

SECTION: **POLICY STATEMENT - GENERAL AND ADMINISTRATIVE**SUBJECT: **NET ASSETS RESERVE POLICY**

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**PURPOSE:** To set forth the general policy and criteria for establishing net asset reserves to ensure continued fiscal viability of operations.

**EFFECTIVE DATE:** **September 10, 2004**

**HISTORICAL:** December 8, 2000

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**NET ASSETS RESERVE POLICY****I. BACKGROUND AND PURPOSE****A. California State University Policy**

The Chancellor of the California State University, on March 6, 2000, issued the Compilation of Policies and Procedures Pertaining to California State University Auxiliary Organizations – Executive Order No. 732, and directed that the Campus Presidents implement these policies.

On the subject of financial standards this policy states: Annually each auxiliary governing board shall review the fiscal viability of the auxiliary organization to include:

1. A review of the management functions to ensure provisions for adequate professional management (ref: Ed. Code, 89904[b]).
2. An evaluation of the need for reserves in the following areas:
  - a. Working Capital
  - b. Current Operations
  - c. Capital Replacement
  - d. Planned future operations (including future new business requirements which have been recognized by the campus and the auxiliary organization as appropriate and within the educational mission of the campus)
3. The establishment or revision of reserves and their funding levels in accordance with the above evaluations.
4. The submission of a report annually to the President which includes a plan to build and maintain appropriate reserves

**B. Accounting Profession Requirements**

In June 1993, the Financial Accounting Standards Board (FASB) issued Statement of

Financial Accounting Standards (FAS) No. 117, *Financial Statements of Not-for-Profit Organizations*. Implementing this standard changed the reporting requirements of not-for-profit organizations. Generally, fund balances become Net Assets. Net assets are used to describe the residual amount remaining after liabilities are subtracted from assets and are split into three categories: unrestricted, temporarily restricted, or permanently restricted.

### **C. Operating Agreement Requirements**

The operating agreement between the University and the Cal Poly Corporation (“CPC”) (required for the performance of functions by the CPC) contains the following section on the disposition of net earnings:

Auxiliary agrees to comply with Trustees policy on expenditure of funds including but not limited to Trustee guidelines for disposition of revenues in excess of expenses, and with Board of Trustee policies on maintaining appropriate reserves.

The first priority for use of net earnings is the payment of obligations incurred through CPC functions. The second priority is the funding of equipment and maintenance reserves and working capital in such amounts as shall be deemed necessary for the effective operation of the functions.

The disposition of net earnings, determined to be in excess of the needs stated above, will be based on the approved plan to build and maintain reserves as stated in Section I (A)(4) above.

## **II. POLICY AND PRACTICES**

### **A. Terms and Definitions**

#### **1. Sources of Funds**

The CPC receives its operating capital from the following sources:

- a. Net earnings from commercial operations.
- b. Grants/Contracts indirect cost recovery.
- c. Fees for administering campus program accounts.
- d. Gifts.
- e. Investment income.

#### **2. Applications of Funds**

The funds received from the above sources are utilized for the following purposes:

- a. Invested in operational assets.
- b. Invested in Plant and fixed assets.
- c. Interfund/Intrafund loans.
- d. Held for restricted purposes.
- e. Designated for specific needs.

