# The Parish Accounting System

The goal of parish accounting is to take the many transactions that happen in the parish and create a set of informative financial statements that give a clear picture of the financial situation of the parish.

Why do we have a parish accounting system? Why bother with budgets, journals, and financial statements? Why not just keep a balanced checkbook?

First of all, it's required. Canon law states that all parishes "are bound to submit each year...an account of their administration."(Can. 1287). The Diocese of Crookston Mission Statement states that "all parish financial records are (to be) maintained in accord with generally accepted accounting principles for fund accounting and the norms of the National Council of Catholic Bishops (NCCB)."

In addition to satisfying these reporting requirements, a good accounting system will provide relevant information to decision-makers that will enable them to make informed decisions when dealing with financial issues within the parish. If the parish just counts on their checkbook to keep track of where they are financially, the only information they'll get is how much money they have. This is just one part of the total picture of the parish's financial health. The parish may have thousands of dollars, but are there restrictions on that money that limit the way it can be spent? Does the parish have any debt? Are they generating enough income to cover their expenses? A good accounting system can answer all of these questions.

## Office of Parish Administration

The Office of Parish Administration is in charge of the parish accounting system. It strives to create a system that meets generally accepted accounting principles while being easy enough for anyone to use regardless of their training and experience level, and at the same time flexible enough to adapt to the varied needs of the parishes throughout our diocese.

Many of the parishes in the diocese perform their own bookkeeping. However, the diocese realizes that not every parish can afford to hire a professional accountant to do their bookkeeping for them. But it is just as important for a parish with 50 families to have a quality accounting system as it is for a parish of 5000 families. Thus the Office of Parish Administration has been charged with assisting smaller parishes with their bookkeeping. The Office provides a qualified resource person to work with the parish's bookkeeper to generate quality financial reports. With the help of this resource person, a small parish with a volunteer bookkeeper will be able to prepare financial statements as good as the statements prepared by a large parish with a full-time bookkeeper on staff.

Each month the parish bookkeeper fills out input forms (Cash Receipts Journal, Cash Disbursements Journal, Payroll Journal, General Journal, and Bank Reconciliation) detailing the parish's financial transactions for that month. These forms are mailed to the Office of Parish Administration, where they are inputted into an accounting program and reviewed. Then a set of financial statements are generated and mailed to the parish for use by the pastor, finance council, etc.

## ***Parish Accounting Manual***

The Parish Accounting Manual is the how-to guide for the parish accounting system. It describes the framework that all parishes will follow in their accounting.

Section 1 gives some general background on accounting, discussing the theory behind the system. Section 2 discusses the input forms (cash receipts journal, cash disbursements journal, payroll journal, general journal, bank reconciliation), as well as the financial statements generated by the system. Section 3 focuses on fund accounting, a concept unique to non-profit accounting. Section 4 discusses planning and budgeting. Section 5 discusses internal controls.

# Section 1:  Accounting Theory

This section will explain some of the basic concepts of accounting, such as debits and credits and account classification.  Many of the terms used later in the manual are defined in this section.  This information is presented as background information; you don't have to master all this information to do the bookkeeping for your parish.  But if you understand the theories behind the procedures, the procedures themselves will make more sense and you will be better-prepared to handle special situations that may arise

## Transactions and Journals

A **transaction** is any event that generates a change in the financial position of the parish.  Writing a check and making a deposit are examples of transactions.  Each transaction should be recorded in the appropriate journal.

A **journal** is a form used to record transactions.  There are four journals used in the parish accounting system.  The **Cash Receipts Journal** is used to record deposits and other additions to cash accounts.  The **Cash Disbursements Journal** is used to record checks and other reductions of cash accounts.  The **Payroll Journal** is used to record payroll checks.  All other transactions are recorded in the **General Journal**.

## Accounts

An **account** is an individual record of increases or decreases in a specific asset, liability, or equity item.  An account could track the amount of cash in a specific bank account or how much is owed to a creditor.  Separate accounts exist for each source of revenue and each type of expense.  Accounts can be as general or specific as required; one parish may have an account called "Fundraiser Revenue", while another parish with multiple fundraisers may have a separate account for each fundraiser.

There are three types of accounts:  headers, footers, and details.  **Header accounts** appear at the beginning of each section and define that section.  "Revenues" or "Operating Assets" are examples of header accounts.  **Footer accounts** are the "total" accounts such as "Total Revenues" or "Total Assets".  **Detail accounts** are the "in-between" accounts, the accounts that provide the details for each section.  Examples of detail accounts include "Savings Account" and "Interest Income".

| | | |
|---|---|---|
| Header- | Operating Assets | |
| Detail- | Checking Account | $546 |
| Detail- | Savings Account | $900 |
| Footer- | Total Operating Assets | $1456 |

**Only detail accounts can be used when recording transactions.**  Headers only identify sections and footers are used only for totals.  Transactions cannot be entered into these accounts.

## Account Classifications

All accounts can be classified into one of three categories:

1. Assets
2. Liabilities
3. Equity

The relationship between these categories is expressed by the **accounting equation**:

$$\text{Assets} = \text{Liabilities} + \text{Equity}$$

**Assets** are all items of value held by the parish. Assets include cash, investments, and receivables. Land and buildings are also assets.

In not-for-profit accounting, it is important to distinguish assets as unrestricted, restricted, and designated. **Unrestricted assets** are available for the general use of the parish. The parish checking account is an example of an unrestricted asset. **Restricted assets** are limited in purpose by the donor. Money donated for a building project would be a restricted asset. The parish is legally obligated to spend restricted assets for their specified purpose only. **Designated assets** are assets that have been set aside by the parish for a specific purpose, usually through a corporate board motion. The parish can remove the designation at any time, making the money unrestricted again.

<u>Types of Assets</u>

Unrestricted-no restrictions

Restricted-restricted by donor

Designated-restricted by parish

**Liabilities** are the debts of a parish. These include payroll taxes withheld from employees' paychecks, unpaid diocesan special collections, and loans from banks. Liabilities are classified as current and long-term. **Current liabilities** are due in one year or less. **Long-term liabilities** are due in over one year.

