

TREE FUND MEMORANDUM

Date: November 22, 2016

To: TREE Fund Board of Trustees

Fm: J. Eric Smith, President and Chief Executive Officer

Re: Report for December 5, 2016 Trustee Meeting

INTRODUCTION:

Last Friday, I returned to our Naperville office after a productive experience participating in the Partners for Community Forestry's (PCF) 10th Annual Conference. I was grateful that the Arbor Day Foundation (who organized the event) gave me a prominent moderating position at the closing general session at this high-value conference, which attracted over 550 people through its two-day schedule, many of whom are new to me and the TREE Fund – and many of whom are decision-makers and policy-shapers who could best benefit from (and support) our research, community engagement and education programs.

This was the final trip of my 2016 “listening tour,” and it was easily among the best networking and “friendraising” events of the year for me. I think it's important to note that this is a conference that TREE Fund staff and management have not attended in the past – in large part because it does not lend itself to small-value retail fundraising. As we seek to “open the circle” of funders in years ahead, though, this event is *exactly* the type of setting where we will make the new connections needed to cultivate new partners, and I see PCF as an anchor of my travel schedule for the foreseeable future accordingly.

Having visited 18 of the 20 U.S. ISA Chapters this year (Rocky Mountain and Michigan are the only two I could not schedule; I have Michigan calendared in early 2017 already, and am working to get to Rocky Mountain in the first half of the year, too), I feel that I have been able to communicate a fresh message and demonstrate the importance that *all* of our ISA colleagues hold for us, and not just those belonging to large and affluent chapters. While I cannot (and should not) attempt to visit all 20 U.S. Chapters on an annual basis, I have set a goal for 2017 and beyond to have staff representation (me or others) at least every other year at every U.S. Chapter, while better empowering our liaisons to be our “champions” in the years when we are not there.

My travel activities in 2017 will focus more on completing the quiet phase of our endowment building campaign (including “seating” the campaign leadership committee), and on identifying and participating in high-impact, high-connection events like PCF. There are likely to be cases where I will be visiting some of your own geographic regions, and in many of those cases, it will advantageous to our campaign outcomes for me to be joined by Trustee(s) as I make cultivation and solicitation visits – so I will be in touch with respectful requests as needed in the months ahead, and am hopeful you will be able to make time to support such activities.

As I've noted to you all before, I believe in frank and full reporting in my communications with you, as I believe you require such candid information to properly fulfill your own fiduciary and governance responsibilities to our corporation. By necessity, such candor also dictates that documents like this one be held closely by their intended recipients, and considered company sensitive information. Therefore, I respectfully request that you do not forward or share this report beyond Trustees, Barb Duke and I, with thanks in advance for your discretion.

KEY PROJECTS COMPLETED IN 2016:

Much of my activity since our October teleconference has been focused on key items that will be carried to the Trustees for action on December 5 via your committee chairs or as part of our report from CCS on the Endowment Building Campaign Feasibility Study, so rather than just reiterating points that will be made in those Committee Reports, I want to provide a very macro summary of some key projects and activities that the team and I have completed this year to provide a sense of how we have moved some strategic elements forward atop our normal tactical operations:

- Created more timely and concise financial reports and implemented monthly Finance Committee meetings to provide more “real time” coverage of our activities.
- Completed Audit Committee RFP and engaged new auditor on three-year contract.
- Completed Feasibility Study RFP and will receive CCS's report on December 5.
- Negotiated a new five-year office lease, doubling our space with only a 50% increase in cost.
- Negotiated a new three-year contract with our STIHL Tour des Trees Tour Manager, more clearly defining staff vs contractor roles to enhance efficiency and accountability.
- Evaluated all insurance policies and made changes to provide enhanced risk management.
- Conducted banking reviews and shifted operating accounts to new provider with better service structure and lower fees.
- Completed full legal and policy review of the Trust Agreement that defines our governance structure and will present restated version for Trustee approval on December 5.
- Clarified the nature of the relationship between Chicago Community Trust (CCT) and TREE Fund, collecting required documentation and recommending Board action to ensure these funds are properly posted in our general ledger and balance sheet.
- Implemented and completed year one of the PG&E challenge, and issued new RFP for pilot program to establish test sites in California for future utility grants; Dr. Dozier will have a recommendation for Trustee action on the \$175,000 pilot grant on December 5.
- Created new Corporate Partnership models that are fully compliant with relevant tax and reporting regulations to ensure proper allocation of charitable contributions vs earned income.
- Reinvented “TREE Fund After Hours” event successfully at the ISA International Conference, beating both revenue and expense goals.
- Completed 2016 STIHL Tour des Trees under new fundraising and community engagement rubric that directs all rider funds to research, allows donors to restrict Tour donations to endowment, and seeks to defray all expenses with corporate partners; all goals achieved, and we are on track for a record-setting \$400,000 rider fundraising response by year's end.