### 3. Net Assets

- a. "Net Assets" is the term used to represent the residual amount remaining after liabilities are subtracted from assets. Typically, net assets are derived from net earnings; however an asset transferred from another organization adds value to both assets and net assets without creating a liability or net earnings. FAS No. 117 requires net assets to be segregated into three categories; unrestricted, temporarily restricted, and permanently restricted.
  1. Unrestricted – The part of net assets that is earned from commercial operations, fees, and investment earnings.
  2. Temporarily Restricted – The part of the net assets resulting from contributions and other inflows of assets whose use by the organization is limited by donor-imposed restriction that either expires by the passage of time or is used up or expend as specified.
  3. Permanently Restricted – The part of the net assets resulting from contributions of assets whose use by the organization is limited by donor-imposed stipulations that neither expires by passage of time nor can be fulfilled or otherwise removed by actions of the organization.
- b. For internal reporting purposes, the CPC augmented the FAS No. 117 net asset categories to include more definitive classifications. The added classes identify the specific purpose or program the net asset supports. The net assets classifications are:
  1. Unrestricted Net Assets
    - a. Operating – Provides unrestricted working capital.
    - b. Contingency – Established for an event that may occur, but is not likely or intended.
    - c. Program - Designated by the Board of Directors or Executive Director to fund current or future events and special programs.
    - d. Capital Replacement – Available for renewal and replacement of plant and/or equipment.
    - e. Investment in Operating Assets – Amount invested in net operating assets.
  2. Temporarily Restricted Net Assets
    - a. Program – Accumulated earnings available for specific purposes or programs.

- b. Spending – Accumulated amount of investment earnings from permanent and quasi-endowments available to support specific purposes or programs.
  - c. Investment in Tangible Property – Value of donated tangible property that can be sold.
  - d. Principal – Initial value of gifts received from donors.
3. Permanently Restricted Net Assets
- a. Principal – Initial value of gifts received from donors.
  - b. Investment in Tangible Property – Value of donated tangible property that cannot be sold or disposed of.

**B. Classification of Net Assets**

Net Assets of the CPC shall be classified in accordance with accepted accounting principles established by the Financial Accounting Standards Board (FASB).

**C. Assignment of Net Assets**

Assignment or designation of net earnings shall comply with donor-imposed restrictions, and Board of Director approved policy and budgets.

**D. Delegated Authority**

The Executive Director has the authority to transfer and assign unappropriated net earnings of the General Fund to the Plant Fund and Designated funds based on present and anticipated financial requirements, expected total return on future investments, general economic conditions, and programmatic need.

**E. Practices**

1. Application of Accounting Rules & Standards

At the close of each fiscal year the net earnings from each function shall be added to separate net asset classification accounts as required by FAS No. 117.

2. Assignment or Designation within Net Assets Classifications

Supplemental assignment or designation of net earnings within the required net assets classifications shall be done as follows:

- a. The first priority for use of net earnings shall be the assignment of funds as available to match the individual function's actual donor-imposed restriction, investment in operational assets, approved budget appropriation, audit/legal requirement, or specific program account. These transfers will be automatic, not requiring Board of Directors' approval.
- b. From net earnings of the Bookstore, Campus Dining, and General Investments, an amount equal to these functions' share of the University Services Program

commitment for the next fiscal year shall be transferred to the Designated Fund to provide funding for these activities. These transfers have been authorized by the Board of Directors' approval of departmental budgets that state their budgeted contribution to University Services. If funding is inadequate for this purpose, transfers from other available net assets must cover the unfunded portion of the commitment.

- c. If a balance remains in the net earnings accounts of the Bookstore and Campus Dining after the above assignment, these funds shall be transferred to the Plant Fund as Capital Replacement funds.
  - d. If a balance remains in the net earnings accounts of Sponsored Programs Administration after the above appropriations, these funds shall be transferred to a Designated Fund for appropriate allocation by the University President.
  - e. If a balance remains in the net earnings accounts for General Administration and the General Investment Pools after the above appropriations, the funds shall be transferred to the Designated or Plant Fund based on Executive Director judgment of programmatic need.
  - f. Specific Reserve goals are detailed in the document "Net Asset Funding Guidelines", which is a supplement to this Policy and the annual Fiscal Viability Report. Annually, in conjunction with the Fiscal Viability Report, the Executive Director will provide a review of the Reserve goals and shall recommend modifications as necessary.
3. Annual Report  
The Executive Director shall annually develop and present to the Board a Fiscal Viability Report. The approved report shall be forwarded to the University President for consideration and approval as the CPC's plan to build and maintain appropriate reserves.