**Equity** represents the parish's ownership in the parish assets. In for-profit accounting, equity is commonly referred to as Capital or Owners' Equity. In non-profit accounting, equity is referred to as **Fund Balance**. Think of the parish's assets as having two groups of "owners," the parish and the creditors. The liabilities are the amount of assets the creditors have a right to; the remainder, the fund balance, is the amount of assets the parish has a right to. If the Fund Balance is negative, that means that the parish's liabilities exceed their assets.

Fund Balance has two main components: net income or loss and retained earnings. **Net income or loss** is the change in Fund Balance that has occurred during the current fiscal year as a result of revenue inflow and expense outflow. If total revenues exceed total expenses, the result is a net income, which increases the total Fund Balance. If total expenses exceed total revenues, the result is a net loss, which decreases the total Fund Balance. **Retained Earnings** is the accumulation of previous years' incomes and losses.

Entries are very rarely made directly to fund balance accounts. Instead, the fund balance is affected by entries made to the revenue and expense accounts. **Revenues** are monies given to the parish for use in their ministries. Common sources of revenue for a church include offertory collections, fundraisers, and interest on investments. **Expenses** are the costs associated with carrying out the ministries of the parish. Common expenses for a parish include salaries and benefits, utilities, and the costs of liturgical supplies. Revenues increase the total Fund Balance; expenses decrease the total Fund Balance. The net effect of these accounts is shown on the balance sheet as Net Income or Loss.

## Receivables and Payables

A **receivable** is an asset account that is used when some party owes the parish money. When the debt is established, a receivable account is created. This indicates that the parish will be receiving money in the future from another party. The balance due will appear on the balance sheet as an asset, because it represents cash the parish will be receiving at some point in the future. When the parish receives the money, the receivable is reduced. When all the money is repaid, the balance of the receivable account should be zero. Receivables are often used in a multi-parish setting to reflect the amount owed to the head parish by the mission parishes for shared expenses.

*Note on pledges*: pledges are not recorded as receivables because the person making the pledge is not legally obligated to pay anything. Pledges are only recognized when they are actually paid.

A **payable** is another word for a liability. It represents an amount the parish owes to another party. When the obligation arises, a payable account is created. The current amount owed will appear on the balance sheet as a liability. When the amount is repaid, the liability is reduced. When the debt is paid in full, the balance of the payable account should be zero.

## Debits and Credits

**Debits** and **credits** in accounting terminology are basically words for left and right. An account consists of three components: the title of the account, the left or debit side, and the right or credit side. This is visualized by thinking of the account as a "T".. Entries are made on both sides of the T. If the total of the transactions on the debit side is higher than the total on the credit side, the account has a **debit balance**. If the credit side is higher, the account has a **credit balance**.

Account Name

| Debit Side | Credit Side |
|---|---|

Think back to the accounting equation: assets = liabilities + fund balance. Accounts on the left side of the equation (assets) normally have debit balances. Accounts on the right side of the equation (liabilities and fund balance) normally have credit balances. Revenue accounts increase the total Fund Balance, so they have credit balances. Expense accounts decrease the total Fund Balance, so they have debit balances. **Debits must always equal credits.** If they do not, the accounting equation does not balance.

<u>Accounts with Debit Balances</u>
Asset Accounts
Expense Accounts

<u>Accounts with Credit Balances</u>
Liability Accounts
Fund Balance Accounts
Revenue Accounts

So when you're recording a transaction, how do you know what to debit and what to credit? To increase an account with a debit balance (asset or expense account), debit that account; paying the priest's salary increases the Priest's Salary expense account, so this would result in a debit to that account. To decrease an account with a debit balance, credit it; transferring money from the checking account

| Debit | Credit |
|---|---|
| Increase assets | Decrease assets |
| Decrease liabilities | Increase liabilities |
| Increase expenses | Increase revenues |

would decrease the amount of cash (an asset) so a credit would be made to the cash account. The reverse is true for accounts with credit balances; liabilities, fund balance accounts and revenues. A transaction that increases one of these accounts is a credit; a transaction that decreases one of these accounts is a debit.

*Helpful Tip:* The best place to start when deciding what to debit or credit is to look at the cash account. Most entries will involve cash in some way. Cash is an asset with a debit balance. Therefore, a debit is made to increase cash, and a credit is made to decrease cash. Once you've determined that debit or credit, the other half of the entry can be made to balance the equation.

Here are some examples:

- Cash is received from the Sunday collection. Cash, an asset, is increased, so a debit is made to Cash. In order to balance the transaction, we need an equal credit amount. The Sunday collection accounts (adult envelopes, loose plate, etc.) would be credited. The total of these credits should equal the debit made to the cash account.
- A check is written to pay for the electric bill. Cash, an asset, is decreased, so a credit is made to the cash account. To balance the transaction, we need a debit; that debit would be to Electricity Expense.
- Money is received from the mission church for shared expenses. Cash is received, so a debit is made to cash. The amount owed by the mission church is recorded on the parish books as a receivable, which is an asset account. Since this account is being decreased (less money is owed by the mission) a credit is made to the receivable.
- The parish takes out a note at a local bank. Cash is received from the bank, so a debit is made to the cash account. The amount owed to the bank is a liability. This amount is being increased, so a credit is made to the appropriate liability account.
- The parish pays back a portion of its outstanding debt to a local bank, along with interest. Cash is going out, so that account is credited. The amount owed by the parish is decreased, so the appropriate liability account is debited. The amount of interest expense is increased, so this account is also debited. The total of these two debits should equal the total of the credit to the cash account.

## Cash vs Accrual Basis of Accounting

There are two standard bases of accounting: cash accounting and accrual accounting. **Cash accounting** records a transaction when cash changes hands. Revenues are recorded when cash is received and expenses are recorded when checks are written. **Accrual accounting** looks more at the substance of the transaction than the actual exchange of cash. Revenues are recognized when they are realized and measurable, and expenses are recognized when incurred. Under accrual accounting, you could recognize an expense for something you haven't paid for yet, or defer recording a revenue for money you've already received.

An example will illustrate the difference between the two bases: you receive a bill from the diocese for the parish assessment. Under accrual accounting, you would record the expense as soon as you receive the bill, along with a liability showing the amount owed to the Diocese. Under cash accounting, the expense would not be recorded until the bill is paid, which may be many months later.

