June 22, 2022

To: Members of the Columbia Association Board of Directors

From: Susan Krabbe, Senior Vice President/Chief Financial Officer

Cc: Lakey Boyd, President/CEO
Dennis Mattey, Vice President, Community Operations
Jackie Tuma, Director of Audit and Advisory Services

Subject: Response to June 16, 2022 Letter from Town Center Community Association on Villages' FY22 Excess Cash Reserves

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In his June 16, 2022 letter (attached) to Eric Greenberg, Chair of the CA Board of Directors, Lyn Locke, Village Manager and Executive Director of Town Center Community Association (TCCA), requested two amendments to CA staff's recommendations related to the FY22 excess cash reserves calculation. CA staff presented their recommendations to the CA Board and community at the June 9, 2022 work session. That information is also attached to this memo.

1. "**Include FY2019 expenses** when calculating the expenses average as requested by all villages. FY2019 is the most recent 'pre-COVID' year that had normalized expenses and we would like those added to FY2020 and FY2022. The three-year average will give a fair depiction of village expenses as FY2019 was close to normal and FY2020 and FY2022 had periods where business expenses were returning to a 'modified normal pattern.' We agree that FY2021 should be excluded as several State and County Emergency Orders were in place and occupancy restrictions were placed on facility rentals which resulted in an anomaly year for both revenues and expenses."

   To be clear, FY 2020 was the fiscal year in which the State-mandated shutdown was in effect for CA and the villages from mid-March 2020 for the last six weeks of that fiscal year and well beyond, not a period of "returning to 'a modified normal pattern.'"

   As stated previously, CA staff believes that FY 2019, completely pre-COVID, is an unrealistic, irrelevant and misleading predictor for cash needs, because it reflects operating conditions that no longer exist for the villages or for CA. We do not recommend that FY 2019 be part of this calculation for this reason. If the CA Board chooses to include FY 2019, then staff recommends FY 2021 also be included for a more balanced picture of current operating conditions.

2. **"Exclude FY21 excess charge share for all Villages of $291,000 paid to all villages in a proportionate amount in April 2021.** Receiving the cash late in FY2021 did not allow for enough time for planning to use the cash due to supply chain disruptions during FY2022, significant labor market disruptions and the ability to hire staff, and dealing with significant cancellation and event changes due to the pandemic."

   It is now over a year since the additional FY 2021 annual charge share grant funds were distributed to the villages. First it should be noted that these funds are annual charge share funds for village *operations. If they are not needed for operations and are beyond the already expanded excess cash reserves amounts, then they should be returned to CA. Perhaps more importantly, given the more than 12 months that have elapsed since the funds were distributed, these funds may have already been spent and therefore already included in the operating expense component of the calculation. To exclude from the excess cash reserves calculation amounts that might no longer exist is not appropriate. CA staff recommends that the FY 2022 annual charge share grant increase be excluded, but not the FY 2021 increase.*

The June 16 letter from TCCA includes a quote attributed to multiple non-profit advocacy group sources recommending that nonprofits should reserve at least 3-6 months of operating expenses; ideally up to 2 years' worth of operating expenses. In our opinion, it is not accurate to view this statement in isolation; non-profit guidance and best practices are clear that the appropriate amount of reserves depends upon various factors, such as the nature of funding sources and risk of unanticipated expenses. The statement does not quantify the actual risks that would be mitigated by such a significant reserve, and does not reflect current best practices based on our research in developing CA's Emergency Cash Reserves Policy approved by the CA Board in FY 2021. Using solely a factor of a number of months of expenses may not reflect the actual risks that village operations face, which is one of the reasons that CA staff did not propose using that basis for CA's Emergency Cash Reserves Policy. If that is the context, then CA's current Emergency Cash Reserves funding of $5,133,000 would provide a reserve that is not even one month of CA's budgeted FY 2023 operating expenses, and CA's risk profile is clearly much higher than that of the villages.

The management contract between CA and the villages already provides for a "rainy day fund." The excess cash reserves threshold is currently 20% of operating expenses, plus previously CA Board-approved exceptions to the calculation, such as the contingency fund distributions. This is then compared to cash on hand *excluding* funds needed to meet existing liabilities.

