Podcast transcript:

Talking about... charity reserves

With Sarah Vibert, CEO, NCVO; Jane Ide, CEO, ACEVO and Caron Bradshaw, CEO, Charity Finance Group.

00:00:00 Sarah Vibert

Welcome to this session on reserves with NCVO, ACEVO and Charity Finance Group. I'm Sarah vibert. I'm the chief executive at NCVO and I'm joined by my colleagues Jane Ide, who's the chief exec at ACEVO, and Caron Bradshaw, who's CEO at Charity Finance Group. Now. It's often said that reserves are something that are kept for a rainy day, and certainly over the last few years. I think a lot of us feel like we are living in a monsoon, never mind a rainy day, and we emerge from the pandemic straight into a cost of living crisis. Energy costs have spiralled, inflations exploding.

00:00:37 Sarah Vibert

And what Jane, Caron and myself are increasingly hearing from our members is big concerns about reserves. They want to know how much they should be keeping. How should they be talking about them to their members, the regulator. How do they strike balance between keeping reserves for the ongoing and next rainy day and spending reserves thinking about what flexibility we need given we've got such volatile and uncertain times.

00:01:07 Sarah Vibert

What we're going to do today is have a bit of a chat about all of this. It's a lot of territory to cover. We'll all share our own experiences, things we've been hearing from our members and hopefully give you a few tips to help you as well running your organisations.

00:01:21 Sarah Vibert

So, I'm just going to kick off by getting Caron, who's definitely the finance expert of the three of us, just to give us a bit of an intro on what are charity reserves Caron.

00:01:33 Caron Bradshaw

Right, so I'm not going to give you a technical explanation because I think we can get into all of the technical reasons around whether or not you include your investments or your fixed assets. Let's just cut it right down to the basics and say that reserves are the money that you don't spend. It's the money you keep back for other things and they don't necessarily sit in your bank account.

00:01:56 Caron Bradshaw

They might be tied up in something else. They might be in an investment, they might be in a building. So we've got, we've got to just keep it right down to the basic level, reserves [are] those things that you hold back in order to be able to deliver your charitable activities to your beneficiaries when you need to.

00:02:11 Caron Bradshaw

And it can be made-up in a whole bunch of things. It could be money that you keep back for working capital, or it might be money that you keep back because you like to be investing in. Buying a building or bringing on board some fundraising expertise for a particular project or whatever, so it they can be made-up of a whole host of different things, and we'll go through that, I'm sure, during the course of this conversation.

00:02:32 Sarah Vibert

Absolutely brilliant, Caron. It's interesting because I think I always say NCVO is a bit of a microcosm of the sector in terms of kind of our experiences and certainly over the last few years we have had to spend reserves because it was that rainy day. It was pouring, money disappeared overnight when our conference suite was shut, and we just had to plug that gap. But also, our trustees are very proactive in how to spend reserves too. So, for example, money was designated several years ago for investing in our digital infrastructure.

00:03:04 Sarah Vibert

That money, you know, has been planned over a number of years to be spent and like you just described some of our reserves are tied up in investments. And it's, you know, it's not readily available then.

00:03:12 Sarah Vibert

Jane, what's your experience in terms of the ACEVO Board and how you're spending or not spending your reserves?

00:03:17 Jane Ide

Well, I'd go back a step actually, Sarah, because I I came into the sector six years ago and I think the first thing is reserves is one of those things everybody in the sector talks about and so few people really understand what they are. It's kind of like a black art trying to understand what it's all about and I started in an organisation that had been surviving on its reserves for several years. It had had its sunny days [and] many, many years previously had fortunately managed to save a lot of that money, put it to the side, by the time I arrived, it had had the monsoon for nearly a decade, actually not far off, certainly six or seven years.

00:03:56 Jane Ide

It was a perfect example of where the world had shifted around it, and the income streams that it had previously built those reserves from simply didn't exist any more. And so I had the job in that organisation of turning it around and having to use those reserves as the way to keep us afloat whilst absolutely believing that there was a future for this organisation and changing that business model.

