Clearly Communicating Ministry Financial Data

by **Dan Busby,** *ECFA President*

Completing timely financial reports is often a challenge for a ministry's financial management staff. You are so relieved when the financials are run and the data appears reasonable!

Additionally, working with the external auditors on the annual audit is frequently a daunting task. You are so pleased when the audit report is received from the auditors and you can send it to the board and/or the audit committee.

Surprise! Your work on the monthly and annual financial data has just begun if the data is going to *read and understood.* Uninterpreted financial reports are a financial data wasteland.

What do you mean? The CEO hasn't asked for interpretative information. The board hasn't raised any issues about the data. Donors rarely ask questions about the financial data included in the annual report. Why should the data be further explained? Read on . . .

- **Determining financial trends—both positive and negative.** Financial trends are often hidden in raw data. The most dangerous unidentified financial trend is a negative one. If you have a early warning system using flash reports to detect negative data trends, you have a running start to address the issues before the situation becomes severe.

- **Providing assurance that donor-restricted net assets are properly funded.** It is the rare financial report that explains whether or not donor-restricted net assets have been borrowed for operational purposes. If your ministry practices short-term borrowing of donor-restricted net assets, approval should be granted by the board prior to the borrowing. (ECFA has prepared a document on this topic: www.ecfamembers.org.)

- **Some financial statement users need the data analysis but will not request it.** Some ministry staff have a good grasp on financial reports without extensive interpretation. But once you move to the board and your donors, the need for interpretation increases exponentially. Provide adequate explanation of financial data *before* people ask.

> *"Uninterpreted financial reports are a financial data wasteland."*

- **You will never know how many contributions you lost because donors didn't understand your financial data.** Yes, donors are asking more questions than ever before about the financial data of ministries in which they wish to invest their donations. However, only a fraction of your donors will take the time to call, write or email you and seek answers to financial data that is puzzling to them.

Tools to Communicate Financial Data

What types of analyses will bring ministry financial statements to life? Data analysis is clearly not a one-size-fits-all world. However, here are a few indicators that may be helpful:

- **Current ratio.** Ideally, the ratio of your current assets to current liabilities is positive. A negative trend in the current ratio over a period of years could be the sign of declining financial health.

Auditors are not required to reflect current assets and current liabilities on the statement of financial condition—and many do not. But these are the ministry's financial statements and *reflecting this data is your choice.*

- **Unrestricted net assets.** Few numbers are as telling on the financial health of a ministry as the unrestricted net assets—*if* the data is properly reflected. Interpretation of unrestricted net assets is crucial because this number includes net property, plant and equipment after deducting related debt.

Again, there is no requirement for auditors to break out the net property, plant and equipment from the total unrestricted net assets number. But unless this simple step is taken on the financials, it is most difficult to analyze trends for this data.

- **Number of days or months of cash.** This is very useful information—the annual budget divided by the average balance of cash—in determining the strength of the ministry's cash position.

Typically a ministry needs more days of cash in its developmental years. As a ministry matures, the number of days of cash is often reduced. For example, for all ECFA's members, those with annual revenue of under $1 million have over 80 days of cash but ministries in the over $10 million revenue range have only 33 days of cash.

• **Restricted net assets compared to the related assets.** Donors may restrict their gifts as to purpose—for example, for a project or as to time; e.g., a gift cannot be used until a subsequent fiscal year. However, donors rarely restrict how their gift must be invested. Therefore, specific assets are generally not identifiable with temporarily or permanently restricted net assets.

Most donor-restricted net assets are held in cash and cash equivalents or investments. So, except for the most complex ministries, a simple analysis of resources available to fund donor-restricted net assets may be done. If cash and cash equivalents plus investments are not equal to the total temporarily and permanently restricted net assets, borrowing of some of these net assets to fund operations may have occurred.

• **Excess of revenue over expense —or vice versa.** While revenue and expenses may exactly match for budgetary purposes, it is a rare year when the actual revenue and expenses data comes to a zero balance.

Significant positive or negative swings in the revenue as compared to expense may be very understandable when the underlying reasons are communicated. However, differences between revenue and expenses are often confusing to a casual reader of the financials.

For example, a large excess of revenue over expense may result during the early stages of a capital campaign. Conversely, in a year when the campaign funds are expended, the depletion of the temporarily net assets may cause a significant excess of expenses over revenue. This is very justifiable but often not clearly understood.

Summary. Analyzing, interpreting and clearly communicating financial data takes time—it's hard work. The work occurs after the internal financial are run, after the audit report is delivered, and after the first draft of the Form 990 is prepared. But it's worth the effort!

Keys To Clearly Communicate Financial Data

• **Audit report to the Form 990.** Be sure the data reconciles between these two documents.

• **Audit report to the annual report.** The data should agree between these two documents. Don't adjust any audit numbers with the permission of your auditors.

• **Use graphics liberally.** A picture—and a graph—is worth a thousand words. Graphics are easy to produce with computer software but it often is challenging to produce graphics that tell a story.

Try to use two related data elements on the same graph. This will enhance understanding and reduce the number of graphs needed to communicate your data.

• **Prepare financial questions and answers (Q&A).** Review your audit with an eye to questions a reader might ask. On an accompanying page, use a Q&A format to answer the questions before they are asked.

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