- Implemented aggressive efforts to increase grant application and award levels; we should exceed the ambitious \$450,000 award goal in 2016, with at least \$350,000 per year to be included in the 2017 budget (this number is contingent on CCS's report) and beyond.
- Managed these activities while declining to accept any payments from Chicago Community Trust this year to demonstrate our ability to live within our means, and draw down surplus operating reserves; the funds we did not take in 2016 will be available to us in 2017 to fund campaign and related expenses.
- Made real time transfers to CCT of endowment gifts throughout the year, rather than mingling funds with operations and doing a single transfer at year end; as a result, the endowment will grow by nearly 25% in 2017.

CAMPAIGN FEASIBILITY STUDY AND 2017 BUDGET

We have a tight series of interconnected activities going on this month to bring both the CCS Feasibility Study report and the 2017 budget to you for action. I provided the detailed 2017 Budget Proposal to Finance Committee on November 4, and we discussed it as a committee on November 18. This budget assumes that the Endowment Building Campaign will be at the \$5.0 million level we are testing in the Feasibility Study. Finance Committee has a follow-up meeting scheduled on November 29 for their final approval of budget levels to be carried to you for approval. CCS's written report of the Feasibility Study findings is due to us on November 30, so I have requested that if CCS anticipates recommending a level below the \$5.0 million goal we are testing, then they let me know that before the November 29 Finance Committee meeting, so that I can adjust the budget figures appropriately. Once the Finance Committee has approved these revised and final budget numbers, I will provide all of the Trustees with the summary budget and the campaign cash flow analysis, and these will be the documents we will review on December 5. On these fronts, I will be seeking two votes from the Trustees at the December 5 meeting: one to affirm the CCS findings, then one to approve the related budget level for 2017.

2016 FINANCIALS

Bottom line: we've had a great year. Through the end of October, here's how things look:

	<u>Annual Budget</u>	<u>YTD Thru October</u>	<u>Year End Forecast</u>
Revenue	\$1,167,500	\$1,459,351	\$1,668,000
Expense	\$1,223,900	\$ 901,397	\$1,369,000
Net Income	(\$56,400)	\$ 243,954	\$ 299,000

Our total transfers to endowment should be about \$570,000 for the year, so our net assets increase significantly, but our cash liquidity will decrease. This is consistent with my budget plan for the year; we had surplus contingency cash reserves in our operating account at the start of the year, and our heightened real-time increased reporting to Finance Committee and monitoring of accounts is allowing us to manage "closer to the bone" than we have in the past.

Revenue lines are up largely because of our success with the PG&E Challenge, the UAA/PG&E Current Year Pilot Project award that came in higher than I had budgeted, gifts to the Collier Fund made at last year's Winter Management Conference, and higher-than-budgeted returns for rider fundraising on the Tour (we should hit \$400,000 this year) and the new TREE Fund After Hours Event. Expenses are in line with budget except in two areas: we are spending more on subcontracted operations (primarily the CCS contract, along with some other consultant labor on the accounting side), and we will book about \$550,000 for grants awarded instead of \$450,000 budgeted due to the accrual nature of our accounting practices, and the ways in which the UAA/PG&E Current Year Pilot Project funding is coming in and going out. (Dr. Dozier will be recommending a vote on a \$175,000 award for this sponsored grant at the December 5 meeting; it will not be paid until 2017 and 2018, but must be booked as an account payable upon completion of its contract in December). We will adjust the 2017 grant award number from \$450,000 to \$350,000 to reflect this timing shift.

In terms of year-end closeout, staff and I will have our kick-off meeting with our new auditors, Sassetti LLC, on December 7, and they have already scheduled their first call with the Audit Committee in January. We have contracted with Laura Flamion of Clear Impact Financial LLC to serve as our independent book-keeper through the end of 2017, with options to continue her service beyond that, so I am pleased that we have stabilized our accounting function with strong, fresh perspective as we move forward into the campaign.