The parish accounting system normally uses a cash basis for recording revenues and expenses. However, parishes have the option of using accrual accounting. The Office of Parish Administration will occasionally recommend accrual treatment for certain transactions to ensure the accuracy of the financial statements. (See page 31 for more information on accrual accounting.) The main exception to the cash basis is depreciation, which is used if the parish has a Capital Fund; see the section on Fund Accounting for more information.

## The Fiscal Year

The most accurate way to measure the net income or loss for any organization would be to measure its operations from the time the organization was formed to the time it was dissolved. Obviously, this isn't very feasible. Decision-makers cannot wait until the organization is dissolved to get information on the financial situation of the organization. Thus the lifespan of the organization is broken down into fiscal periods, usually of one year's length. In the parish accounting system, the fiscal year runs from July 1 to June 30.

Each month, interim statements are prepared. The monthly report for June is the year-end statement for the parish. Once the year-end report has been verified, the books for the year are closed. This involves resetting all revenue and expense account balances to zero and posting the net income or loss for the year to retained earnings. This procedure is normally performed by the parish's accounting software.

This artificial division of the parish's lifespan can sometimes result in reports that may not accurately reflect a given situation when handled on a cash accounting basis. Say, for example, that a parish has a special collection in June to pay a big repair bill in July. The money from the collection will appear as revenue in one year but the associated expense will not show up until the next year. Some of these situations can be avoided through the use of accrual accounting, discussed above.

## Financial Statements

Two financial statements are generated in parish accounting. The **Balance Sheet** shows the assets, liabilities, and fund balance of a parish as of a certain date. By looking at this statement you can see how much the parish has in its checking account or how much is owed for special collections. The balance sheet is issued as of the last day of the month. The **Income Statement** shows the revenues and expenses of the parish over a period of time. This statement shows the amount received in adult envelopes and the amount paid for church electricity, and so on.

In addition to these two financial statements, there are two other reports that are commonly prepared. The **general ledger** shows the beginning and ending balances for each account, along with a list of transactions grouped by account. The **trial balance** is a list of all accounts, along with their beginning and ending balances and the net change in each account for that month. (See page 35 for more information on the financial statements)

## Year-End Reports

The parish's year-end report consists of two statements: the June 30 balance sheet and the income statement for the year ending June 30. The parish year-end report must be approved by the parish's corporate board within 90 days of the end of the fiscal year. The pastor, trustees, and bookkeeper must sign a Statement of Accountability verifying the accuracy of the report.

## Payroll

Payroll transactions are often a source of confusion for bookkeepers. This section discusses payroll concepts that bookkeepers should be familiar with. Page 18 discusses payroll entries in a Payroll Journal, and page 27 discusses payroll entries in a Cash Disbursements Journal.

There are three categories of pay that the bookkeeper needs to be familiar with. The **gross pay** is the amount that is being paid to the employee before any deductions have been made. If the employee is salaried, this is the amount of salary earned. If the employee is hourly, this amount is the number of hours worked multiplied by the hourly rate. Gross pay is the amount that needs to appear as salary expense for the employee. The **taxable pay** is the gross pay less any pre-tax deductions. Payroll taxes are computed on the taxable pay. The **net pay** is the amount paid to the employee after all deductions have been made; basically, the amount of the check.

<u>Types of pay</u>

Gross Pay=amount employee earns, before any deductions are made

Taxable Pay=gross pay less pretax deductions

Net Pay=gross pay less all deductions

There are a number of withholdings made from an employee's paycheck. All payroll withholdings are recorded as liabilities, because the parish will need to pay these amounts to some other entity in the future. These include:

- **Federal income tax**: the amount of federal tax withheld is determined by referring to the federal tax tables provided annually by the Internal Revenue Service. The amount withheld depends on whether the employee is married or single, and how many exemptions the employee claims. In addition to the computed amount, the employee can also elect to have additional taxes withheld. Federal tax withholding is calculated using taxable pay.

- **State income tax**: the amount of state tax withheld is based on the specific rules for the state in which the employee resides. For Minnesota employees, the Minnesota Department of Revenue provides tax tables to determine the amount of withholding. State tax withholding is calculated using taxable pay.

- **FICA taxes**: there are two components to this tax, **Social Security tax** and **Medicare tax**. Both of these taxes are a percentage of the employee's taxable pay. At the time this manual was written, the percentages are: Social Security=12.4% Medicare=2.9%. Half of this amount is withheld from the employee's paycheck; the other half is paid by the employer. This matching payment is recorded as an expense of the parish.

- **Insurance premiums**: at the time this manual was written, there were four diocesan-sponsored benefit plans that employees may be paying out of their paychecks. Employees may have payroll tax withholdings for medical insurance, dental insurance, supplemental life insurance, and/or the SelectAccount Cafeteria Plan. Medical and dental insurance premiums are pretax deductions, unless the employee specifically elects not to have them withheld pretax. Cafeteria plan deductions are also pretax. Supplemental life insurance premiums are not pretax.

- **Other deductions**: there are a number of other items that employees could have withheld from their paycheck. Some of the possibilities include tuition payments and contributions to retirement accounts. These other deductions may or may not be pretax.

Pre-Tax Deductions

Some employees may have items that are withheld on a pre-tax basis. Under Component A of our cafeteria plan, all money withheld for diocesan medical and/or dental premiums is withheld pre-tax. Withholdings elected under Component B and C of the cafeteria plan are also withheld on a pretax basis. Other qualifying items can be withheld on a pretax basis, such as contributions to a qualifying pension plan.

The bookkeeping for a pre-tax item is no different than that of any other withholding. A liability account is used when the paycheck is recorded, and that same liability account is used when the money is paid to the appropriate agency. The main point to focus on here is the effect this has on taxes.

The pretax deduction, as the name implies, is subtracted from the employee's salary before payroll taxes are computed. Let look at the example of a parish secretary who receives a salary of $2000, and has $200 withheld for her medical/dental insurance. Her gross pay is $2000, but her taxable pay is $1800 ($2000 gross wages less $200 pretax deduction). Her federal, state, and FICA taxes will be based on the taxable pay. The taxable pay is used when preparing the quarterly 941 report and the annual W-2 reports. However, all other benefits (pension plan, life insurance, long-term disability, unemployment, workers compensation) are based on the gross pay.

One note about health insurance premiums: when you pay the diocese for the employee's premiums, make sure you divide the total premium between the liability account (employee's portion) and the appropriate expense account (employer's portion).

