Section 3: Finance and Investments

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November, 2009

3.1 Budgeting Policy

Budget Process and Implementation
Budgeting for any fiscal period will not deviate materially from the mission, goals, and strategies of the Society; risk fiscal jeopardy; nor fail to show a generally acceptable level of foresight. Staff will present a draft of the annual budget to the Finance Committee for review and modifications prior to its being submitted to the board.

The SRNT board approves the annual operating budget for each calendar/fiscal year that will project income and expenses and will provide for programs and support services. The board will approve the annual budget prior to the start of the fiscal/calendar year.

The board authorizes the executive director to manage the organization in accordance with the approved annual operating budget. Unbudgeted programmatic or operational changes that may have a significant impact on the annual budget ($10,000 or more) must be reviewed by the board between budget cycles and may lead to a budget revision. The board, with input from the Finance Committee, will determine whether or not the budget should be revised mid-year.

3.2 Financial Audits Policy

Annual Audit
The finance committee will recommend to the board whether an audit, a review, or no external review will be undertaken in a given year. However, barring any such recommendation SRNT will undergo a review of finances in odd-numbered years and an audit in even numbered-years; however, if a particular funder requires an audit in order to continue funding, SRNT will have annual audits.

Any audit or review will be undertaken by an independent CPA firm that has a significant group of nonprofit clients. If the same audit firm conducts the audit for more than five consecutive years, the finance committee is authorized to review the firm's services and decide if the firm or the audit partner needs to rotate.

The audit firm will not be hired to perform non–auditing services, except for tax preparation and Form 990 preparation and will not perform substantial services for any officer or director personally. The audit firm is engaged to present annual audit findings to the executive director, the finance committee, and the board. The finance committee will review the audit and make its recommendation to the board.

*3.3 **Spending Authorities Policy***

An authorized check signer will make disbursements only upon review and approval of the transaction. This will include review for the existence of proper supporting documentation, such as an invoice or receipts.

The secretary/treasurer, executive director, and the finance manager are authorized to sign checks.

All expenses and/or check requests must be approved by the executive director; payments greater than $5,000 require approval of the secretary treasurer.

The executive director is authorized to approve unbudgeted expenses up to $2,500.

The Secretary-Treasurer is authorized to approve unbudgeted expenses between $2,500 and $5,000.

The President is authorized to approve unbudgeted expenses between $5,000 and $10,000.

The Board must approve unbudgeted expenses greater than $10,000.

3.4 IRS Form 990 Policy

The executive director will ensure that filing of tax returns and any government-ordered payments or other filings are undertaken in a timely and accurate manner.

The executive director will sign and certify that the IRS Form 990 is accurate and complete.

The secretary/treasurer is authorized to review and approve the IRS Form 990 annual tax filing prior to submission, and the full board will receive a copy of the IRS Form 990 within 30 days of its submission.

Consistent with the requirements of §6104(d) of the Internal Revenue Code, copies of the organization's Form 990 will be made available, upon request, in a timely manner, to any individuals who request it.

3.5 Risk Management Policy

Asset Protection
The management company hired by SRNT will adequately protect and maintain from unnecessary risk SRNT's records, other documentation and any assets, as well as staff assigned to SRNT. Accordingly, the management company will

- Insure against theft and casualty losses of tangible personal property to at least 80 percent replacement value and against liability losses to board members, staff, or the organization itself at no less than minimally acceptable prudent levels
- Have sufficient employee dishonesty insurance for personnel with access to material amounts of funds
- Protect intellectual property, information, and files from loss or significant damage
- Hold operating capital in secure instruments, such as insured checking accounts, bonds or other interest-bearing accounts in accordance with board-approved policies and/or direction from the finance committee
- Protect the organization, its board, and staff from exposure leading to claims of liability
- Not endanger the organization's public image or credibility, particularly in ways that would hinder its accomplishment of mission, except when necessary to accomplish its mission

Insurance
SRNT will purchase necessary policies to insure the organization against risk. Types of insurance to be purchased should include

- General liability (personal and property damage and punitive damage)
- Nonprofit Officers' and Directors' Liability (also knows as association professional liability)
- Annual Meeting Cancellation
- In all cases, SRNT will be insured at the highest-possible levels.

