

**American Library Association
2010 Midwinter Meeting
Finance and Audit Committee
Report to the Executive Board
Tuesday, January 19, 2010**

It is my pleasure to report to the Executive Board on the activities of the Finance and Audit Committee (F&A) at this Midwinter Meeting. Below are some topics F&A discussed:

- Proposed Presidential Initiatives Budget – BARC #15 (EBD #3.4)
- FY 2009 Budget Update
- FY 2010 1st Quarter Budget Update – BARC #5.4 (EBD #3.3)
- Membership & Dues Update
- FY 2011 Budget Guidelines – BARC Info #5
- Endowment Trustees Report – EBD #13.1
- Indirect Cost Study Assumptions – EBD Info #1
- FY 2009 Audit Report – EBD #4.5
- Controller’s Report – EBD #4.7

On Friday morning, January 15, the Finance and Audit Committee of the Executive Board met jointly with BARC. F&A then met separately on January 16 and 18.

Proposed Presidential Initiatives Budget – BARC #15 (EBD #3.4)

BARC and F&A reviewed the presidential initiatives proposed by President-Elect Roberta Stevens. In addition to building on the work of previous Presidential office holders, this budget will be focused in three areas:

1. “Frontline Fundraising” In response to the nationwide reduction in resources at libraries - \$22,500
2. “Our Authors, Our Advocates” Using well known authors as advocates to highlight the key role of libraries - \$40,000
3. “Why I Need My Library” Utilizing the energy and exuberance of young people to advocate for libraries via a contest - \$37,500

ACTION:

It was moved and passed that BARC and Finance and Audit approved the proposed presidential budget, 2010-2011.

FY 2009 Budget Update

BARC reviewed the final FY 2009 results. The Consolidated Summary of Operations indicates net revenues of \$683,102, a year-to-year decline in net assets largely explained by the financing of the new CHOICE building and General Fund net revenues of \$213,296. ALA had put in place a budget reduction plan of \$1,624,000, anticipating significant erosion in revenues. This included one-time expense adjustments, operating expense reductions including a staff furlough (\$250,000), and the use of Board reserves (\$436,000). The net revenue result of a positive \$213,296 was achieved without use of Board reserves, and is net of a one-time organizational incentive for staff totaling (\$250,000).

FY 2010 1st Quarter Budget Update – BARC #5.4 (EBD #3.3)

BARC reviewed the first quarter FY 2010 budget report and noted the following highlights: Total ALA (all combined funds) revenue of \$11,057,169 is \$665,477 (6%) more than budget. The General Fund revenue of \$4,743,990 is \$283,029 (-6%) less than budget. Shortfalls are mainly in Publishing, primarily in Products & Promotions (\$168,146) due to the impact from the slow economy on library spending. Subscription and advertising are also being impacted. Division revenues of \$4,146,086 are more than budget by \$1,433,780 due to early recognition of the AASL national conference revenues. Grants and Awards revenues were \$1,902,743 which is \$540,057 less than budget due to timing. Investment interest and dividends are more than budget by \$61,811 (46%) or \$195,953.

Total ALA expenses of \$11,444,480 are \$1,159,131 (9%) less than budget. The General Fund expenses of \$5,802,008 are \$729,049 (11%) less than budget. The General Fund expense budget has been reduced by 3% due to expected revenue shortfalls. Division expenses are \$164,838 (-5%) more than budget at \$3,660,462. Grants and Awards are \$1,902,743 (22%) less than budget due primarily to timing.

On the plus side it was noted that the General Fund will be realizing savings in a couple of areas. Human Resources recently renegotiated the Association's life and disability coverage, which will result in savings of \$108,000. Additionally, another \$28,000 in savings will be realized by pooling the state unemployment compensation with other organizations.

Total assets for the period are \$69,209,767 and are \$8,549,092 (14%) more than the same time last year as a result of increases in property, plant & equipment, inventories and long-term investments. This increase was offset by a decline in cash and short-term investments to \$18,456,744 as compared to \$19,253,041 last year due to lower deferred revenues and higher property, plant and equipment purchases. The Long-Term Investment Fund totals \$29,032,554 as compared to the \$22,617,368 balance at November 2008. As a result, net assets increased by \$3,311,543 or (14%) more than November last year totaling \$27,418,321.

As a continuation of the update on the FY10 budget update, the discussion shifted to revenue and expense expectations for the remainder of the year and beyond. Management has been proactive in examining the economic landscape and its potential impact on ALA. At this point in time

management is anticipating a budget shortfall of \$1.1 million. The anticipated shortfall is broken down as follows:

Publishing (contribution margin)	(\$ 250,000)
Conferences (contribution margin)	(\$ 500,000)
Dues Reduction	(\$ 220,000)
Benefits Increase	<u>(\$ 90,000)</u>
Total	(\$1,060,000)

Note: Contribution margin is revenue minus expense not including overhead.