Special Tax Status Of Priests/Deacons

Priests and deacons (hereafter referred to collectively as "clergy") have a special dual-tax status. When working in a church environment, they are considered employees for federal and state income tax, but are considered self-employed for FICA taxes. This means that the parish does not withhold FICA taxes from their paychecks, and does not provide the matching payments for the clergy. The clergyman will be responsible for paying the entire tax himself, in the form of self-employment tax.

Although the clergyman cannot have FICA taxes withheld from his paycheck, he can have additional federal tax withheld from his paycheck to cover the amount he'll need to pay for self-employment taxes. For example, if a deacon's salary is $20,000 the deacon could have an additional $3060 (20,000 X 15.3%) of federal tax withheld throughout the year to cover the amount he owes the federal government for his FICA taxes. This preference would be indicated on the W-4 form.

One side-effect of this unique tax status is that it allows clergy the benefit of having a portion of salary designated as nontaxable. This can be done through unreimbursed business expenses and/or a housing allowance.

Clergy can have a portion of their paycheck set aside as unreimbursed business expenses; taxes would not have to be paid on this amount. To qualify as an unreimbursed business expense, the expense must meet two criteria: the item must relate to the clergy's occupation, and the expense must not be paid by the parish. For example, a priest pays for a subscription to a magazine that will help him perform his duties better. Since this is a legitimate business expense, and the priest is paying this expense out of his pocket without reimbursement from the parish, he can claim this as an unreimbursed business expense. If the parish reimbursed the pastor for this expense as part of the continuing education benefit, the pastor could not claim it because the parish ultimately paid for the item. Items that can be claimed as unreimbursed business expenses include professional fees, books, periodicals and subscriptions, memberships and dues, continuing education, supplies, mileage, and postage. Donations to the parish can also be claimed as a pretax deduction.

Mileage is one area that confuses a lot of people. Assume the IRS mileage rate is 32¢ a mile. If a priest traveled 1000 miles in one month during the course of his work, and did not receive a mileage reimbursement from the parish, he could claim $320.00 as an unreimbursed business expense. If he received a mileage reimbursement from the parish (in our example, at 30¢ a mile), he could claim the difference between the two rates, 2¢ a mile, as an unreimbursed business expense of $20.00 for that month.

There are two methods that can be used to handle unreimbursed business expenses. The first method has the pastor submitting these expenses to the parish, and the parish paying the bills, indicating in their records that these items are unreimbursed business expenses. When the time comes to pay the pastor, the amount of unreimbursed business expenses is totaled, and that amount is subtracted from the pastor's salary as a pretax deduction. The parish would then write a check to the priest for the remaining salary. If a priest makes $2000 a month and the parish has paid $500 of unreimbursed business expenses, the priest's taxable income would be $1500 and he would receive a check for that amount.

The other option has the pastor paying the expenses himself. At the end of the month he submits a Preists' Business Expense Form (found on page 147a-1 of the Diocesan Policy Book) to the parish listing his unreimbursed business expenses for the month along with receipts verifying the expenses. The pastor will then receive two payroll checks: one tax-free check for his unreimbursed business expenses, and another check for his taxable income. In our above example, the priest would a check for $500 and another check for $1500, less taxes.

An important thing to remember about unreimbursed business expenses is that they are pretax payroll deductions and are part of the pastor's salary. No matter which method is used, the unreimbursed business expenses must be coded as salary when paid. In the example above, the total priest's salary for the month is $2000, regardless of how much of it is unreimbursed business expenses. The expenses come into play when looking at tax issues. In the situation above, the priest would have a gross salary of $2000 but a taxable salary of $1500. The taxable salary is the amount that will be reported on his W-2 form and is used to calculate his taxes for the year.

For more information on this topic, refer to item II(b) on page 147 of the Diocesan Policy Book.

Clergy can also claim a housing allowance; this normally only applies to deacons because priests have residences provided to them. This allowance is income tax free, but not free from self-employment tax. Items that can be claimed include rent or mortgage payments (principal, interest, taxes, and insurance), utilities, capital improvements, repairs and maintenance, and interior furnishings. The allowance is limited to the lowest of the following three restrictions: the amount designated in advance by the employer, the fair rental value of the residence, and the actual expenses incurred in providing for the residence. However, a deacon who receives a tax free housing allowance is required to reduce business expense deductions in proportion to tax-free income to total income. For example, a deacon with a $20,000 salary has a tax-free housing allowance of $12,000. His ratio of tax-free income to total income is 60% (12,000/20,000). The deacon can only deduct 40% of unreimbursed business expenses. It is strongly recommended that the clergyman consult a tax accountant when setting up a tax-free housing allowance.

# Section 2: Journals and Reports

This section can be thought of as the "how-to" section. It discusses the input forms the bookkeeper fills out each month: the cash receipts journal, cash disbursements journal, payroll journal, general journal, and bank reconciliation. It also discusses the reports generated each month by the parish accounting process.

Parishes that report to the Office of Parish Administration: Some parishes receive bookkeeping assistance from the Office of Parish Administration. Each month, the bookkeeper records the parish's transactions in journals and sends the information to the Office of Parish Administration. This office enters the transactions into the accounting software, reviews the information, and generates financial statements that are returned to the parish.

This section is vitally important for these parishes. It discusses the journals that the bookkeeper will complete each month, and the financial statements the bookkeeper will receive.

Parishes that are "on their own": Some parishes do not report to the Office of Parish Administration on a monthly basis. These parishes are not required to complete the journals discussed in this section. However, the bookkeeper may still want to use these journals to provide documentation for the entries that need to be made for the accounting software, and bank reconciliations will still need to be done for cash accounts. Even if the bookkeeper decides not to prepare journals, the examples in this section can guide the bookkeeper in making the appropriate entries in their accounting software program.

Parishes that do not report to the Office of Parish Administration on a monthly basis are still required to submit a year-end financial report. The section on financial reports discusses the requirements for the year-end report, and also discusses the importance of these reports.

## The Bookkeeper's Role

The parish bookkeeper is the most important person in the Parish Accounting system. The bookkeeper is responsible for recording and coding all transactions. It is the bookkeeper's responsibility to see that all transactions are recorded accurately and completely. If a transaction is omitted or coded to the wrong account, the bookkeeper may be the only one who can catch the error.

