

## **What is the right amount to keep in reserve?**

All nonprofits need to have a “rainy day” fund they can tap into in an emergency. But how much rain do you need to be ready for? Determining the appropriate amount of your organization’s reserves can be tricky.

A reserve fund is what keeps your work moving forward after a sudden financial hit, such as the loss of a long-time supporter or a global disaster that attracts donor dollars at the expense of your cause. It should be of sufficient size and easily accessible. The bonus of building a healthy reserve is that, if you don’t need to tap it in an emergency, you might be able to use it to invest in your organization.

## **Determining the magic number**

Every nonprofit will have a different answer to the question “How much money should be in our reserve?” You’ll need to base the amount on how much it costs to run your organization and the types of scenarios you must be prepared for.

Many not-for-profits determine what it costs each month to keep their organization afloat, and then multiply that amount by a specific time period to come up with their reserve amount. In this scenario, an adequate reserve might be equal to six months, one year or even three years of operating expenses. Generally, the steadier your cash flow (meaning you have regular and predictable expenses and a smooth influx of cash), the lower your reserves need to be. As volatility increases, so should your financial cushion.

In addition to covering day-to-day cash needs, a reserve can provide a way to finance unexpected problems or opportunities. For instance, the reserve can cushion a budget deficit created by a fund-raising event or conference that falls short of financial expectations.

If your warehouse no longer meets your inventory needs, consider setting aside a greater reserve amount so you’re prepared to move or build a new warehouse. If you plan to offer new services in the future, you can use a reserve to help offset startup costs.

In these cases, your board should brainstorm the possible scenarios your group might find itself in over several years’ time, estimate the costs and determine ways to set aside cash into a reserve for coverage.

## **Stashing the cash**

After calculating a reserve figure and determining a way to allocate part of your budget to it, make smart decisions about what to do with the reserve so your funds are secure, earn interest if possible and are accessible.

There are many types of investment vehicles to consider, so do your homework. You can use interest-bearing checking or savings accounts, certificates of deposit, Treasury bills, bond funds, money market accounts and numerous other vehicles that might be a good match for your situation.

There are pros and cons to all these accounts, and if you don't pay attention to the details, fees and penalties can chip away your hard-earned reserve. Be aware of minimum balance amounts and penalties if you drop below that threshold as well as fees for drawing on the funds. Another area to watch for is availability. Will you have access to your reserve when you need it?

Your accountant can help you weigh the pros and cons of the investments you are considering. If you have very large reserves, consider retaining a professional financial advisor to manage the investments with the input of your board.

## **Is “too much” possible?**

When you're diligently allocating part of your monthly budget to your reserve, earning a bit of interest and not taking any money out, eventually you'll find yourself with more than the amount you were shooting for. Congratulations! You now have the ability to invest some of that money into your organization. The goal is not to grow the biggest reserve you can. It's to grow the biggest reserve you *need*.

In fact, amassing more than several years' worth of operating expenses may raise a red flag with organizations like the American Institute of Philanthropy, Charity Navigator, and the Better Business Bureau's Wise Giving Alliance, which provide guidance to consumers on charities and charitable giving.

Associations aren't immune from the “too much in reserve” quandary. Members may agree that having a safety net is prudent, but at a certain point they want to see their dues and other monies invested in membership benefits.

## **Shelter from the storm**

Having a rainy day fund is just good business. If your organization doesn't have a policy for and the means of funding a reserve account, start making plans today. Those storm clouds could roll in when you least expect them.