In order to address the projected revenue shortfall, a preliminary contingency plan has been discussed. The projected shortfall will be offset by expense reductions in the following areas:

Unallocated Fund	\$ 250,000
Staff Furlough	\$ 260,000
General Fund Unit Expenses	\$ 250,000
Use of Reserves	<u>\$ 300,000</u>
Total	\$1,060,000

At this point these proposed actions will be taken under advisement. Sometime after this Midwinter Meeting – March/April – a more definitive decision will be made on the proposed reductions as ALA’s financial results become much clearer. Whether or not to implement a staff furlough will be based on financial data available at the spring meeting.

The committee also took the opportunity to look beyond FY 2010. ALA is faced with the recurring issue of only one national division conference in FY 2011. This will potentially have a budgetary impact of approximately \$600,000. The fact that libraries across the country will be negatively impacted by the poor economy for at least 18 – 24 months is a major concern. The negative budgetary impact to ALA is likely to be felt in conference attendance, membership, publishing, and products and services in FY 2012.

Membership and Dues Update

Cathleen Bourdon and John Chrastka joined F&A and BARC to update the committees on some membership information. They reported that the December figures were about where they were expected to be at 3% under budget. It was noted that personal membership was over budget by 2%.

Despite recent economic conditions, decisions by ALA personal members to renew or join ALA are not significantly at variance from either 7, 5, or 3-year averages of activity. During an average fiscal year, membership volume follows a well established pattern wherein the months of November, December and January account for 35% of transactions and the remaining months

are realized at a smoother rate. This pattern appears to be continuing during this fiscal year, ensuring predictability of dues income.

Looking forward to the next several years, key indicators of the stability of this revenue stream include any material changes to the pattern of renewals, the impact of retirements around the profession and rate of replacement in those positions, as well as the ratios of members by type within the Association. As the 2010 dues increase phase-in has been fully realized, attention to our average dollar per member will also be an early actionable indicator.

For Organizational Membership, we are in the first quarter of a two-year dues increase. It is too early to assess the impact of the dues on renewal and recruitment patterns. More information will be available in the spring.

Corporate membership patterns have stabilized after a recent dues increase. Stronger booth sales for Boston and anticipations for Annual will provide year-to-year consistency in this revenue line.

FY 2011 Budget Guidelines – BARC Info #5

BARC reviewed the budget planning strategies for FY 2011 and the guidelines provided to ALA unit managers. Several key elements were noted:

- This is the first year of the implementation of the ALA 2015 strategic plan
- The FY 2011 budget is being prepared on the analysis of the actual FY09 results
- The FY 2011 budget is being prepared with a zero percent increase over the FY 2010 approved budget, including the carry forward of a 3 percent reduction in the FY 2010 budget
- There will be no adjustment for staff compensation nor staff additions
- Endowment transfers will be deferred
- Contingency plans for managing expenses in the face of declines of revenue in FY 2010 and FY 2011 are being put in place with a priority assigned to the sustenance of member services.

As the discussion continued, it was noted that BARC took an action earlier to amend the budget instructions to eliminate the possibility of making any net asset transfers to the endowment. The action was a direct result of a management recommendation after a review of the impact on the Associations cash flow. As a result of the CHOICE property purchase, investments in Publishing and lower than expected revenue growth in Publishing and Conferences, the impact on cash was clear. BARC has the responsibility of monitoring the current budget and reviewing the proposed budget instructions. As such, some critical decisions must be made quickly. BARC however recognizes the importance of communicating such decisions to all impacted parties.

Endowment Trustees Report - EBD #13.1

Dan Bradbury joined the committee to report on the performance of the ALA Endowment Fund. For the calendar year ending 12-31-09 the endowment fund realized a return of 23.8% compared to its benchmark of 20.7%. The fund grew by \$5.3 million to \$28.7 million. It was indicated that this is extraordinary performance in view of how poorly the market performed during the first quarter of the year. All of the managers reported positive gains, with the largest coming from Alliance - Large Cap Core (\$1.3 million) and Pimco – Fixed Income (\$1.1 million). This led to a discussion on the impact of active management compared to passive management. Over the last six years the portfolio has generated \$6.6 million. This compares to \$5.0 million from passive management, which means that the portfolio generated an additional \$1.6 million to the benefit of the Association.

It was noted that there were a number of strategic and tactical changes to the portfolio since Annual Conference. The former large cap value manager – Blackrock – and large cap international manager – Lazard – were replaced IDP portfolios. IDP portfolios are in essence manager of manager portfolios that offer more diversity and lower risk. During this period the Trustees also made the decision to overweight large cap value and reduce large cap growth. Finally, the Trustees also took the opportunity to invest \$2.0 million in the hedge fund “The Endowment Fund.” The Endowment Fund is a hedge fund of funds that is registered with the SEC. It was noted that the Trustees performed a good deal of due diligence and proceeded with caution as they moved into this arena. Additionally, the finance staff supplemented the work of the Trustees by working with ALA’s auditor to determine and establish clear guidelines for monitoring the activities and a methodology for valuing the hedge funds. Also under review with the Investment Advisor – Merrill Lynch – is new language for the investment policy that will spell out the monitoring practices.