## Chart of Accounts

The master chart of accounts is in Appendix A. Your parish will not need all the accounts in the master chart, and may need accounts that are not in the master chart. Each parish will have its own individualized chart of accounts, based on the master chart of accounts but customized to fit the parish's needs. You should use the parish chart of accounts when determining account numbers for journal entries.

Pay close attention to the classification of the accounts. The parish may have three accounts for grounds upkeep: one for the rectory, one for the church, and one for the RE facilities. If someone mows the lawn around the rectory, make sure the appropriate grounds upkeep account is used.

Transactions may occur that cannot be classified in any of the accounts in the parish chart of accounts.  If the transaction is not expected to occur again and is small in amount it can be recorded in a miscellaneous account such as Miscellaneous Expense or Miscellaneous Revenue.  If the transactions is significant in amount and is expected to be reoccurring, a new account should be added for it.

## Expense Allocation

Expenses in the operating fund are divided into five categories:  administration (priest compensation, secretary/bookkeeper compensation, etc.), education (RE, sacrament preparation, etc.), worship (expenses associated with the liturgy), Christian service (donations to the needy, pro-life support, etc.), and other expenses (capital projects, cemetery expenses).  It is important that expenses are properly classified into the appropriate divisions so that the parish has a realistic picture of how much it is spending on each division.  If the church is used for mass and religious education, the expenses associated with the church should be divided between worship and education expenses.  A janitor's compensation may need to be allocated between the rectory (an administrative expense), the church (a worship expense), and the RE building (an education expense).

## Working with the Journals

There are four journals used to enter transactions.  The Cash Receipts Journal is used to record deposits.  The Cash Disbursements Journal is used to record checks and other outflows.  The Payroll Journal is used to record payroll checks.  The General Journal is used to record transactions that don't fit into the other two journals (such as error corrections).  These journals are described in more detail in the following sections.  The other input form, the bank reconciliation, is also described.

When entering amounts in the Amount column of any journal, an entry that decreases an account should be marked with a minus sign or put in parenthesis.  For example, when recording a transfer of $1000 from the savings account to the checking account, the entry for the savings account would be recorded as -$1000 or ($1000) because the savings account balance is being reduced.  When a special collection is paid, this would be recorded as a negative because you are reducing the amount owed for that special collection.

## Cash Receipts Journal

The cash receipts journal is used to record transactions that deal with the receipt of cash. Transactions recorded in this journal include the offertory collections, receipt of money from mission churches, and interest received.

A section of a cash receipts journal is pictured below:

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| | | | | |
| | | | | |
| | | | | |

Date: the day the transaction occurred
Description: a brief description of the entry
Ref #: the reference number of the transaction. Entries are numbered sequentially starting with number one each month. This number is used to reference a specific transaction (e.g. I have a question about entry 12 in the December cash receipts journal).
Acct #: the number of the account affected by the transaction
Amount: the dollar value of the transaction

Most parishes have more than one bank account that deposits are made into. The bookkeeper can either make all entries in the same journal, or have separate journals for each bank account.

Entries are recorded on the day that a deposit is made. Each individual component of the deposit is listed, along with the total amount of the deposit.

SAMPLE TRANSACTION: The collection for July 6 is deposited. The amounts are: adult envelopes = $2000 children’s envelopes =$10 and loose plate =$250.

The date of the transaction, July 6, is recorded in the date column. For a description, the bookkeeper can simply write “Adult envelopes” or “Sunday Offertory”. Since this is the first entry recorded for that month, the reference number is 1. The appropriate account number, 4111000, is recorded in the account number column, and $200 is recorded in the Amount column. The other entries are handled in the same way. The completed entry is shown below:

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 7/6 | Adult envelopes | 1 | 4111000 | 2000.00 |
| | Children’s Envelopes | 2 | 4112000 | 10.00 |
| | Loose Plate | 3 | 4113000 | 250.00 |
| | Deposit to checking account | 4 | 1110000 | 2260.00 |

If $500 of the collection is deposited to a savings account, the entry is as follows:

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 7/6 | Adult envelopes | 1 | 4111000 | 2000.00 |
| | Children's envelopes | 2 | 4112000 | 10.00 |
| | Loose plate | 3 | 4113000 | 250.00 |
| | Deposit to checking account | 4 | 1110000 | 1760.00 |
| | Deposit to savings account | 5 | 1120000 | 500.00 |

Interest received is recorded in the cash receipts journal.

SAMPLE TRANSACTION: Interest on the savings account for July is $5.

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 7/31 | Interest on savings account | 15 | 4520000 | 5.00 |
| | Deposit to savings account | 16 | 1120000 | 5.00 |

## Multi-column Cash Receipts Journal

This specialized journal can be used instead of the standard Cash Receipts Journal. It is a standard cash receipts journal, with extra columns added for the most frequently-used accounts: Adult Envelopes, Youth Envelopes, Loose Plate, and the Checking Account. This allows you to record the Sunday Offertory as a one-line entry. Compare the Sunday offertory entry below with the entry on the previous page.

| Date | Description | Ref # | Acct # | Amount | Adult env 4111000 | Youth env 4112000 | Loose 4113000 | Checking 1110000 |
|---|---|---|---|---|---|---|---|---|
| 7/6 | Sunday Offertory | 1 | | | 2000.00 | 10.00 | 250.00 | 2260.00 |

The bookkeeper can use whichever cash receipts journal he/she is most comfortable with.

# CASH DISBURSEMENTS JOURNAL

The Cash Disbursements Journal is used to record transactions that result in the outflow of cash, usually by check. Bank service charges are also recorded here.

A section of the Cash Disbursements Journal is displayed below:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| | | | | | |
| | | | | | |
| | | | | | |

Date: the day the transaction occurred
Check #: the number of the check. If the transaction is not a check, this field can just be left blank
Payee: the party the payment is being made to
Purpose: a brief description of the entry
Acct #: the number of the account affected by the transaction
Amount: the dollar value of the transaction

Each transaction in the journal is listed individually. At the end of the month the transactions are totaled; this amount is recorded at the end of the disbursements journal as a negative entry to the asset account. A separate cash disbursements journal is kept for each bank account.

SAMPLE TRANSACTION: Payment is made on February 25 to the Diocese for payment of employees' insurance, divided as follows: medical insurance, priest: $246; life/LTD insurance, priest: $12; unemployment compensation for part-time bookkeeper: $2. Check number 654.

