

**American Library Association
Finance and Audit Committee Report
to the ALA Executive Board
Saturday October 22, 2016**

The Finance and Audit Committee (F&A) is pleased to report to the Executive Board on its activities at its fall meeting. The Committee met on Thursday October 22nd to discuss and review a number of financial issues. Below is a list of the primary topics discussed:

- BARC Report (EBD #3.1)
- F&A Orientation
- FY16 Audit Process & Introduction
- 2016 Year-End Budget Review (EBD #14.1)
- Final FY 2017 Budget Review (EBD #14.2)
 - **Action Item**
- Controller's Report (EBD #4.2)
- Director of Financial Reporting and Compliance Report (EBD #4.3)
- Endowment Report (EBD #13.1)

BARC Report – EBD #3.1

Ann Martin reported to the committee on the activities of the BARC committee at their fall meeting on Wednesday, October 19, 2017. Because of some overlapping topics to be covered later in the F&A meeting; only a small number of their activities were covered in this report. These included the following:

- Orientation for new committee members (2)
- Action to approve the ALA FY17 budgetary ceiling of \$66,741,279
- Action on the Spectrum Program referral from Council
 - Will notify the mover of the resolution of action and prepare a communique to Council
 - BARC strongly supports the continued efforts of expansion in the area of diversity
- ITTS Update
 - Looking to implement major portions of the IT review
 - Soft launched of Ecommerce Dues & Donations
 - Office 365 Microsoft upgrade (Fall 16)
 - Estore Project manager and Data/Business Analyst (Fall 16)
 - Migration to new ALA Connect (2/17)
 - Ecommerce store requirements being refined (launch date Spring 17)
 - New telephone system (Spring 17)
- Publishing Update on FY16 and moving forward

- Conference Services Update
 - Conference sites drive overall success
 - Working with Conference committee on options for future conferences
 - Being challenged more often by hotels on cost
- Membership (Dues) Update
 - Current dues plan tied to CPI now in year 4 of 5
 - Will work with Membership committee to plan next steps
 - New plan will need to be approved by Council at the 2018 MW meeting

F&A Orientation

The Chair welcomed the newest members of the committee (Andrew Pace and Loida Garcia-Febo) and conducted a brief overview. The session covered the following information:

- Committee Charge and Responsibilities
- Organizational Structure and Decision Making Process
- Budget and Financial Planning Calendars
- ALA Fund Structure
- The Operating Agreement and Indirect Costs
- Long-Term Investments
- APA Responsibilities

Auditor Briefing FY16 Audit Process & Introduction

John Fedus, Partner at Mueller & Co (ALA's external auditor of four years), joined the committee to provide a briefing on the status of the 2016 audit. He noted that audit planning was held for one week in late June to plan the timeline for the work to be completed during the fieldwork in November. During this time there was a review of the minutes, internal controls, the valuation processes to be used and a discussion of the discount rate to be used for the Postretirement obligation review. He also noted that in August Mueller personnel acted as an observer at BrightKey (ALA's order billing vendor) during inventory and confirmed that the testing went well. On site fieldwork is scheduled to be conducted over a three week period beginning on October 31st. Finally, plans are being made to conduct a briefing on the findings of the 2016 audit with the Treasurer during the first or second week of December. After that briefing plans will be made to present the final findings and results to F&A and the Executive Board in Atlanta at the Midwinter Meeting.