Indirect Cost Study Assumptions - EBD Info #1

The committee reviewed with staff the indirect cost study assumptions to be used in the 2009 study. The study will be conducted in the same manner as the 2008 study. The most significant issue for this study, as compared to last year, is how equitably to apply the composite rate to the new ALTAFF division. As a result of operations in Chicago and Philadelphia, the full rate would not seem to apply. As such, some discount will likely be negotiated. The document goes on to summarize the sources of the information used in the study i.e. 2009 Audit report and internal performance reports etc., the allocation methods to be used and timeline. The results of the study will be summarized and presented for review at the spring meeting.

FY 2009 Audit Report – EBD #4.5

Frank Jakosz, Partner and John Fedus, Manager of Grant Thornton presented the audit results related to the fiscal year 2009. They highlighted the impact of four major new additions to the audit which required significantly detailed footnote additions to the audit report that are as important as the required schedules. ALA received an unqualified opinion and that the financial

statements fairly represent in all material respects the financial position of the American Library Association.

ACTION:

F&A recommends to the Executive Board acceptance of the FY 2009 Audit as presented by Grant Thornton.

Controller's Report – EBD #4.7

R. Swedowski was present to highlight his report for the committee.

Inventory Levels - Inventory levels at November 30, 2009 were ALA Editions at \$762,125, and Products and Promotions (Graphics) at \$665,370. The ALA Editions inventory reflects a \$34,000 valuation for Guide to Reference Books, 11th Edition. The largest item in the inventory for Products and Promotions was \$112,000 for Read products.

The excess and obsolete inventory reserves for ALA Editions and Products and Promotions are \$293,000 and \$159,000 respectively. During the year Graphics and ALA Editions destroyed \$15,821 and \$10,039 of excess or obsolete products. All destroyed product were charged against their respective inventory reserves for excess and obsolete products. In FY 2010, Graphics has destroyed \$46,870 to date.

Credit and Collections - Trade accounts receivable were \$2,083,497 as compared to \$1,946,243 at November 30, 2008. The 150+ day aging bucket at November 30, 2009 contained \$186,292 of receivables as compared to \$235,439 at November 30, 2008. The decrease is a result of various Midwinter exhibitor billings that are outstanding; the billings were done one month earlier in 2009 as compared to 2008.

Unrelated Business Income Tax (UBIT) - The preparation of the final UBIT worksheets and the actual tax returns will commence in February, with a target completion date of early April. The proper extensions have been filed to extend the January 15th due date to April 15th and June 15th for the 990T. Estimated payments for FY 2009 were made in a timely manner. There is no expected tax liability for the Federal or the state of Illinois returns. The final close of 2009 included additional revenues and expenses that were not in the close used to compute the provision. As a result, the actual tax liability may be slightly higher than the provision.

The new version of the Form 990 will be used in the preparation of the 2008-2009 filing. Significant operational impacts are expected. Specific changes include an 11 page core form and a series of 16 supplemental schedules. In addition, there are expanded questions on governance and executive compensation, as well as key areas of financial data. The preparation of the new Form 990 will likely result in the participation of staff other than just the Finance staff. As a result, an extension to file this return by July 15, 2010 will be submitted.

Cash Management and Bond Fund- Total cash and short-term investments at November 30, 2009 amounted to \$18,456,744 as compared to \$19,253,041 a year ago. The decrease is due to lower deferred revenues for subscriptions and meetings/conferences and an increase in property, plant and equipment and inventories. Year-to-date interest income is \$243,911, which is \$58,926 more than the budget of \$184,985 and \$21,886 more than last year.

The Neuberger Berman bond fund investment balance is \$15,099,214 at November 30, 2009 as compared to \$14,837,288 at November 30, 2008. The increase reflects an improved market since there were no additions/withdrawals to the investment. As noted in schedule 6, this investment has produced over \$8,005,000 in interest income since December, 1991 and the yield has been well above the yield from certificates of deposit. With regard to risk of principal, the account finished FY 2009 with a realized/unrealized gain of \$382,050 and is currently reflecting a net gain of \$135,878 for FY 2010. At November 30, 2009 the cumulative (computed since December, 1991) net realized/unrealized gain is \$231,050.

ALA Financial System Replacement - The finance department is in the process of evaluating its current financial system with the expressed purpose of finding a replacement. The finance staff and an outside consultant have prepared a preliminary timeline for the development of a needs assessment, RFP development and vendor selection. The new system will include a process review to improve the month-end and year-end close process and augment the grant implementation process and endowment accounting process to comply with accounting standards by utilizing available technology.

Acknowledgements

We continue to be well served by Greg Calloway, Keith Brown, Sandra Lee, Russ Swedowski and Elaine Klimek of the ALA financial staff. They have been very dependable, reliable and thorough in assisting in our financial oversight responsibilities.

Respectfully submitted:

Rod Hersberger, Chair
Em Claire Knowles
Jim Neal, BARC Chair
Larry Romans
Steve Matthews