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The Steward's Prophet

FINANCE FOR FAITH COMMUNITIES

Rev. Karen McArthur, editor

Prophet-able Stewardship

I've been thinking about micro and macro lately. In soccer, we teach "micro-soccer" — individual ball handling skills and small games of keepaway that are designed to focus the child's attention on their own handling of the soccer ball. We also teach "macro-soccer" — the big picture — passing, teamwork, strategy, and rules to keep the game flowing safely. The two are intertwined.

Likewise, in economics there are two branches: microeconomics and macroeconomics. Microeconomics looks at an individual consumer or business and studies its behavior. If the price of a product rises, the consumer will likely buy less. If the price falls, s/he will buy more. If the cost of producing a product increases, a business is likely to produce less of it. If the production cost falls, the business will supply more. Microeconomics has a narrow focus.

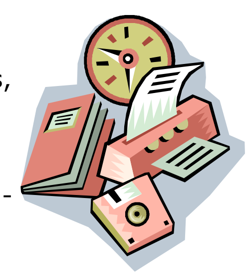
On the other hand, macroeconomics looks at the big picture. How is the amount of money circulating in a country related to inflation? Macroeconomics is the study of Gross National Products and tax policy, public goods and services and unemployment rates. Macroeconomics is about community and relationships.

Without a doubt, the Biblical prophets observed both individual behavior and the big picture. Through their wisdom and their stories, they were able to convince individuals to change, and therefore to change the behavior of kings, tribes, and whole nations.

Faithful stewardship of a congregation's resources requires attention to the multitude of details, along with the ability not only to see and analyze the big picture, but to explain it clearly and concisely. It requires being able to speak to individual desires as well as to congregational decisions.

In 1993, the Financial Accounting Standards Board overhauled non-profit financial reporting, consolidating the various fund designations (capital fund, endowment fund, operating fund, plant fund, etc.) into three types of funds.

With the availability of personal computers, small non-profits became able to account for the tiniest of budget details — and to track these total fund balances easily. This newsletter issue presents the first of these "new" reporting formats, FASB116: Accounting for Contributions Received and Contributions Made.



Links to the full statement and a summary are available at www.stewardsprophet.com/LibraryLinks.html

Inside this issue:

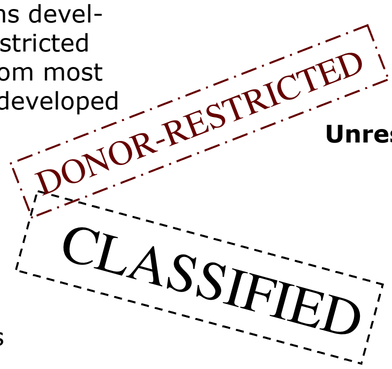
Questions of the month:

- *Does your system keep meticulous records for all of your restricted gifts?*
- *Can you translate from the language of the church to the language of bookkeeping?*

Modeling Faithful Stewardship begins at church

What do you do when you receive a contribution earmarked for a specific purpose? How does the church keep track of it?

Prior to 1993, non-profit organizations developed their own systems for tracking restricted funds. Since churches were exempt from most external reporting requirements, they developed their systems mostly on their own.



This changed in 1993 when the Financial Accounting Standards Board issued their Statement No. 116 (known as FASB116), which standardized non-profit financial reporting.

First, they consolidated various kinds of funds (operating, restricted, capital, endowment, etc.) and named only three types of funds. Contributions may be:

Permanently Restricted — the donor stipulates that the funds must be invested in perpetuity, with the income used for either unrestricted or temporarily restricted purposes.

Temporarily Restricted — the donor's funds may all be spent, but only for a specific purpose or at a specific time.

Unrestricted — funds may be used for any purpose within the mission of the organiztion.

Contributions may be restricted either by purpose (contribution for the Organ Fund) or by time (a contribution for next year)

Note that a church board may not *restrict* funds — only donors can do so. If a Board sets aside unrestricted funds for a specific purpose, they can be listed as "Board Designated Funds" — a subfund of the Unrestricted Fund. The Board can also vote to remove the designation.

There once was a church ...

There once was a church with a comfortable balance in the bank — not too much and not too little.

They realized that it wasn't the church's purpose to accumulate wealth, so they began to expand their ministry. They received gifts for building a school in Africa, as well as gifts for the addition of a new church office and elevator.

The long-time pastor retired and the budget surpluses turned into deficits. The church wasn't concerned, because they still had plenty of money in the bank.

However, what they didn't realize was that although they had $80,000 in the bank, the missions gifts of $32,000 and the elevator gifts of $54,000 were both Temporarily Restricted, leaving unrestricted net assets of negative $6,000.

QUIZ

Classify these net assets as either Unrestricted, Temporarily Restricted, or Permanently Restricted:

1. Gift to be used for Hurricane Relief Fund
2. Sunday morning plate offering
3. Baker Fund, given to be invested, with the income only spent on food and fellowship.
4. Capital Campaign contributions
5. Last year's surplus, to be used for painting the parsonage
6. Century Fund, to be invested for 100 years, with all income retained. After 100 years, the Fund remains invested forever, with the income used for general church purposes.
7. $2000 prepayment of a pledge
8. A $5000 bequest received in 1896, income to be used for missions. It has been kept in the endowment fund and has grown to $84,000.

ANSWERS ARE ON PAGE 4

The Usual Disclaimer

This newsletter seeks to provide current and accurate information about the topics presented.