00:04:21 Jane Ide

And if those reserves had not been there, that opportunity would have been lost and I was very, very proud of the fact that we were able to turn it around and it is still a very thriving organisation and moving forward. What I've inherited at ACEVO is almost the opposite example in the sense that my predecessor, Vicky [Browning, former CEO] had done a fantastic job of putting the organisation on a really solid footing.

00:04:44 Jane Ide

We have very good reserves. In fact, if anything, we have too much in our reserves by as measured by our reserves policy...and I'm sure we'll talk a lot about reserves policies in all of this because I think that it’s fascinating.

00:04:56 Jane Ide

And right. And actually ACEVO has had a possibly a rather unusual history compared to many in the sector that there have been regular attempts and continued in attempts to spend down those reserves and to invest that money wisely. And it has been used in all sorts of very interesting ways. And yet because the income generation model that we work on is actually proving very successful and has done so far, we keep achieving a surplus, so we keep putting money back into those reserves even though we're trying to pay them down.

00:05:27 Caron Bradshaw

For us, CFG [Charity Finance Group] had a whole load of plans to spend down their excess reserves as we came into the pandemic. And then immediately had to ditch all of those plans and use them for a completely different purpose. Because I don't think anyone's policy would have said all of your income routes are going to be cut off overnight and your income is going to be really suppressed, but your expenditure is not going to be easily cut back or reduced.

00:05:55 Caron Bradshaw

Because, for us, and probably same for you, is most of our costs are in our building and our people. So, there wasn't a lot that we could do to pull on levers to reduce our expenditure without short of laying people off, which I know an awful lot of organisations had to do, but we were able to use our reserves to get through that period of real uncertainty in depressed income.

00:06:14 Sarah Vibert

And I think that gets to kind of guess the heart of why you need to have reserves because it does give you that agility. It buys you time, doesn't it?

00:06:22 Sarah Vibert

I was going to just ask you though, Caron, I think we've talked – Jane and I both gave a couple of examples of how we view and use reserves to keep an organisation going to be brought more money in or to very deliberately spend down reserves – because let's not forget your membership. Bodies and Members want to see us using our money for impact in the sector, other things that organisations probably shouldn't be spending reserves on.

00:06:44 Caron Bradshaw

So, I think probably the first thing I should have said in our original conversation is that actually the law doesn't require you to keep any money back. You are supposed to spend it, and you're only supposed to keep hold of it if you've got a good reason to hold on to it.

00:06:57 Caron Bradshaw

But then the question is when you do have this pot of reserves, what should you be using it for? And I think it's a really important question at this point in time when we are leaning into a huge cost of living crisis. Our staff are struggling. We probably need to make investments in things that are much more expensive than they were before. So perhaps what you put away or designated for a particular cause isn't going to even touch the sides in terms of fulfilling that intent from the board. So what I would say is there's no rule of thumb. No one area that you can't spend reserves on as long as it's within your charitable objectives. But! And here's the big but, you should never spend money on something that you require an income source to keep going on an ongoing basis. So, if you want to invest in bringing on a fundraiser, for example, there's nothing wrong with that. There's nothing wrong with using your reserves to fund a fundraiser, but the reason why that's a problem is because the fundraiser, in theory, should be bringing in funds, so they're going to be effectively replenishing those reserves in future.

00:07:55 Caron Bradshaw

Similarly, a lot of us have put some money towards our staff during the cost of living crisis to try and reflect the fact that they're going through really hard times. So CFG certainly gave a one-off payment to staff, so that again goes towards salaries etcetera. But it's something that we're not building into the expenses of the organisation without knowing how we're going to then cover that on an ongoing basis.

00:08:16 Caron Bradshaw

So, nothing's off the plate, as it were, but you do have to have a thought on if you're going to spend it, you've spent it, it can't then be spent on something else. So how are you going to ensure that the money is then replenished for you to be able to keep on investing in delivering impact to your beneficiaries? Because that's ultimately what you're trying to do. You're not there to protect reserves. The reserves are there to protect the charity.