2016 Year-End Budget Review (EBD #14.1)

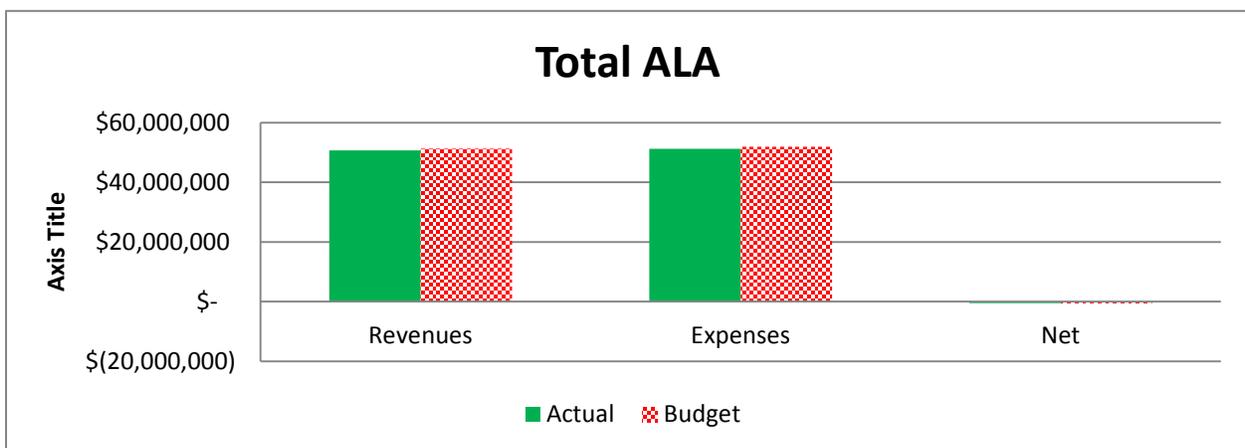
Mark Leon led the committee in a discussion of the twelve month FY 2016 year-end 3rd close results. This close information represents the most currently available information in preparation for the year-end audit. However, it was pointed out that some additional non-operating adjustments are yet to be made.

Five-Year Plan – The discussion began by directing the committee to the Association's five-year plan. It was noted that the document has become an essential planning tool for management. The document focuses on the General Fund and the revenue and expenses that can be

controlled by management. The latest version highlighted the actual third close information for FY16 and the FY17 budget approved at the Annual Conference in Orlando. Also included was a column for a revised FY17 budget which reflected necessary adjustments to the original FY17 budget driven by the results of the FY16 actuals.

Finally, it was pointed out that three additional lines of information were added to the bottom of the document to help track some important non-operating expenses. After some discussion management felt that including a non-controllable, non-operating expense item like amortization worked against the goals of the planning tool. However, the expense is still too important not to track.

ALA Operations - The following is a summary of the results for Total ALA:

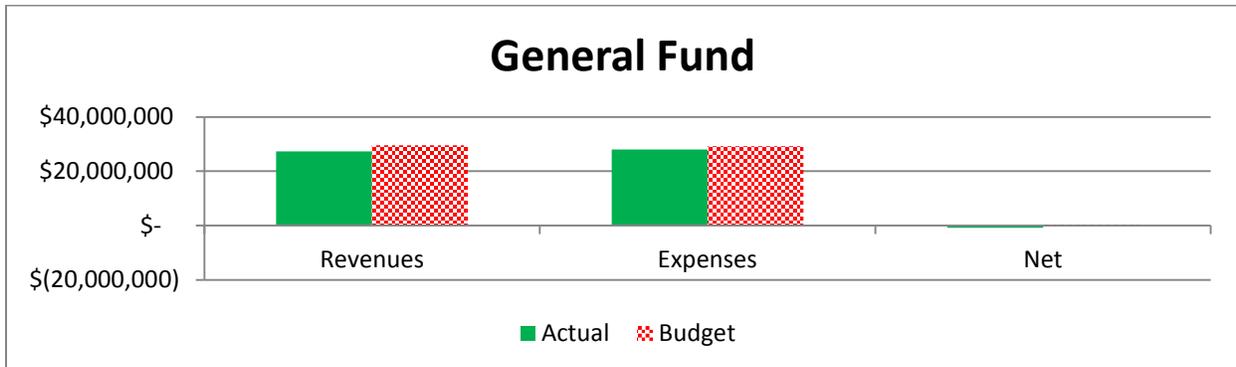


- Total ALA revenues were \$50.7 million compared to the budget of \$51.2 million;
- Actual revenues were lower than budgeted revenue in the General Fund (\$2.3 million). This was offset by higher actual revenue than budgeted in Grants & Awards (\$1.4 million), LTI (\$171,280) and Division activity (\$122,713);
- Total ALA expenses were \$51.3 million compared to the budget of \$51.9 million;
- Lower total expenses were the result of savings in the General Fund (\$1.2 million) and the Divisions (\$845,507). Expenses for Grants & Awards were higher than originally budgeted (\$1.4 million) due in part to the recent receipt of two Dollar General grants (\$549,863) and a Gates Foundation grant (\$253,802). This was completely offset by equal unbudgeted grant revenues;
- The result was net expenses of (\$566,380), which compares to the budgeted net expense of (\$655,161) for a positive net variance of \$88,781.

Referring the committee to the Statement of Financial Position, Mark Leon noted that the information being reviewed represented just a moment in time and that a number of year-end adjustments that will typically take place. He noted that total assets were \$75.7 million, a decline of \$1.9 million from the same period last year. There were reductions in most categories but primarily in lower Cash, Grants Receivable, Prepaid Expenses and Fixed Assets. These reductions were slightly offset by a gain in the value of the endowment of \$1.4 million.

Total liabilities for the period were \$43.9 million, which is a decline of \$2.2 million from the same period last year primarily in Accounts Payable and Long-Term Debt. The result was a fund balance of \$31.8 million, which is a small increase of \$225,217 (0.7%) from the same period last year. The Association’s financial position remains quite strong.

The committee was then referred to the General Fund. As noted earlier the General Fund represented the significant drag on revenue. The results are reflected below:



- General Fund revenues were \$27.3 million compared to the budget of \$29.5 million, a shortfall of \$2.3 million
- Actual revenue was lower than budgeted due to shortfalls in Publishing (\$1.2 million),-particularly ALA Editions (fewer released titles/no Editor) and Booklists (lower subscriptions), and Conference Services, particularly registration and exhibit sales revenue. Both Publishing and Conference Services did contribute to the General Fund substantially via overhead with contributions of \$3.0 million and \$2.2 million respectively.
- General Fund expenses were \$28.0 million compared to the budget of \$29.2 million for an expense savings of \$1.2 million
- The net results was net expenses of (\$745,055) compared to budgeted net revenue of \$368,856 resulting in a negative variance of (\$1.1 million)

In closing staff noted that due to the results in the General Fund, adjustments were made to the FY17 budget to better reflect more realistic revenue expectations, particularly in Publishing. Also, that both the Divisions and Roundtables have been performing quite well and met budget expectations.

FY17 Health Benefits Cost Adjustment – CBD #9 (CD BARC #27.0)

Closed Session - Dan Hoppe updated the committee on a planned adjustment to the healthcare plan offered by the Association. Due to the increasing cost related to healthcare, management over the last 12 -15 months has been reviewing and discussing its options over for controlling these costs while maintaining the current level of quality in the plans that are offered. The first

step has been taken and the impacted parties are in the process of being notified during this meeting with a scheduled opportunity to discuss the details on October 27, 2016. Details of the change and its execution will be discussed with the Executive Board in closed session.

Publishing Report (BARC #23.0)

Don Chatham updated the committee on the year-end operating results in the Publishing department, as well as, expectations for future activities. He also took the opportunity to introduce Chris Murphy the new ALA Editions Editor. He began the discussion by acknowledging that FY16 was a difficult year for the publishing operation, particularly in ALA Editions/Neal Schuman. Overall total revenues were \$11.7 million compared to a budget of \$12.9 million for a shortfall of \$1.2 million (-9.3%). Most of the shortfall was in ALA Editions (\$933,698) with revenues of \$3.8 million and Booklists (\$155,906) with revenues of \$4.9 million. ALA Editions was impacted by sales that were not realized in July and August for the Neal Schuman operations best-selling book by Rubin, as well as, the disruption in the Publisher position and the lack of a consistently applied publishing strategy. As expected sales were not realized adjustments were made on the expense side resulting in total expenses of \$10.8 million compared to a budget of \$11.5 million for a savings of \$643,459. As a result the publishing operation realized net revenue of \$881,417, which compares of a budget of \$1.4 million for a shortfall of \$550,730. Despite the shortfall, the overhead contribution to the General Fund was \$3.0 million, which was less than the budget by \$309,295.