The villages' cash balances, their risk profiles and the submitted FY 2022 financial reports do not reflect a need for cash above the levels enabled by the CA staff-proposed calculations. CA staff does not support the amendments requested by TCCA.

COLUMBIA TOWN CENTER

www.columbiatowncenter.org
ph: 410.730.4744

June 16, 2022

Eric Greenberg
Chairman
Columbia Association Board of Directors
6310 Hillside Court, #100
Columbia, MD 21044

RE: Villages' FY22 Excess Cash Reserves

Dear Mr. Greenberg,

The Village Managers shared with Columbia Association (CA) staff a letter on February 17, 2022, regarding the calculation of "excess cash" for FY2022. We outlined the exclusions that we felt were necessary given the disruption to village operations because of the COVID pandemic. We appreciate that the Columbia Association staff reviewed our request and that Susan Krabbe, CA CFO, prepared a proposal for the CA Board to consider.

On June 9, 2022, Susan Krabbe presented the Columbia Association staff recommendation for handling FY2022 Excess Cash Reserves for all villages at the CA Board Work Session (see attached). In the proposal Ms. Krabbe outlined areas of exclusions to calculate the cash reserves including the following:

1. Modifying the expense formula using an average of FY20 and FY22 expenses
2. Excluding CARES Act distributions and grants and tax credits
3. Excluding the end of year FY22 excess charge share cash payment to all villages that was paid the last week of the fiscal year ($356,000 total across ten villages).

We agree with Ms. Krabbe's recommendation; however, we have ***one inclusion*** that we would like you to consider as well as ***one exclusion*** to add to the proposed recommendation. These amendment/changes are outlined below.

Amendments Requested

We respectfully ask that the following amendments/changes be added to the Columbia Association proposal when calculating the FY22 Excess Cash Reserves Formula:

- **Include FY2019 expenses** when calculating the expenses average as requested by all villages. FY2019 is the most recent "pre-COVID" year that had normalized expenses and we would like those added to FY 2020 and FY2022. The three-year average will give a fair depiction of village expenses as FY2019 was close to normal and FY2020 and FY2022 had periods where business expenses were returning to a "modified normal pattern." We agree that FY2021 should be excluded as several State and County Emergency Orders were in place and occupancy restrictions were placed on facility rentals which resulted in an anomaly year for both revenues and expenses.

- **Exclude FY21 excess charge share for all Villages of $291,000 paid to all villages in a proportionate amount in April 2021.** Receiving the cash late in FY2021 did not allow for enough time for planning to use the cash due to supply chain disruptions during FY2022, significant labor market disruptions and the ability to hire staff and, dealing with significant cancellation and event changes due to the pandemic.

Justification for Requests

The COVID pandemic continues in FY2023 although the nature of the pandemic has changed and we are no longer under mandatory State and County masking orders, occupancy orders and/or in a shutdown situation. However, the possibility of another business disruption exists, and we feel that additional reserves are needed to protect ongoing operations through creation of a "rainy day fund."

Last Fiscal Year 2022 was still an anomaly year in revenues and expenses and the above recommended amendments will help Villages to do the following:

- To fulfill the Villages Board of Director's fiduciary responsibility to maintain community operations in Town Center for TCCA and provide direction to the Village Manager/Executive Director as to the resources available to manage significant emergency situations with the oversight and direction of the TCCA Board of Directors.
- To maintain Village staffing levels and day-to-day operations to the extent possible and feasible in the event of catastrophic, significant, or unforeseen events that result in negative impacts to revenue either in the short- or long-term. As with the Columbia Association policy, the reserves are "not intended to replace a permanent loss of revenue or subsidize an ongoing budget gap."
- To instill confidence across vendors, clients, community residents and others that use the services of both TCCA as well as Historic Oakland that TCCA can maintain itself as a viable operation despite catastrophic events, e.g., the COVID-19 pandemic that fully shut down the operation from March 2020 to July 2020 and curtailed the operation for another twelve months thereafter.

The National Council of Non-Profits, Maryland Nonprofits, Inc., and other advocacy groups suggest that:

> "As a general rule of thumb, nonprofits should set aside at least 3-6 months of operating costs and keep the funds in reserve. Ideally, nonprofits should have up to 2 years' worth of operating expenses in the bank."