00:08:36 Sarah Vibert

Really well put. And I think one of the things we've seen from Members recently has been just really challenging decisions that trustees are having to make around things like pay rises. And I think what I'm hearing you say is that, you know, using reserves to fund consolidated pay rises on an ongoing basis, unless there's an income stream attached to that, you're going to run into problems and being able to continue to sustain the organisation after a few years once the reserves are gone.

00:08:59 Caron Bradshaw

Yeah, once you've spent them, they're spent. So, it's the long-term, sustainable approach to it, isn't to just simply add it on to salaries and hope that at some point in the future things will get back right because you're not doing anyone any favours. You want the staff to be able to continue to provide support to beneficiaries, but if you're taking away, all of the flexibility that you described a minute ago, and all of the ability for you to be able to invest in the future and to support beneficial and ongoing basis blowing that all in one go and building in a whole load of expenses that you can't then recover at a later point, you're not doing anyone any favours least of all your beneficiaries, or your staff.

00:09:39 Jane Ide

And if I can just sort of add to that, because I think that's exactly where we've been at a key vote in the sense that we're small team, we're a hybrid organisation. We don't have a building to invest in. We're not about to go out and buy one. This would certainly not be the time to do that. There are a number of things that we wanted to spend our reserves on over the years in terms of projects and programmes and so on, but actually right now our biggest challenge is capacity, that our membership has nearly doubled in the last 5-6 years and the size of our team really hasn't. And there comes a point where, you know, we're not going to be able to continue to deliver what we currently deliver.

00:10:13 Jane Ide

And that that is just as you said earlier, Sarah, microcosm of what so many of our Members are going through. And for me this is actually a really good example of good governance because we've gone through the process of identifying what the cost would be of investment in that capacity, and thinking very hard about actually what will that additional capacity do. Will it help us just stand still? Will it help us grow? Will help us improve services? And so on and so forth. Really work that one through and link that to this challenge we have about our reserves actually being currently higher than they should bein our reserves policy.

00:10:48 Jane Ide

We created a model which enables us to plan four or five years ahead, and it was, you know, at the time we started it was well, if this happens, then this happens and this happens and this happens. But what that's actually enabled the board to do is to make a really clear decision about where they were prepared to risk not using our reserves, with the absolute understanding that every quarter, every month if necessary, we will be updating that model so we can see exactly the point at which it becomes detrimental to our reserves to have that investment running forward.

00:11:24 Jane Ide

And again, it's always about, it's exactly as, as Caron says, it's not about just paying the salaries. There are times when you have to do that. That's what I had to do in a previous role because we wouldn't have had anybody there to build the organisation, but that was absolutely on this basis that as my board there put it, we either you know this is our one last shot, we go down with all flags flying and we use our reserves to do that intelligently because otherwise what's the point they're just sitting there doing nothing while the organisation fails. But in this case, it's very much about recognising and believing we need to do something. This is the lever we have available to pull, but once we've pulled it, we then absolutely have to keep a very close eye on what the consequences are.

00:12:03 Jane Ide

I think there's always a danger when you're using your reserves around salaries and people that you've got in your team, there is always a danger that that becomes the way it is, always going to be. And, of course, we all want to be in a position where that's the case, but you have to be realistic about the fact that sometimes you may have to change that and you may have to pull back and say this is putting us in too much of a risky situation and it's about weighing up those risks and that's all of this is absolutely about governance far more than it is about money.

00:12:32 Sarah Vibert

Absolutely. And I mean the word both of you have used as well is risk and I guess it's, as trustees, weighing up the risk of doing something versus not doing. Something which I guess again just gets to the heart of kind of board operation, sorry Caron, you're going to come in?

00:12:45 Caron Bradshaw

Yeah, no, exactly. The point you're going to make, Sarah. It's risk management. What we're talking about here is active risk management. Having a really detailed reserves policy and then not being flexible to be able to be agile when something comes from you left field.