Looking Forward – As noted earlier, as revenue expectations were not realized adjustments to the publishing operation were made in the last quarter of the fiscal year to establish a stronger foundation for future efforts. Some of the changes include the following:

- Publisher for ALA Editions is in place
- Staff Additions for FY17
- Technology Improvements for FY17
- Operational Efficiencies Planned for FY17
- Additional Neal-Schuman Textbook Releases for FY17/18
- Partnering with AASL on Standards

Challenges and Areas of Focus – As changes have been made to the general publishing operation in FY17 and beyond for better results, there are still challenges that must be addressed and given significant focus.

- Building Frontlists
- Addressing the 2 year publishing timeline
- Stabilizing the financial recording process
- Activating sales reports from the new Order Processing/fulfillment vendor

Final FY 2017 Budget Review (EBD #14.2)

Mark Leon and Brad Geene led a discussion on the Final FY17 budget highlighting the most significant changes that occurred since the Annual Conference in Orlando. It was noted that the FY17 budget was adjusted during the summer to better reflect the actual results of FY16 budget, particularly in Publishing where revenue was significantly less than budget. The budgetary ceiling approved at the Annual Conference was \$65,403,215. The changes that occurred since then were in a number of different areas but the most significant change was an increase in newly secured Grants & Awards \$1.1 million, along with a reduction in publishing revenue of (\$498,998). The Grants & Awards included Dollar General- American Dream #5 (\$314,797), PLA – Gates African Leadership Training (\$253,802), Diversity – Dollar General American Dream 2014 Supplement (\$235,066) and Development Office – Library Champions (\$146,000). As illustrated in the table, the result was an increase in the budgetary ceiling

Category	AC Orlando	Fall Meeting	(\$ change)
General Fund	\$30,120,362	\$29,587,223	(\$533,139)
Division Fund	28,349,272	28,702,106	352,834
Round Tables	2,090,736	2,210,882	120,146
Grants & Awards	4,475,827	5,393,710	917,883
Long-Term Investment	367,018	847,358	480,340
Total ALA Budgetary Ceiling =	\$65,403,215	\$66,741,279	\$1,338,064

of \$1.3 million (2.1%) to \$66,741,279. After some additional discussion the following action was taken:

Action: F&A concurs with BARC and recommends to the Executive Board approval of the final FY 2017 budget as reflected in EBD #14.2 (BARC #20.2) with a Budgetary Ceiling of \$66,741,279

Finally, it was noted that the capital budget of \$1.9 million remained unchanged from the Annual Conference.

Controller’s Report (EBD #4.3)

Joann Lee, Controller, presented the Controller’s report to the committee. A number of information pieces were covered in other sections of this report. The following represents the remaining highlights of the report:

- The Association’s Debt Service Coverage and Cash to Debt ratios were strong at 1.2 compared to 7.9 to 1.0. These ratios are required to be filed via a Compliance Certificate semi-annually with JP Morgan Chase

- The Cash and Short-Term investments balance was \$14.4 million compared to \$15.5 million last year
- The Statement of Position Working Capital was \$1.9 million compared to \$3.3 million last year. This resulted in a current ratio of 1.1 compared to 1.2 last year
- Made a \$1.0 million draw on line of credit for operations with expected repayment (3) beginning in October. Also made a withdrawal of \$1.5 million with the Working Capital account.
- Deferred revenue was \$13.5 million compared to \$12.3 million last year due to higher Grants & Awards
- Scheduled long-term debt payment of \$1.5 million made in August. The next scheduled payment (\$1.3 million) is August 2017. The current outstanding balance is \$4.5 million

Endowment Report (EBD #13.1)

Rod Hersberger updated the committee on the status of the ALA Endowment Fund for the calendar year nine months ending 9-30-16. He noted that volatility has remained on the high side as investors are being whipsawed by uncertainty from around the world.