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 2/25 | 654 | Diocese of Crookston | medical insurance | 5192000 | 246.00 |
| | | | life/LTD | 5192000 | 12.00 |
| | | | unemp comp | 5288000 | 2.00 |

A bank service charge is recorded as follows:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 5/31 | | First National Bank | service charge | 5908000 | 3.00 |

At the end of the month, the total amount of cash disbursed is recorded at the end of the journal, with a negative sign or parenthesis because it is a reduction of the cash account.

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 7/30 | 2100 | Diocese of Crookston | Pension | 5284000 | 25.00 |
| | | | | | |
| 7/31 | | Disbursements-July | | 1110000 | (1474.44) |

# Payroll Journal

The Payroll Journal is a special cash disbursements journal used exclusively for recording payroll checks. Because of the various payroll withholdings, payroll check entries are often a source of confusion for bookkeepers. Using this special journal makes payroll entries simple and straightforward.

The Payroll Journal is a modified Cash Disbursements Journal. The first five columns are similar to the columns in a regular Cash Disbursements Journal. The Payroll Journal has six additional columns to represent accounts that are regularly used in payroll transactions.

The Payroll Journal is an optional journal. If the bookkeeper is not comfortable with this form, payroll checks can be recorded in the regular Cash Disbursements Journal (see page 27 for more information). If this journal is used, then payroll checks are not recorded in the Cash Disbursements Journal.

A section of the Payroll Journal is displayed below:

| Date | Check # | Payee | Acct | Amount | Federal Withheld | State Withheld | S.S. Withheld | Medicare Withheld | Medical Withheld | Check Amount |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | | | |
| | | | | | | | | | | |
| | | | | | | | | | | |

Date: the day the check was written
Check #: the number of the check
Payee: the person the check is written out to
Acct: the number of the account affected by the transaction. This column is used only for items that do not belong in one of the special columns.
Amount: the dollar value of the transaction. This column is used only for items that do not belong in one of the special columns.
Federal Withheld: the amount of federal tax withheld from the paycheck
State Withheld: the amount of state tax withheld from the paycheck
SS Withheld: the amount of Social Security tax withheld from the paycheck
Medicare Withheld: the amount of Medicare tax withheld from the paycheck
Medical Withheld: the amount of medical/dental insurance premium withheld from the paycheck
Check Amount: the amount of the check. This is the amount that will be credited to the appropriate checking account

The special columns are used to record the amounts of the various payroll withholdings. Any item that does not have its own column is recorded in the "Acct" and "Amount" columns, just like in a regular Cash Disbursements Journal.

A separate Payroll Journal should be used for each checking account.

(Note: refer to page 8 for a discussion of payroll concepts.)

EXAMPLE: The parish secretary receives a paycheck for $391.75. Her gross pay is $500. The withholdings are: federal=$50 state=$20 Social Security=$31 Medicare=$7.25.

The gross pay of $500 has to show up as secretary salary. The various payroll withholdings are then listed as reductions of the gross amount. The entry is the Payroll Journal is:

| Date | Check # | Payee | Acct | Amount | Federal Withheld | State Withheld | S.S. Withheld | Medicare Withheld | Medical Withheld | Check Amount |
|---|---|---|---|---|---|---|---|---|---|---|
| 2/15 | 1598 | Joanne Smith | 5230000 | 500.00 | 50.00 | 20.00 | 31.00 | 7.25 | | -391.75 |

Note that only the amount of the check receives a negative sign. The amount of the check is a reduction of the checking account. Although the various withholdings decrease the amount of the check, they increase the amount of the withholding liability. Therefore they do not receive negative signs.

EXAMPLE: The janitor receives a paycheck for $391.75. His gross pay is $500, and is split as follows: 20% rectory, 40% church, 40% RE building. The withholdings are: federal=$50 state=$20 Social Security=$31 Medicare=$7.25.

| Date | Check # | Payee | Acct | Amount | Federal Withheld | State Withheld | S.S. Withheld | Medicare Withheld | Medical Withheld | Check Amount |
|---|---|---|---|---|---|---|---|---|---|---|
| 2/15 | 1599 | Duane Larson | 5353000 | 100.00 | 50.00 | 20.00 | 31.00 | 7.25 | | -391.75 |
| | | | 6353000 | 200.00 | | | | | | |
| | | | 7353000 | 200.00 | | | | | | |

Periodically (either monthly or quarterly), the payroll taxes are paid to the appropriate agency. For FICA taxes, the parish must match the amount withheld from an employee's paycheck. That matching amount is recorded as an expense. The payment of these taxes is recorded in the Cash Disbursements Journal.

EXAMPLE: The parish pays Hometown Bank the amounts withheld from employees' checks for federal tax and FICA. Federal tax withheld amounts to $100 and FICA withheld is $76.50. The parish writes out check 4843 for $253 ($100 federal + $62 employees' Social Security + $62 employer's matching Social Security + $14.50 employees' matching Medicare + $14.50). The entry in the Cash Disbursements Journal is:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 3/2 | 1635 | Hometown Bank | Fed Tax Witheld | 2131000 | -100.00 |
| | | | Employees’ SS | 2133000 | -62.00 |
| | | | Employer’s SS | 5280000 | 62.00 |
| | | | Employees’ Medicare | 2134000 | -14.50 |
| | | | Employer’s Medicare | 5282000 | 14.50 |

The entries to the liability accounts have negative signs because they are reducing the amount owed for these liabilities. The expense item is positive because the amount of the expense is being increased.

# GENERAL JOURNAL

The General Journal is used to record entries that do not fit into the other two journals. Examples of transactions that would be recorded in the general journal include corrections of errors and voided checks.

A sample General Journal is pictured below:

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| | | | | | |
| | | | | | |
| | | | | | |

Date: the day the transaction occurred

Ref #: the reference number of the transaction. Entries are numbered sequentially starting with number 101 each month. This number is used to reference a specific transaction (e.g. I have a question about entry 102 in the December general journal).

Description: a brief description of the entry

Acct #: the number of the account affected by the transaction

Debit: the dollar value of the account being debited

Credit: the dollar value of the account being credited

General Journals are a little more difficult to work with because they are based on debits and credits, where the other journals are based on increases and decreases. See page 5 for an explanation of debits and credits.