00:13:05 Sarah Vibert

I mean, I found Jane's example really interesting because it's almost exactly the same situation I had with my first chief exec role. I also inherited an organisation with good reserves, and took a decision to invest in staff because we needed to grow and grow impact. But I wonder, Caron, - I mean that was a very small organisation and I guess ACEVO is a small to medium organisation – is it the same across the board for all charities, or are there different considerations for a much larger organisation compared to smaller charities in terms of kind of reserves policy and how you're thinking about reserve?

00:13:31 Caron Bradshaw

I think in principles, at a theoretical level, there shouldn't be any difference. But I think there are practical differences and when you are a very large organisation. You may have a number of other levers that you could call that are beyond just cash or cash equivalents. And increasingly, we're seeing large organisations use things like liquidity policies where they look at how liquid their assets are and therefore do they need to keep back reserves in the way that we would typically consider reserves to be, when actually they might be able to sell off a particular part of an activity or they might be able to sell a building or whatever the asset might be that they can liquidate to use for the benefit of the beneficiaries.

00:14:14 Caron Bradshaw

And you saw quite a lot of that during Covid, actually, where there was a lot of adjustments being made on profiles that were anticipating fundraising being really, really hard-pressed by Covid, for example. So an awful lot of organisations, larger organisations were falling back on liquidating some of those assets in order to give them that cushion, rather than really hammering their reserves. So yeah, there are differences between large and small, and I think the other aspect I'd pull out is I think reserves can be reputationally damaging whether they're excess or adequate, particularly for larger organisations. For smaller organisations, I think people expect you to be a bit more hand-to-mouth, so there's less eyebrow raising if you're operating with no reserves, but for a larger organisation, there's an anticipation that they should be sitting on a reasonable chunk of money to enable them to be able to, you know, deal with whatever is thrown at them.

00:15:04 Sarah Vibert

You mentioned reserves policies earlier. Let's get into the nitty gritty of reserves policies. How could charities that are listening to this, how should they be going about calculating the right level of reserves? Because it's kind of like $1,000,000 question, isn't it?

00:15:15 Caron Bradshaw

My sort of starter for 10 would be to sit down and think about your business model. Because if you don't understand where your income streams are coming from, then how can you determine what you need to keep back in order to to give you that support. The next bit is thinking about how sensitive those income streams are, how volatile they are. So if you're an organisation that has, let's say, 10 years of guaranteed funding that covers everything, arguably, why would you need to keep reserves at all, because you've got everything guaranteed.

00:15:44 Caron Bradshaw

Conversely, if you're an organisation that is very much on short cycles where there can be a lot of volatility in your income, you might want to be keeping a much bigger chunk of money back to safeguard against those income streams going down. Often as organisations we'll think about things in terms of working capital. So, what do I need on an ongoing basis to be able to deliver the services and activities that we're doing?

00:16:05 Caron Bradshaw

So if an organisation, for example, is thinking if we bought a building and we delivered out to our beneficiaries much more efficiently through that, but we don't actually currently have the money, you might start putting aside reserves with a view to saving up for or providing some sort of match funding pot that you can then go to a grantmaker and leverage that money and say, look, we've got this money, would you support the other bit? And we can then bring about that and so that will be across the board, that could be an IT system or it could be a physical asset, it could be a minibus, it could be a whole bunch of different things and then you might have stuff that is that you keep aside to deal with other types of risk. So really the rule of thumb is what's your business model? How much do you individually as an organisation think you need to safeguard against the risks that you are facing and that's the amount of money that you should be putting aside, not a three to six months of operating costs. And ideally it should be arranged so on the minimum level, we think this, on the maximum level we think that, and then aiming for somewhere between the two.

00:16:59 Sarah Vibert

That's super helpful and I guess I mean the other thing to say here and certainly this is what kind of the NCVO team would talk about a lot in terms of good governance is just being really transparent about that decision making and making sure that all of your stakeholders and donors and kind of everyone else knows what decisions you've made and why you're holding the level of reserves that you are.

