Is Your **Church Budget** Useless?

by Dan Busby, CPA

THAT MAY SEEM LIKE A STRANGE QUESTION COMING FROM SOMEONE COMMITTED TO FAITHFUL ADMINISTRATION OF KINGDOM RESOURCES.

So, let me reaffirm – church budgets are not useless – unless we destroy their usefulness. Keep reading to see what I mean.

Churches readily understand the importance of preparing an annual budget and having it duly approved by the appropriate church committee, board, and/or the congregation – whichever is charged with financial accountability and oversight responsibility.

Most also know that after you create and formally adopt your church budget, the next step is periodically comparing revenue received and expenses incurred against the budget throughout the year. These comparisons are helpful in identifying early indications of potential opportunities, problems, and significant variances. The comparisons also lay the groundwork for deciding how your church will respond to any significant differences (variances) between the actual and budgeted amounts.

Here is the BIG catch! *A budget is a largely useless document* unless the monthly budget allocations are done well. Decisions of whether to make spending adjustments must be informed by sound allocations of revenue and expenses. For example:

- Utility costs are higher in the winter especially for churches located in the Midwest and the Northern parts of the U.S., so the budget must reflect the higher expenses in those months if the monthly budget to actual comparisons are to be accurate.

- Likewise, while digital giving has flattened out what we used to see as lean summer months, December is still the month where the highest giving is anticipated. Simply spreading giving revenue on a ratable basis (i.e., 12 equal monthly proportions) would produce inaccurate data.

- Additionally, there may be one-time costs related to special church programming at Easter, August (back-to-school), and Christmas. To spread these expenses ratably throughout all 12 months would result in meaningless allocations.

So, what is the solution? Changing a budget line is often difficult. These amounts may be etched in stone. In fact, many churches have a policy never to change the budget once it is adopted. Even if the budgetary changes net to zero, modifying budget lines might require board or finance committee approval.

On the other hand, allocations of revenue and expenses between months are generally an internal matter – allocations can be modified by staff, in most instances. So, do not live with your bad budget allocations for the entire year! That is so-o-o painful. Make mid-year adjustments to the allocations to help keep your budget to actual reporting on track.

HOW DO SOME CHURCHES (THIS WOULD NEVER BE YOUR CHURCH!) SHORT-CHANGE THE BUDGET ALLOCATION PROCESS?

Here are three possibilities:

- **A church takes the easy way out on budget allocations.** The simplest and most inaccurate way to arrive at monthly budget numbers is to divide each budget line-item by 12 months. This may work for monthly rent payments and insurance premiums, but for most line-items, it is not a valid approach. If January and February always have disproportionate heating bills plus a big annual insurance premium, then every single year you will start off quickly sinking behind budget, and then spending the next several months saying, "we are way behind." Then if a truly "way behind the budget" situation occurs, your appeal may then find resistance or giver fatigue from people saying, "but we just went through that!"

- **A church allocates the line-items based solely on previous year data.** This approach is better than dividing the line items by 12 months; however, it falls short of sound allocations because it fails to take into account changes in circumstances for the current year. There may be changes in one-time or cyclical program expenses, such as new or increases in line items that are effective only for part of the year. Suppose last year's women's retreat was in the spring and this year moves to the fall. If you do not reallocate your budget, you might unwittingly spend any spring excess and get caught short in the fall.

- **Budget allocations do not match where expenses are charged.** When the budget was adopted, there was an expectation that certain expenses would be charged to particular expense accounts; however, there is a significant mis-match on the charging of some large expenses. Some categories, therefore, show major variances only because the budget dollars are on one line and the actual expenses are on another.

WHAT CAN HAPPEN IF YOUR BUDGET IS NOT PROPERLY ALLOCATED?

Let us say a church is at the midway point in the year – with six months actual data on the books. Based on the comparative data, with poorly sourced revenue and expense budget allocations, the financial statements reflect that revenue is behind projections and expenses are significantly over budget as shown below:

MISLEADING REPORT BASED ON *POOR* ALLOCATIONS

	YTD Budget	YTD Actual	Variance
Revenue	$1,200,000	$1,000,000	$(200,000)
Expense	1,100,000	1,400,000	(300,000)
Excess	$ 100,000	$ (400,000)	$(500,000)

However, if the proper budget allocations had been made, the reports would have shown that revenue and expenses are both right on target as shown here:

MORE ACCURATE REPORT BASED ON *MORE CAREFUL* ALLOCATIONS

	YTD Budget	YTD Actual	Variance
Revenue	$1,000,000	$1,000,000	$ -0-
Expense	1,400,000	1,400,000	-0-
Excess	$ (400,000)	$ (400,000)	$ -0-

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Here are just two unfortunate decisions that could be made from the report based on poor allocations:

- **Programs are started and jettisoned based on poor information.** A new ministry to millennials was started at the beginning of the new church year. Because the comparative data outlook is so gloomy, the church board decides to temporarily stop the new program until finances improve. By the time the accurate data is available, the church restarts the program, but considerable momentum is lost because of starting, stopping, and restarting the program.

- **Staff are hired or terminated based on poor allocations.** Based on the inaccurate data at the six-month point, the church board reduces two full-time staff members to half-time and eliminates four part-time positions.

A few months later, the church board realizes it took these extreme actions based on faulty information.

WHAT IS THE CHURCH FINANCIAL TEAM TO DO?

Take these simple steps:

1. **Take monthly budget allocations seriously.** Do not go through the arduous budget development process and destroy the usefulness of the budget by failing to do the further hard work of making sound revenue and expense allocations by month.

2. **Study prior year actual data by month.** The starting point for current year budget allocations is the prior year actual data. Study it to determine the significant data that will change for the current year. For example, in the prior year, suppose a large expense for attorney fees occurred over a four-month period because of a lawsuit brought against the church. The matter is now closed and only a modest amount is in budget as a legal retainer – this amount might well be spread ratably over the current year.

3. **Reflect on changes in revenue or expenses patterns for the current year.** Certain new or increased activity for the current year may modify the monthly revenue or allocation pattern for the current year. For example, a new program may be scheduled only to run for three months in the spring and three months in the fall, therefore the budget allocations by month must match the anticipated expense pattern.

Here is the bottom line: The usefulness of comparative financial statements is highly dependent on the validity of line-item budget allocations over the 12 months of the year. To say it another way, the meaningful analysis of monthly or quarterly data between actual and budget numbers is virtually impossible without sound budget allocations by month.

Sound budget allocations will help your church make more informed decisions. Try it, and see for yourself how useful a budget can be.

Author

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