To see sample transactions using the General Journal, refer to the section on Special Bookkeeping Issues, starting on page 25.

# BANK RECONCILIATION

The bank reconciliation form is used to verify the balances of cash accounts. The report aims to reconcile the balance on the bank statement with the amount recorded on the balance sheet. A bank reconciliation must be filled out for the checking account, and it is recommended that a reconciliation is done for every bank account. A sample bank reconciliation form appears on page 24.

The process for completing a bank reconciliation is detailed below.

1. The parish receives the bank statement. The ending balance on the bank statement is recorded as the Balance per Bank Statement.
2. Any "deposits in transit" are recorded in the appropriate section. A deposit in transit is a deposit that has been recorded in the Cash Receipts Journal but does not appear on the bank statement.
3. The "outstanding checks" for the month are listed on the right-hand side of the form. An outstanding check is a check or other reduction that is recorded in the Cash Disbursements Journal or Payroll Journal but does not appear on the bank statement. Also check to see if the outstanding items from the previous month have cleared the bank this month; if they have not, they should be recorded as outstanding this month also.
4. The amount of outstanding checks is totaled, and this total is recorded in the appropriate section on the left-hand side of the form.
5. The Reconciled Bank Statement Balance is computed. This number is the Balance Per Bank Statement plus the total Deposits in Transit less the total Outstanding Checks.
6. The Beginning Balance Per Books is recorded on the appropriate line. This number is the Reconciled Balance from the previous month's Bank Reconciliation.
7. The Cash Receipts Journal total for this account is recorded.
8. Any other increases to this account are recorded. These are items that appear on the General Journal.
9. The additions to the account are totaled and recorded in the appropriate spot.
10. The Cash Disbursements Journal total for this account is recorded.
11. The total of the "Check Amount" column of the Payroll Journal for this account is recorded.
12. Any other decreases to this account are recorded. These are items that appear on the General Journal.
13. The withdrawals from the account are totaled and recorded in the appropriate spot.
14. The Reconciled Book Balance is computed. This amount is the Beginning Balance Per Books plus the Total Additions less the Total Withdrawals.
15. The Reconciled Bank Statement Balance should equal the Reconciled Book Balance.

If the two balances are not equal, there are a number of possible errors to look for. Recompute all the numbers to make sure the math is right. Review the deposits in transit and outstanding checks to see if any were missed, including outstanding items from previous months that still have not cleared, and that the correct amounts were recorded for all outstanding items. Also look for automatic charges or deposits such as service charges or interest that are on the bank statement but were not recorded in the journals. Look for discrepancies between transaction amounts on the bank statement and the journals, such as a check recorded as $9.83 on the bank statement but $9.88 on the Cash Disbursements Journal.

# Bank Reconciliation

Parish Name ____________________________ Parish Number _____________

For the Month of ____________________________________

_____________________________________________

Balance per Bank Statement _____________

<u>Add:</u>

Deposits in Transit _____________

_____________

Total Deposits in Transit _____________

<u>Less:</u>

Outstanding checks _____________

Reconciled Bank Statement Balance _____________

__________________________________________________

Balance Per Books-Beginning _____________

<u>Add:</u>

Receipt Journal ___________

Other ___________

___________

Total Additions _____________

<u>Less:</u>

Disbursements Journal ___________

Payroll Journal ___________

Other ___________

___________

Total Subtractions _____________

Reconciled Balance Per Books _____________

Outstanding Checks

| Check | Amount |
|---|---|
| | |
| | |
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# Special Bookkeeping Issues

## Recording Multi-Facility Payments

Some bills contain charges that relate to more than one facility. For example, the electric bill may include charges for electricity used in the church, rectory, and religious education facilities. The totals of these bills must be divided between these facilities to accurately record the expenses of each facility. Also, a facility may be used for more than one purpose; for example, the church basement may be used for religious education. The charges for the church should then be divided between Church (Worship) and Education Facility expenses.

Some bills may be easily traced to the facilities based on use; if each building has its own meter, electricity charges could be distributed based on actual usage. If this is not the case, the parish will need to decide how to split the charges between the facilities/purposes. A percentage based on actual use is best. For example, if the church is used for RE 15% of the time, Education Facilities should be charged with 15% of the facility charges for the church. When a bill is paid, the percentages are applied to the total amount of the bill to find the portion allocated to each facility. This amount is then charged to the appropriate account.

SAMPLE ENTRY: Check 654 is issued on January 20 to NSP for payment of a $100 electric bill. The percentages for each facility, based on use, are: rectory = 40% church = 40% religious education facility = 20%. The entry in the Cash Disbursements Journal is:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 1/20 | 654 | NSP | rectory elect | 5311000 | 40.00 |
| | | | church elect | 7311000 | 40.00 |
| | | | rel ed elect | 6311000 | 20.00 |

## Allocation of property and liability coverage charges

The Diocese currently has its multi-peril coverage with the Catholic Mutual Group. Each year the parish receives a charge from the Diocese to pay for this insurance. The premium is divided into two parts: property coverage and liability coverage. Property coverage covers damage to the parish's property, such as wind damage or vandalism. Liability coverage covers people injured on parish property. When these premiums are recorded, it is the bookkeeper's responsibility to allocate these charges among the buildings owned by the parish.

Property coverage charges are charged to the buildings the parish owns. Each year the parish receives a ledger page for their location (this is sent out with the bill from the diocese). The ledger page lists the buildings owned by the parish, the type of coverage for each building (replacement cost, actual cash value, agreed amount, or liability only), and the cost of the coverage for that building. When the property insurance is paid, the total cost should be divided based on the amounts on the ledger page.

Liability charges are not based on the value of the buildings, but are instead charged to the parish as a whole. The charge then needs to be allocated between the buildings owned by the parish. The parish can use any method of allocation that seems logical. The amount of use is usually the best factor to consider; the more a building is used, the higher the chance an accident will occur there. Therefore, a building that has many people using it, such as a church, should receive a higher percentage of the liability charge than a building that experiences a low volume of traffic, such as a rectory or garage.

Parishes who share a priest may be sharing all expenses associating with the rectory. In this situation, the property charge for the rectory may be shared among the parishes since it is a cost of that building. However, the liability charge should not be a shared expense in this setting because it is a cost of the parish and not a specific building.