However, it is offered with the understanding that if you need accounting advice, you should contact an accountant who can review your situation personally and offer her or his professional advice.

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Bookkeeping Bible: It started with a Franciscan Friar

Who said money and religion have to be separate? It was a Franciscan monk in the late 15th century who is credited with developing the system of double-entry bookkeeping. Lucas Pacioli, who collaborated with Leonardo da Vinci for many years, developed the system that is still in use today.

In double-entry bookkeeping, everything balances. Those who are trained in bookkeeping talk about "debits" and "credits." The difficulty for those of us who have not taken accounting coursework is that half of the time, the transaction is intuitive (if you want to record income received, you credit it) but the other half of the time, it is counter-intuitive (if you make a deposit to your bank account, you debit it).

So let's stick with "increase" and "decrease" for now and learn what happens. Once we get the concept, we can pretty much let go of the debits and credits anyway, since accounting software will take care of it for us, hidden in the background.

The **four types of transactions** (asset, liability, expense, and income) are all interrelated. If we explore a few examples, we'll begin to see patterns.

- If you purchase coffee for coffee hour, you increase your fellowship line (expense) and you decrease your bank account (asset).
- If you transfer money from your investment account to your checking account, you decrease the investments (asset) and increase checking (asset.)
- If you purchase stamps using a church credit card, then you increase your postage line (expense) and increase your credit card balance (liability). (When you pay off the credit card, you decrease your credit card balance and decrease your checking account).
- If you receive a deposit for nursery school tuition for next year, you increase your bank account (asset) and increase your prepaid tuition (liability.) Then, when school starts, you decrease your prepaid tuition (liability) and increase the tuition line (income.)
- If you make a mortgage payment, you decrease your bank account (asset), increase mortgage interest (expense), and decrease mortgage principal (liability.)

From these examples, we can discern the following principles:

- If the two sides of a transaction are both the same type, then one will increase and the other decrease.
- Assets behave like expense – and income behaves like liabilities. If a transaction involves an asset or expense on one side and income or liability on the other, then either both will increase or both will decrease to keep everything in balance. Similarly, if a transaction involves an asset and expense or if it involves income and liability, then one will increase and the other will decrease.
- If something happens in multiple steps, each step along the way will balance. In example #3 above: ↑ postage expense & ↑ credit card liability, then ↓ credit card liability & ↓ bank account. The middle two cancel each other out, which leaves you with the transaction in example #1 above.
- If you have a split transaction (such as a loan payment), then the total of the increases and the decreases won't necessarily balance, because some are debits and some are credits – but the total of the debits will always equal the total of the credits.

A note for all of us who are theologically, rather than financially, trained: Regarding debits and credits, you can get by memorizing only two concepts: <u>to increase a liability, you credit it</u> and <u>liabilities and income behave alike</u>. (Remember that L's and I's look alike). From there, you can figure everything else out. If increasing a liability credits it, then increasing an asset must debit it, etc. In #5 above, to increase an interest expense you debit it, to decrease mortgage principal (a liability) you debit it, and to decrease an asset you credit it. So the credit amounts and the debit amounts do balance, just like the friar taught us 500 years ago.

The advent of computerized bookkeeping has made double-entry accounting more accessible to small organizations. A picture of a check comes up on the screen – you fill in the date, the payee, the amount and what you're charging it to – and the software does the rest, debiting the expense and crediting the asset. This can be a good thing … increasing the ability of churches to monitor their financial activity and be faithful stewards of their resources. But "with great power comes great responsibility." If we don't know just what we're doing, the tasks of bookkeeping can feel confusing and overwhelming, and ultimately decrease the congregation's confidence in its stewardship.

FINANCE FOR FAITH COMMUNITIES

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Since 1996, Karen McArthur has specialized in financial management for churches and faith communities. Her ministry is based at First Church in Cambridge, Massachusetts, where she is Affiliate Minister of Stewardship and Finance, as well as a Stewardship Consultant for the Massachusetts Conference of the United Church of Christ. She is available for consultation and training both in person and on-line.

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ANSWERS TO QUIZ

1. *Temporarily Restricted*
2. *Unrestricted*
3. *Permanently Restricted, with income temporarily restricted*
4. *Temporarily Restricted by purpose*
5. *Unrestricted—Board Designated*
6. *Permanently Restricted, with income also permanently restricted for 100 years*
7. *Temporarily Restricted by time*
8. *$5,000 Permanently Restricted; the remainder temporarily restricted*

It only takes a spark ... Pass it On!

This is a brand new newsletter offered with the hope that sharing knowledge of non-profit accounting practices will strengthen the ministry and mission of local congregations.

In order to spread the word, developing a mailing list of interested readers is essential. Please use the forwarding feature at the end of the accompanying e-mail to share this with anyone and everyone you think might be interested in the topics. You may subscribe to the newsletter list by entering your email address in the box labeled "subscribe." Back issues are available on the website at www.stewardsprophet.com.

Your contact information will not be sold, given away, or otherwise shared. You may unsubscribe fully and completely via a link at the bottom of each monthly e-mail.

COMING NEXT ISSUE:

Financial Reporting Formats

Bookkeeping Bible:

Developing a capital budget

A simple one-page budget format

Financial Accounting Standards Board Statement 117 translated into church language

UPCOMING TOPICS:

FASB 124—Accounting for investment income, gains and losses

Payroll bookkeeping

Internal controls