Additional types of insurance needed to protect the organization must be approved by the board.

3.6 Financial Reserve Fund Policy

Recommended Reserve Policy: SRNT will maintain in reserve funds sufficient to meet operating and other necessary expenses for a period of no fewer than 12 months.

Rationale: A reserve fund is necessary to cover operating expenses if income does not meet expenses. Based on a review of similar organizations and the recommendation of our auditors, we recommend a reserve fund that covers approximately 12 months of operating expenses in any given year. Sources of our current income includes (a) new and renewal memberships, (b) registrations at the annual meeting, (c) grants, including

the American Legacy Grant to support publication of our flagship journal, (d) contributions, (e) journal subscriptions, and (e) investments/interest.

Areas of Concern: We are particularly concerned with the stability of the income associated with registration at the annual conference, grants, and contributions.

a) Annual conference: Conference registration is not reliable and, because we are unable to predict income from the annual meeting, variability in income is expected.
b) The American Legacy Grant ends in March of 2007. SRNT has relied on this income to fund the publication of *Nicotine and Tobacco Research*. While steps are in place to reduce costs associated with the publication of this journal, it is unknown if these steps will sufficiently reduce the costs.
c) The receipt of other grants and contributions to SRNT has been substantial, but future receipts are uncertain. In the past, SRNT has relied on specific members to solicit grants and to obtain contributions to support annual meetings and the society.

Proposal: The finance committee proposes that a minimum of 50% of the annual net income (annual revenue minus expenses) be put into the reserve fund, until the long term goal is reached. The remaining dollars will be placed in the general fund to be used at the discretion of the board.

3.7 Investment Policy

GENERAL PRINCIPLES

The investment policy governs the investment of all financial assets of the Society for Research on Nicotine and Tobacco (SRNT)

Objectives

Investment of funds should be made solely for the purpose and in the best interest of the Society's objectives.
The investment policy reflects objectives of meeting both short-term and long-term goals. Short-term goals involve meeting the operating expenses of the Society. Long-term goals include building a reserve fund ("rainy-day" fund) in case of future unforeseen needs along with building savings for future projects identified by the Board of Directors.

Fiduciary Responsibility and Limits of Fiduciary Responsibility

Members of the Finance Committee, other members of the Board of Directors, and officers of the SRNT management company have a fiduciary responsibility to monitor the finances of the Society.
Members of the Finance Committee, other members of the Board of Directors, and officers of the SRNT management company, acting in accordance with written policies and procedures and exercising due diligence, shall not be held personally responsible for a specific investment's credit risk or market price changes.

Members of the Finance Committee, other members of the Board of Directors, and officers of the SRNT management company must disclose any personal business activity or financial/investment positions that could be related to the performance of the investment portfolio or that could conflict with the proper execution and management of the investment program or that could impair their ability to make impartial decisions.

Role of Finance Committee

The SRNT Bylaws state that "the Finance Committee shall be responsible for recommendations regarding fiscal policy to the Board, including but not limited to proposals and recommendations regarding investment and management of Society reserves."

The Finance Committee is responsible for adhering to the principles specified in this investment policy.

The Finance Committee is responsible for periodic reporting at the Board of Directors meetings on the status of investments. The Finance Committee is also responsible for bringing to the attention of the Executive Committee any significant changes in the Society's investments.

The Finance Committee will be responsible for identifying when changes to the investment portfolio need to be made.

The Finance Committee will be responsible for making specific suggestions for changes to the investment portfolio, consistent with the investment policy. Such changes will be presented in writing to the Board of Directors if an annual meeting is scheduled to occur within the next month, or to the Executive Committee if an annual meeting is not scheduled to occur within the next month.