00:17:18 Jane Ide

But can I also add to that because I think you're absolutely right on that and exactly everything that Caron has said. But I think there's also a fundamental piece of which is review your reserves policy. I've seen so often the reserves policy kind of sits there. It gathers dust, it gets cobwebs growing all over it, and it's set in stone. So, when I go back to, you know, our own experience at ACEVO, though, you know, we've set out this plan. The monitoring is absolutely crucial. It starts from this financial year. So it's new in place and as part of our normal governance routine, we will be reviewing our reserves policy at our next finance and Audit Committee. And it's entirely possible that that reserves policy that underpins this plan will change, and therefore everything in the model will need to change.

00:18:04 Jane Ide

But that's how you, by planning it out, by thinking ahead, by having those formulas, can actually say, well, if we change this button here then it changes that outcome there. That's how we can manage those risks.

00:18:18 Jane Ide

Just one question, Caron, over what period of time ahead do you think people should be thinking about this in terms of, you know, you were talking about if somebody's got 10 years of funding, then fine, you're okay for 10 years, but at some point you've got to start thinking beyond that 10 year point?

00:18:33 Caron Bradshaw

Yeah, it depends. But I think it does. And I think in terms of what you should put in your reserves policy, I think it's sensible to have a thought about short term, medium term and long term horizons and think about your risks in that way. I think it's the same with, as you were just saying, about the funding example I gave. If you are an organisation that sees your service delivery to beneficiaries going beyond that 10-year time horizon, because of course we're not here to keep charities going just because we want the charities to keep going, they're here to meet a need. If that need is going to continue after the 10 years, then absolutely you should be thinking about, well, how do we set ourselves up to a position where that funding might completely come to an end, and what would we then do?

00:19:20 Caron Bradshaw

But it might be totally feasible that after 10 years the need is met and you no longer need to be around. So your attitude towards what you keep in reserve might be quite different then it might be about orderly closing down of an organisation.

00:19:31 Sarah Vibert

What you just said then, Caron, just reminding me of a few conversations I've had in the last, over the last year, I guess, we're seeing a sector really in crisis because of cost of living and I've heard charity leaders say things like, well, we're probably just going to have to kind of almost sacrifice the organisation. There's so much need in front of us, when the funding isn't coming in, the costs are spiralling. So, we're just going to keep going until there's nothing left. I mean, I know there's guidance from the Charity Commission around kind of closing in an orderly way. Maybe you can maybe talk a bit to that, but also I mean I guess, there's a big picture thing here around kind of where the sector is and the levels of reserve and the sector and the kind of financial pressures on the sector right now. How trustees can be making responsible decisions within that kind of framework.

00:20:15 Caron Bradshaw

Yeah, I mean, every year as part of our accounting periods, we have to, if we, if we're big enough to have to put in together true and fair accounts, we have to say that we've 'going concern' and that's signed off every year. If you are of a size to be audited by the auditors on the basis of whether you can reasonably keep going for 12-18 months after the date that the audit is signed off, so I think anybody who is assuming that they are not a going concern should be having a bigger conversation than simply about their reserves, which is one of my objections to why the wording of the reserves guidance changed by the Charity Commission all those years ago in the light of The Kids Company, because I think it focused us on the wrong things.

00:20:57 Caron Bradshaw

What we should have been talking about was educating trustees and executives to think about the relationship between risks and reserves and actually bigger risk. The risk of being overly reliant on a particular source of income, which in that case might have been a very persuasive fundraiser, but equally, it could have been a contract with an entity that you think is a surefire thing, and you've put all your eggs in that basket. You've assumed that it's never gonna end and suddenly it does. So I think for me the reserves question should have been one of what's the relationship between risk and reserves and ensuring that trustees and executives are equipped to have honest conversations about what those risks really are, rather than skating around some of these more difficult conversations, particularly things like, you know, staff, CEOs, buildings, contracts, relationships. These are all difficult and messy conversations sometimes to have.

00:21:47 Sarah Vibert

Yeah, absolutely. And what about you, Jane? What are you hearing from your Members? Are you hearing that real kind of financial distress.