GOVERNANCE

I have been working with Governance Committee to review and update our Trust Agreement to reflect current realities (legal and organizational), as well as organizational aspirations. The document has been "edited by accretion" since our organization in 2002, with occasional edits to change committee names, number of trustees, titles of officers, etc. But it contains some language that is inconsistent with current nonprofit practice and our own policies, and it defines terms and commitments that are making it more difficult than it should be to recruit new Trustees. The Governance Committee completed a comprehensive review of the document with recommendations for updates, and I subsequently provided the amended documents to an attorney recommended to us by ISA for legal and regulatory review.

As a result of this process, we have prepared a Restated Declaration of Trust which will be presented to the Trustees for approval and ratification. Four separate motions will be requested on this document, as follows:

- Revisions to term limits (Trustee terms shift from two three-year terms to three two-year terms; officer terms shift from two years to one year);
- Allowance for funds to be restricted in perpetuity (Original language limited donor restrictions to 15 years, undercutting arguments that we are an endowment fund);
- Clarification of reimbursement for Trustees (Original language allowed Trustees to be compensated; new language allows reimbursement of expenses not covered by employers, but no compensation);
- Other administrative changes (A "catch-all" for other administrative changes designed to reflect current nonprofit law and policy; none have material impact on operations).

Assuming approval of this Restated Declaration of Trust, I will support Governance Committee in 2017 in conducting a thorough review of our policies to ensure they too reflect the current declaration and best nonprofit practice.

RESEARCH AND EDUCATION

Based on our success with the Raise Your Hand for Research auction at TREE Fund After Hours, and the budget-beating performance of our riders in the 2016 Tour, I notified the Research and Education Committee that we will be able to award three Duling grants and two Kimmel grants at our December 5 meeting, presuming the Committee had sufficient high-quality applications to support those levels. (Canadian TREE Fund will pay for one of the Kimmels, and we will pay for the other). As noted above, we will also have a recommendation to award \$175,000 for a PG&E/UAA-Sponsored grant to establish long-term test plots in California for integrated vegetation management research under the UARF umbrella. As refresher/reminder, such sponsored grants are not competitive, and we collect a “management fee” for handling them; in this case, we will apply that fee to the UARF endowment so that we may receive the 50% matching gift from PG&E in 2017. Also as noted above, from an accounting standpoint, we will need to book this grant in 2016, even though the funds will not be paid until 2017 and 2018. Our final report of grants awarded in 2016 will be ~\$550,000 accordingly, a record-setting performance that positions us well as we move into the endowment building campaign. 2017’s research budget will be adjusted from \$450,000 to \$350,000 to reflect the cash flows associated with the PG&E/UAA-sponsored grant and our two open Research Fellowships, both of which will have payments due in 2017.

FUTURE MEETINGS

I have asked the Liaison Committee, and would respectfully ask the Trustees as well, to consider how we manage our meetings of these groups. While there are positive elements associated with bringing Trustees and Liaisons together each December for a shared meeting, the downside of this approach is that the Liaison Chair is not able to fully participate in the Board’s deliberations, and I am not able to fully participate in the Liaison Committee’s deliberations. As we are seeking to adapt the roles of the liaisons from retail fundraising to “friendraising,” I think these overlaps may be undermining effective communication. I would respectfully like to consider (or return to) a model where the liaisons meet independently of the Trustees, possibly moving to different chapters each year. I would also ask the Trustees to consider whether the December meeting in Rosemont is optimal each year; to me, it seems to prioritize staff convenience over all other considerations, and I do not believe that should be our top priority. Would we want to gather elsewhere at that time? Perhaps at sites that are supported by our grants, etc., as we do in the spring at Morton Arboretum? I would welcome the opportunity to discuss these matters with Executive and Liaison Committees in 2017.

CONCLUSION

2016 has been an exciting year, and I think we are poised for 2017 to be truly transformational. We should have a clear road-map from CCS on necessary steps in the early part of the year to establish our campaign leadership committee and hopefully complete the quiet phase of the

campaign in an expeditious fashion. As noted in my prior report, I may need to make changes to our human resources pool to achieve these goals, with a combination of staff and consultant positions being budgeted in my 2017 proposal. I will not know exactly what this mix looks like until we receive CCS's report, but I have built in the flexibility necessary to allow me to manage the campaign under all likely outcomes. I will keep you posted as we move forward.

Please don't hesitate to let me know if you have any questions, comments, or concerns with anything contained in this report. I remain excited about my work, happy to represent our organization around the country, and pleased with the leadership and wise counsel you have provided to me.

All best,

A handwritten signature in black ink, appearing to read "J. Eric Smith", with a stylized, flowing script.

J. Eric Smith,
President and Chief Executive Officer

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