The Town Center Community Association adopted a new *Contingency Fund & Emergency Cash Reserves Policy* in December 2021 modeled after CA's policy to exercise appropriate stewardship over community resources. Other Villages have similar policies.

Thank you for reviewing this matter and considering the amendments.

Sincerely,

Lyn Locke
Village Manager, Town Center &
Executive Director, Columbia Town Center Residential Community Association

CC: TCCA Board of Directors
Lakey Boyd, Columbia Association, President/CEO
Susan Krabbe, Columbia Association, Senior Vice President/Chief Financial Officer

June 3, 2022

To: Members of the Columbia Association Board of Directors

From: Susan Krabbe, Senior Vice President/Chief Financial Officer

Cc: Lakey Boyd, President/CEO
Dennis Mattey, Vice President, Community Operations
Jackie Tuma, Director of Audit and Advisory Services

Subject: Villages' FY22 Excess Cash Reserves

Background

CA has a longstanding practice of allocating a portion of the CA annual charge to the ten village community associations ("villages"). While it is sometimes referenced as "pass through," it is not. It is actually the responsibility and right of CA to assess, bill and collect the annual charge in its entirety. The share of the annual charge paid by CA to the villages is required to be reported to the IRS by all parties as a grant. This distinction is important because it reflects the fiduciary responsibilities that both CA and the villages have for oversight of the funds collected from annual charge payers. The alternative to this practice would be for each village to collect its own fees and assessments in accordance with its individual governing documents.

In addition to the annual charge share, CA provides a substantial amount of additional support such as employee benefits, legal (covenant) fees, repairs and maintenance, depreciation, insurance, taxes, interest, and administrative support. In FY22, this totaled approximately $6.4 million:

Annual charge share	$	3,427,500
Other funding/support	$	2,989,000
Total - FY22	**$**	**6,416,500**

NOTE: CA also provides a wide variety of in-kind support (e.g., rent-free use of the 24 community buildings, event support, snow/trash removal), the value of which is not included above.

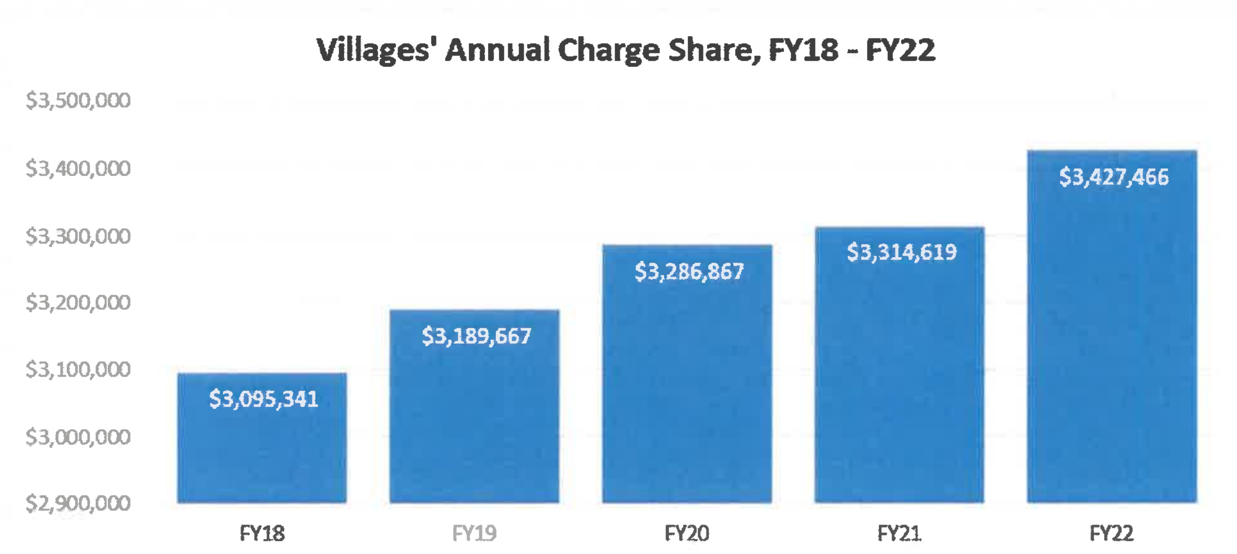
The current funding structure was developed through a joint effort between CA staff and village managers and then approved by CA's Board of Directors in FY18. The methodology is designed to fund the villages' mission-related functions and also defray some of the costs associated with occupying CA buildings.