It was noted that there were a number of factors that have impacted the market such as the following:

- Secular anti-globalization political risks rising
- Liquidity provided by central banks via negative interest rates beginning to illustrate the limits of monetary policy
- Federal Reserve likely to increase in interest rates by year-end
- Outcome of Presidential risk still uncertain
- Emerging markets, small caps and high yield bonds lead 3rd quarter returns
- Market recovering from initial outcome of Brexit vote

The current value of the portfolio at 9-30-16 was \$39.9 million for a return of (6.0%). The Trustees feel that in view of what's happening in the markets around the world, this is a reasonable return and expectations are that the year may end at or slightly above this level. During the 3rd quarter emerging markets, small cap stocks, and non-US developed country stocks outperformed, while commodities, real estate and bonds underperformed.

He concluded his remarks by discussing some of the recent work and concerns of the Trustees. The Trustees held their fall meeting in the Washington Office hosted by Emily Sheketoff and her staff. The Trustees had an opportunity to hear about the work of the office and how the positive returns from the endowment work to help enhance the resources made available to the office to advance the mission of the office. As part of the meeting the Trustees had a very good meeting with its newest portfolio manager Clearbridge ESG. The representatives were very engaging and explained in great detail the process the firm uses in making its investment decisions. It was pointed out that the firm's returns were on par with investment managers of any type, not just SRI. There was a very lively give and take between the Trustees and the

representatives, which further reinforced the Trustees' decision to hire Clearbridge. Finally, he concluded his remarks by reiterating the fact that the ALA endowment has realized most if not all of its growth over the years via investment gains i.e. no formal fund raising campaign or program.

Director of Financial Reporting and Compliance Report (EBD #4.3)

Denise Moritz, Director of Compliance and Financial Reporting, presented the Director's report to the committee. Highlights of the report reflected the following:

- Form 5500 for ALA's Employee Benefit Plans filed with the Department of Labor and form 8955-SSA with the Department of Labor and the IRS
- Impairment testing planning meetings held in September/October with Publishing and Finance to update Neal-Schuman business plan, which was sent to Plante Moran – ALA's valuation expert – and ALA's auditor Mueller & Co in September to discuss the timeline for valuation work and assumptions. A draft report will be delivered during the week of October 31st. Preliminary indications are that there will be *no expectation of a write down on the Neal-Schuman Goodwill*
- Discussions with Mueller & Co and ALA's actuary resulted in a discount rate of 4.5%, which will be used to calculate the post-retirement benefit obligation. This is a decrease from FY15 and is expected to increase the Postretirement liability by \$2.0 - \$2.5 million.
- All Federal and state 990/990T/AG990-IL/PC forms have been filed with the appropriate entities
- Received the final audited financial statements for the Association's retirement plan and the following action was taken:

Action: F&A Recommends to the Executive Board acceptance of the 12-31-15 403 (b) audit as highlighted in EBD #4.3.

Acknowledgements

We continue to be well served by Mark Leon, Keith Michael Fiels, Mary Ghikas, Joanne Lee, Brad Geene, Keith Brown, Denise Moritz and Latasha Bryant. They have been very dependable, innovative, reliable and thorough in assisting in our financial oversight responsibilities.

Respectfully submitted:

Susan Hildreth, Treasurer and Chair
Loida Garcia-Febo
Peter Hepburn
Andrew Pace
Ann Martin, BARC Chair