00:21:53 Jane Ide

Yes, and what, certainly, what we're hearing at the moment is that whereas a year ago when I first arrived, finance has always been an issue, you know, there's always gonna be some pressure around that. So is the relationship between chair and chief exec then, you know, that was the thing that was driving most of our calls to our support line I think then. Around sort of the latter end of last year coming into Christmas, it was much more about the deep anxieties that leaders were feeling about how were they going to support their teams, their organisations in the cost of living crisis. And what I'm hearing now is that we're back into that or we're heading back into that place where it's the money really, you know, quite tangibly, it's the lack of funding that you're starting to drive those calls.

00:22:39 Jane Ide

My instinct is that we're now at the beginning of that, that period of time, that the risks and the difficulties that we could see coming through the pandemic are now starting to come home to roost and maybe not necessarily in the same organisations that we thought that we were going to. I think there's been, you know, quite a lot of shifting around, but I had a conversation with a funder not that long ago, who was telling me that, you know, they are so oversubscribed this year that they have had to say no to a number of organisations who would normally have been funded and who have built their business plan around the fact that they've always had that funding, exactly as Caron said, it's always been there. And now all of a sudden it's not.

00:23:17 Sarah Vibert

So I'll come to each of you. What's your top takeaway that yu want people to take from this little conversation we've had today?

00:23:25 Jane Ide

I think for me, the top takeaway is think about it. Don't, don't just let it happen to you, particularly if you're the leader of your organisation, you know, work with your board, work with your Treasurer, work with your Finance Committee, your head of finance, whoever it is that you've got around, you and I recognise that for many in smaller organisations, even you know, not even all of those things would be in play, but think about it and think about it intelligently. Tie your reserves to your risks and work out what you're trying to do.

00:23:53 Jane Ide

What is the rainy day you are trying to protect yourself against? And how do you best use what available to do that as it appears right now and be prepared to change that again in a year's time or in two years' time or whatever it is because the world will keep changing.

00:24:06 Sarah Vibert

Brilliant. Thank you, Jane. And that's certainly very close to what my top takeaway would be, which is around kind of how closely this is linked to risk and particularly that earlier conversation we had around, when is it actually a sensible risk-based decision to spend money on new staff coming in to deliver more impact versus when you shouldn't be drawing on reserves to fund things that won't have future income streams attached to them. Caron, what's your biggest takeaway?

00:24:31 Caron Bradshaw

Well, I think mine probably nicely and neatly follows on from both of yours, which is about the communication of it. I think people can make assumptions about what you do and you have to tell them actually what it means. Otherwise, you will have people looking at your reserves and saying, well, I'm not going to donate to you because your reserves are massive and not recognising that it's being kept aside to buy an air ambulance or pay for a lifeboat, for example. Or conversely, you don't have enough money and we think you're fragile, so be clear on what your reserves policy is, be clear on what your current position is and how you are living in context to that position above or below your reserves policy. Then communicate, communicate, communicate, not just through your trustees' annual report, but on your website. In every opportunity, with your funders, etcetera, your supporters, your donors, your staff. And the other thing I think is worth thinking about is obviously a lot of these policies will have been written in a low inflationary environment and we are now in a very high inflationary environment and that means that the money in the bank and the money in reserves is worth less, but it also means your ability to be able to generate a surplus in order to rebuild reserves that have been dipped into is also undermined. So, you know, I think we underestimate the impact of inflation on our reserves position at our peril.

00:25:48 Caron Bradshaw

And I think an awful lot of boards need to just sort of stand back and think about that question of what does inflation now mean, not just whether we're going to experience another pandemic or there's going to be another crisis down the road.

00:26:00 Sarah Vibert

Caron, Jane, thank you so much. It's been brilliant talking to you and thank you everyone, for listening.

00:26:05 Jane Ide

Thank you, Sarah.

00:26:06 Caron Bradshaw

Been a pleasure.

With thanks to Sarah Vibert, Jane Ide and Caron Bradshaw.