The management contract between CA and each village specifies the amount of cash reserves that can be retained by each village (currently 20% of operating expenses), with any excess beyond that threshold returned to CA. This enables the villages to receive funds needed for operations while retaining reserves for unexpected expenditures. Any excess returned to CA supports the "other funding/support" noted above and other community-wide activities and projects, such as free community events throughout Columbia, outdoor pools and CA-wide open space maintenance.

In FY19, a contingency fund (excess cash returned to CA but held for the villages' use in case of significant unusual or unexpected needs) was dissolved due to a lack of use, with CA Board approval. Half of that fund, a total of $304,000, was distributed to the villages, becoming an additional layer of cash reserves as another exclusion to the excess cash reserves calculation.

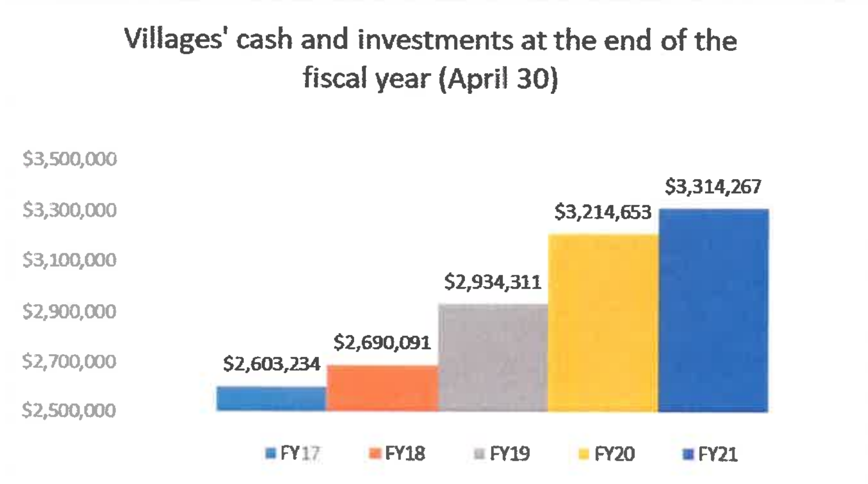
Modifications due to COVID

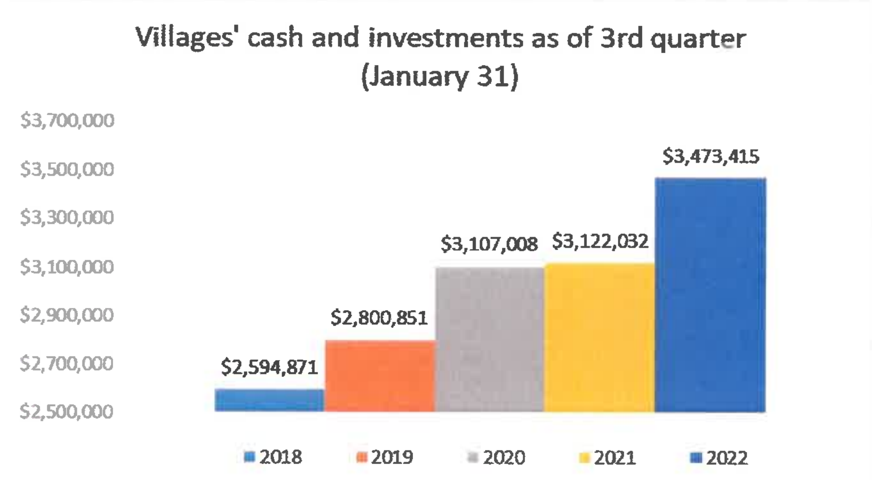
Because of the impact of the pandemic on CA and the villages, the annual charge share amounts for FY21 and FY22 were initially reduced with many other components of CA's budget, due to both realized and expected pandemic impacts, as compared to pre-pandemic years. However, once it was determined that CA's annual charge revenue was not negatively impacted, additional funding more in line with the annual increases pre-COVID was granted to the villages for both FY21 and FY22. A five-year history follows.



