality of our service delivery is constantly reviewed by Easterseals Midwest’s staff and evaluated by Commission on Accreditation of Rehabilitation Facilities (CARF) every three years. Program enhancements that are currently not funded are discussed annually as part of the budget process. These would include enhanced training and certifications, assistive technology for our clients, etc. are examples.

Easterseals Midwest would like to establish a reserve that would allow for implementation of these new program enhancements.

Reserve Goal: $100,000

Current Status:

No funds are presently set aside for this purpose.

4. OFFICE EXPANSION AND EQUIPMENT UPGRADES

As the organization grows to serve additional clients, the office requirements also grow. Additional staffing may be necessary. Generally speaking, office landlords pay for tenant improvements for leased office space; however, that additional cost is amortized over the life of the lease and passed through to the tenant as increased rent. Other costs are associated with office expansion, including such things as office furnishings, computer and communication equipment, stationery, and other supplies. A general rule of thumb would be roughly $25/square foot of space to cover such costs.

Reserve Goal:

Funds sufficient to cover office expansion
of 5,000 square feet: $125,000

Current Status:

No funds are presently set aside for this purpose.