Role of Board of Directors and Executive Committee

The members of the Board of Directors will be responsible for reviewing the report of the Finance Committee at the Board of Directors meetings.

The Board of Directors will be responsible for approving changes in the investment portfolio. This may be done by voice vote at the Board of Directors meetings or by electronic vote at times other than Board of Directors meetings. In the latter case, the Finance Committee will present specific suggestions in writing to the Executive Committee. The Executive Committee will determine whether the suggested change has sufficient urgency to warrant an electronic vote by the Board of Directors.

In situations that are considered particularly urgent, the Executive Committee may approve changes in the investment portfolio. In this case, the voting will be done by voice vote at the Executive Committee conference call or by electronic vote at times of other than Executive Committee conference calls. Such actions and the reasons for the urgency must be reported to the Board of Director's at its next meeting.

Specific Investment Policies

SRNT, because of its commitment to impartial research on nicotine and tobacco, will not knowingly hold investments in companies whose primary business is related to nicotine, tobacco, nicotine replacement products and other aids to smoking cessation, or services related to smoking.

SRNT will manage its investments in a manner that will not risk the public's trust of the Society.
Alternative investments which are widely viewed as having a high degree of risk are not permitted. Such investments include, but are not limited to: venture capital, private equity, hedge funds, margin accounts, options, and futures.

Classes of Assets

Assets held by SRNT will be divided into three classes. The objectives, level of acceptable risk, required liquidity, asset allocation parameters, and asset quality requirements differ across the three classes.
Objectives of each class of assets – The three classes of assets are primarily defined by anticipated cash flow requirements. The first class has as its objective to meet immediate cash-flow needs. The second class has as its objective preservation of special funds (e.g., grants and contributions) that are earmarked for specific purposes. The third class has as its objective building a reserve fund and saving for future goals.
Level of risk acceptable for each class of assets - The level of risk varies across classes. For the first and second class, there should be the lowest level of risk involved. For the third class, some risk is acceptable commensurate with a long-term investment perspective.
Liquidity in each class of assets - The degree of liquidity varies across the three classes of assets. The first class must be immediately convertible to cash. The second class must be convertible to cash within the timeframe of the specific need. The third class must be held in investments that can be converted to cash. However, the purpose of these funds is to build a reserve fund and savings for the Society, so funds allocated to this third class should be viewed as long-term investments that will rarely need to be liquidated to meet immediate cash needs.
Asset allocation parameters in each class of assets – The asset allocation parameters vary across classes of assets. In general, assets in all three classes should be diversified. However, the degree is diversification is greatest for the third class of assets. Assets in the first and second classes that are held in cash may have limited diversification taking into consideration the need to have efficient accounting of cash transactions and ready access to these funds.
Asset quality in each class of assets – Assets in all three classes should be held in high-quality investments with the caveat that a portion of funds in the third class may be invested in lower grade corporate bonds if the degree of income is judged to reasonably offset the degree of risk. The exposure to such lower-grade funds should be limited.

Policies regarding the first class of assets – those needed to meet immediate Cash-flow requirements

Objectives of this class of assets – The first class of assets differs from the other classes of funds in that it has as its primary objective to meet immediate cash-flow needs.
Level of risk acceptable for this class of assets - For the first class, there should be a very low level of risk and a very high level of safety involved.
Liquidity in this class of assets - The first class of assets must be immediately convertible to cash.

Asset allocation parameters in this class of assets – Assets in the first class may have limited diversification given the low risk of cash held in U.S. banks and cash-equivalents held in U.S. security firms. There is also need to have ready access to these funds and efficient accounting of cash transactions. For example, one checking account is preferable to multiple checking accounts. However, it should be noted that the Federal Deposit Insurance Corporation insures accounts up to $100,000. Because of this maximum, the accounting firm for SRNT points out that there is possible risk, and advises that funds held at any one institution be limited to $100,000.
Asset quality in this class of assets – Assets in this class should be held in high-quality investments.
Given the parameters described above, the specific investment principles for this class of assets are:

- Maintenance of sufficient assets to meet the expected operating expenses of the Society
- Preservation of capital with a very low level of risk and high degree of safety
- Maintenance of sufficient liquidity to meet immediate cash-flow needs
- Generation of income to the degree practical, given the over-riding requirement of the first three principles.