Recognizing that the villages were concerned about the impact of the pandemic on operations, CA's Board of Directors also approved modifications to the excess cash reserves requirements in FY21 and FY22.

While the villages experienced a significant decrease in lease and rental revenue, operating expenditures were also lower, yet the annual charge share from CA remained largely at pre-pandemic levels. Some villages also obtained CARES grants and/or loans. As a result, villages' cash and investments have actually increased since FY19 (pre-pandemic).





Note: Certain cash and investment balances are adjusted for comparability due to timing of the quarterly distributions.

Recommendation for FY22 excess cash reserves

As all of our organizations pivot to a new normal, CA's commitment to the villages remains clear. It is also incumbent upon both CA and the villages to exercise good stewardship of the annual charge share, including being able to justify expenditures and the need/extent of cash reserves.

The village managers sent CA a memo in February 2022 requesting several modifications to the FY22 excess cash reserves (see attached). Based on financial data, trends, and the structure in place to enable the villages to retain a healthy and sufficient amount of cash reserves, staff recommends that any excess cash for FY22 be returned to CA, with four exceptions:

1. Use an average of FY20 and FY22 operating expenses (excluding depreciation) to calculate the 20% operating reserve. The request from the village managers was to use an average of FY19, FY20 and FY22. CA staff agrees that FY21 should be excluded, because it was a fully COVID year and

therefore an unrealistic predictor of cash needs. However, FY19, as a fully pre-COVID year, is also an unrealistic predictor for cash needs and should also be excluded.

2. Exclude grants, tax credits and CARES Act distributions received in FY22 from the FY22 excess cash reserves calculation. To be clear, all unpaid loans are already excluded from the excess cash reserves calculation. These grants, tax credits and other government distributions were intended to address immediate, urgent needs created by the pandemic at that time of distribution. Thus, we recommend and agree that any such grants, tax credits and CARES Act loan proceeds or distributions received in FY22 should be excluded from the FY22 excess cash reserves calculation.

3. Exclude the FY22 annual charge share grant increase ($356,000 in total) from the excess cash reserves calculation. This increase of 10.7% over the final actual FY21 annual charge share grant amount brings the amount more in line with pre-COVID years. Since this is being distributed at the end of the fiscal year, we recommend this amount be excluded from the FY22 excess cash reserves calculation. Note: This was not part of the village managers' request; they submitted their request before this additional distribution was determined and communicated. CA staff is recommending that this amount be excluded for FY22.

4. CA will invest any excess funds in the village from which it came with a focus on promoting environmental projects. This was not part of the village managers' request. CA staff is making this recommendation, identical to the motion passed by the CA Board in July 2021 to support further community priorities around environmental stewardship and sustainability.

As a result of exceptions approved last year and the generally favorable impact of the pandemic on villages' cash balances, the second chart on page 3 demonstrates that the overall amount of cash and investments for which the village community associations are responsible has increased almost 34% since FY18. If such policies are not already in place, CA staff strongly urges the village community associations to develop cash reserves policies and investment policies based on best practices and their organization's risk profile and cash needs, so that there are clear, up-to-date guidelines for the responsible stewardship of these community resources.

Kings Contrivance Community Association

Amherst House 7251 Eden Brook Drive, Columbia, Maryland 21046

(410) 381-9600 Kings@VillageOfKC.org

February 17, 2022

Dear Susan and Jackie,

FY22 has continued to be an anomaly year with the continued disruption of village operations due to the Covid pandemic.
The village managers discussed this at length, and request that the CA Board pass a similar resolution for FY22 to the one passed for FY21 for the excess cash reserve calculation:

1. Use an average of the FY19, FY20 and FY22 expenses to calculate excess cash reserves in light of the fact that just like FY21, FY22 continues to be an unusual year for village expenses.
2. Exclude in the FY22 Cash Reserves calculation any grants, loans, tax credits or CARES ACT distributions to the villages.

Thank you for your consideration and presenting this to the CA Board as soon as possible.

Sincerely,

Village Managers
Dorsey's Search Community Association
Harper's Choice Community Association
Hickory Ridge Community Association
Kings Contrivance Community Association
Long Reach Community Association
Oakland Mills Community Association
Owen Brown Community Association
River Hill Community Association
Town Center Community Association
Wilde Lake Community Association