Given these investment principles, allowable investments for this class of assets include and are limited to cash and cash equivalents. These may include:

- Checking accounts
- Savings accounts
- Money market funds
- Short-term certificates of deposit

Choices among these options should be based on ease of accounting and access along with maximizing interest rates.

Policies regarding the second class of assets – special funds raised for specific purposes

The purpose of this second class of assets is to segregate those funds that are generated outside of the usual sources of income and that have a specific purpose identified. These assets include those that are generated from grants and contributions that are earmarked for a specific purpose (for example, a contribution to support a special award or a grant to support an upcoming meeting). These assets are usually received by the Society and held for some period of time until relevant expenses accrue. For accounting purposes, there may be benefits to segregating these assets from the general operating funds of the Society. This is particularly true if the granting organization requires accounting of expenditures related to these funds or if the holding period extends beyond a year.
Objectives of this class of assets – The second class has as its objective preservation of special funds (e.g., grants and contributions) that are earmarked for specific purposes.
Level of risk acceptable for this class of assets - There should be a very low level of risk and a very high level of safety involved.

Liquidity in this class of assets – These assets must be convertible to cash within the time frame of the specific need.
Asset allocation parameters in this class of assets – In general, assets should be diversified. However, assets in the second class may have limited diversification taking into consideration the need to have efficient accounting of cash transactions and easy access to these funds.
Asset quality in this class of assets – Assets should be held in high-quality investments.
Given the parameters described above, the specific investment principles for this class of funds are:

- Maintenance of sufficient funds to meet the specific requirements specified by the grants or contributions that generated these funds
- Preservation of capital with a very low level of risk and high degree of safety
- Maintenance of sufficient liquidity to meet the time horizon of these funds
- Generation of income to the degree practical, given the over-riding requirement of the first three principles.

Given these investment principles, allowable investments for this class of assets include and are limited to cash and cash equivalents. These may include:

- Checking accounts
- Savings accounts
- Money market funds
- U.S. government treasury bills
- U.S. government bond funds
- Certificates of deposit

Choices among these options should be based on ease of accounting and access along with maximizing interest rates.

Policies regarding the third class of assets – those needed to build a reserve fund and save for future goals

Objectives of this class of assets – The third class has as its objective building a reserve fund and saving for future goals. Assets not currently needed for cash-flow requirements (the first class of assets) or earmarked for specific purposes (the second class of assets) may be allocated to this third class of assets.
Level of risk acceptable for this class of assets - Some risk is acceptable commensurate with a long-term investment perspective.
Liquidity in this class of assets - The third class must be held in investments that can be converted to cash. However, the purpose of these funds is to build a reserve fund and savings for the Society, so funds allocated to this third class should be viewed as long-term investments that will rarely need to be liquidated to meet immediate cash needs. The time horizon for investments should be 3 – 10 years.
Asset allocation parameters in this class of assets – Assets should be diversified. Diversification is an accepted approach to minimizing risk when funds are invested in non-cash equivalents. Assets will be diversified both by asset class (fixed income and

equities) and within each asset class. Further diversification is easily attained by investing in mutual funds. For this reason, mutual funds will be the only acceptable form of investment in fixed-income and equities.

Asset quality in this class of assets – Assets should be held in high-quality investments with the caveat that a portion of funds in the third class may be invested in lower grade corporate bond funds if the degree of income is judged to reasonably offset the degree of risk. The exposure to such lower-grade bond funds should be limited.

Given the parameters described above, the specific investment principles for this class of assets are:

- Safety and preservation of principal
- To increase the real (inflation-adjusted) value of the assets over the long term
- Maximization of yield on the portfolio and prudent participation in growth with a 3-10 year horizon

Given these investment principles, allowable investments for this class of funds include and are limited to:

- Fixed income
    - Government bond funds
    - Corporate bond funds
    - International bond funds
- Equities
    - U.S. equity funds
    - International equity funds
- Cash or cash-equivalents (a minimum amount of funds may be held in cash, but this should not be normally viewed as an investment vehicle that meets the objectives stated above)

Asset allocation

Asset allocation should fall within the following ranges:

- Cash-equivalents 0% to 25%
- Fixed income 25% to 75%
- Equities 25% to 75%

The objectives of this class of assets suggest that the investments should include maximization of yield and prudent participation in growth. Because risk is a concern to the Society, the portion of assets invested in growth funds should not exceed 75% of the total market value of the equity funds. The remainder of the assets invested in equity funds may be invested in value funds or balanced funds.

To balance risk, equity funds should be diversified among large cap, medium cap, and small cap funds. Because risk is a concern to the Society, the combination of medium cap and small cap funds should not exceed 50% of the total market value of equity funds.

To decrease risk to any one geographic market, equity funds should be diversified across domestic and international funds. Investment in international markets may include international funds, world funds, foreign funds, or global funds. International funds should be broadly based and should not be limited to a specific geographic region. The portion invested in international funds should not exceed 25% of the total market value of the equity funds. The portion invested in emerging market funds should not exceed 10% of the total market value of equity funds.

Fixed income funds may include government bond funds or corporate bond funds. The portion of funds invested in lower grade corporate bond funds (e.g., high yield bond funds or junk bond funds) should not exceed 10% of the total market value of fixed income funds.

Emerging market debt securities should not exceed 10% of the total market value of fixed income funds.

A summary of these asset allocation principles is listed in the table below

Asset category	Minimum recommended percent	Maximum recommended percent
Cash equivalents	0% of total investments	25% of total investments
Equity funds	25% of total investments	75% of total investments
Growth funds	25% of equity funds	75% of equity funds
Value or balanced funds	25% of equity funds	75% of equity funds
Large cap funds	25% of equity funds	75% of equity funds
Medium and small cap funds	25% of equity funds	50% of equity funds
International equity funds	0% of equity funds	25% of equity funds
Emerging market equity funds	0% of equity funds	10% of equity funds
Fixed-income funds	25% of total investments	75% of total investments
Government bond funds	0% of bond funds	100% of bond funds
Corporate bond funds	0% of bond funds	100% of bond funds
High yield corporate bond funds	0% of bond funds	10% of bond funds
Emerging market bond funds	0% of bond funds	10% of bond funds

Principles for selecting specific investments

The proportions outlined above will guide the asset allocation of the funds in this third class of investments. Specific investments will be made with a 3-10 year time horizon in mind.

Each selected fund's performance will be monitored at least bi-annually, comparing it to peer funds' and appropriate indices performance.

To identify and monitor specific investments, historic performance in terms of total return and volatility will be considered. Specific investments will be sought that have high performance over a 3-year, 5-year, and 10-year period relative to peer funds' performance or appropriate market sector indices. Risk, as measured by the annualized standard deviation of quarterly returns, should be less than that of the market index or sector average over the same 3-year, 5-year, and 10-year rolling periods. Specific

investments should have performance data available for at least 5 years, but may be considered if they are younger than 10years old. Benchmarks such as Morningstar, Inc. ratings may be used to identify specific investments.
Ideally, investments will be bought with a “buy and hold” strategy in order to maximize return. The Society will seek investments that will grow in value over time, rather than attempt to buy and sell in anticipation of short-term changes in market value. However, investments may be sold before they mature in the following instances:

- A security with declining credit may be sold early to minimize potential loss of principal
- A change in securities which would improve the quality, yield or target duration of the portfolio
- Liquidity needs of the organization require the investment to be sold.