## Expenses Shared With Other Parishes

Parishes sometimes receive reimbursements from other parishes, usually mission, for bills paid on their behalf. There are two different methods available to handle these transactions, based upon the agreement between the parishes.

To demonstrate the various methods, we will use the following example: Parish 1 has two missions, Parish 2 and Parish 3. Parish 1 is allocated 50% of shared expenses, and the remaining 50% is divided evenly between the two missions. Parish 1 pays priest's salary of $1000. Parish 3 reimburses Parish 1 $250 on December 3.

<u>Method 1: The Receivable Method</u>

This method is used when the mission parish reimburses the head parish for specific expenses paid by the head parish. The mission parishes will periodically receive a bill from the head parish for their share of actual expenses paid by the head parish. Using the example above, Parish 1 would pay the pastor $1000, and Parish 2 and Parish 3 would each reimburse Parish 1 for their share (25%) of the total cost.

The head parish will record the missions' share of each payment in a receivable account at the time of the transaction. The receivable is an asset account because it represents an amount that the parish will receive in the future. Only the portion allocated to the head parish is recorded as an expense. When the mission reimburses the parish, this is recorded as a reduction to the receivable.

EXAMPLE: Parish 1 pays priest's salary of $1000.

Cash Disbursements Journal

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 11/20 | 2510 | Fr. Smith | priest salary | 5110000 | 500.00 |
| | | | | 1161000 | 250.00 |
| | | | | 1162000 | 250.00 |

Parish 1 receives $250 from Parish 3 as reimbursement for expenses. The entry is made in the Cash Receipts Journal.

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 12/3 | Received from Parish 3 | 3 | 1162000 | (250.00) |
| | Checking Account | 4 | 1110000 | 250.00 |

Note that entry 3 is in parenthesis because the entry is reducing the amount receivable from Parish 3.

This method provides an accurate picture of the actual expenses of the parish since only the parish's share of expenses appears on its income statement. The amount that the mission parishes owe appears on the head parish's balance sheet as a receivable.

Method 2: The Revenue Method

This method is used when a mission pays a set amount per month to the head parish. The head parish is in effect "providing a service", and the mission is the "customer" paying for that service. All expenses are fully expensed to the head parish. When money is received from the mission, it is treated as payment for services performed and is recognized as revenue.

EXAMPLE: The priest's salary is expensed entirely to Parish 1.

Cash Disbursements Journal

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 11/20 | 2510 | Fr. Smith | priest salary | 5110000 | 1000.00 |

When Parish 1 receives money from Parish 3, this amount is recorded as revenue in the Cash Receipts Journal.

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 11/29 | Received from Parish 3 | 30 | 4552000 | 250.00 |
| | checking account | 31 | 1110000 | 250.00 |

This method could lead to a material misstatement on the financial statements if the mission parish falls behind on their payments. If one of the missions owes a substantial amount of money to the head parish, both parishes may want to record the obligation on their financial statements.

## PAYROLL

It is strongly recommended that all paychecks be recorded in the Payroll Journal (see page 18). If for some reason the bookkeeper does not want to use a Payroll Journal, paychecks can be recorded in the Cash Disbursements Journal.

EXAMPLE: The parish secretary receives a paycheck for $391.75. Her gross pay is $500. The withholdings are: federal=$50 state=$20 Social Security=$31 Medicare=$7.25.

The gross pay of $500 has to show up as secretary salary. The various payroll withholdings are then listed as reductions of the gross amount. The entry in the Cash Disbursements Journal is:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 2/15 | 1598 | Joanne Smith | payroll | 5230000 | 500.00 |
| | | | | 2131000 | 50.00 |
| | | | | 2132000 | 20.00 |
| | | | | 2133000 | 31.00 |
| | | | | 2134000 | 7.25 |

Note that none of these amounts receive a negative sign. Although the various withholdings decrease the amount of the check, they increase the amount of the withholding liability. Therefore they do not receive negative signs.

Periodically (either monthly or quarterly), the payroll taxes are paid to the appropriate agency. For FICA taxes, the parish must match the amount withheld from an employee's paycheck. That matching amount is recorded as an expense. The payment of these taxes is recorded in the Cash Disbursements Journal.

EXAMPLE: The parish pays Hometown Bank the amounts withheld from employees' checks for federal tax and FICA. Federal tax withheld amounts to $100 and FICA withheld is $76.50. The parish writes out check 4843 for $253 ($100 federal + $62 employees' Social Security + $62 employer's matching Social Security + $14.50 employees' matching Medicare + $14.50). The entry in the Cash Disbursements Journal is:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 3/2 | 1635 | Hometown Bank | Fed Tax Witheld | 2131000 | -100.00 |
| | | | Employees' SS | 2133000 | -62.00 |
| | | | Employer's SS | 5280000 | 62.00 |
| | | | Employees' Medicare | 2134000 | -14.50 |
| | | | Employer's Medicare | 5282000 | 14.50 |

The entries to the liability accounts have negative signs because they are reducing the amount owed for these liabilities. The expense item is positive because the amount of the expense is being increased.

## In-Out (Custodial) Accounts

A custodial account is a liability account used for money the parish receives in a custodial capacity: the parish collects money for some other entity, then turns the money over to that entity. These accounts are often referred to as in-out accounts because the money flows "in and out" of the parish. Custodial accounts in the parish chart of accounts include the Diocesan Special Collection accounts and the In-Out account.

The main custodial transactions at the parish level deal with Diocesan special collections. These are special collections that are taken up at certain points throughout the year to help fund special ministries or needs. The parish collects the money from its parishioners during the collection, then sends the money to the Diocese, who in turn forwards it to the appropriate agencies.

SAMPLE TRANSACTION: The parish collects $230 for the Propagation of the Faith collection on October 21. This money is sent in to the Diocese on November 10.

Cash Receipts Journal

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 10/21 | Propagation of the Faith | 20 | 2513200 | 230.00 |
| | checking account | 21 | 1110000 | 230.00 |

This entry establishes a liability to the Diocese for the amount collected. The payment of the liability is shown in the next entry. Note that the amount is negative because it is a reduction of the amount owed.

Cash Disbursements Journal

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 11/10 | 516 | Diocese of Crookston | spec. collect | 2513200 | (230.00) |

Custodial transactions other than special collections are recorded in the In-Out Account. One example is a youth group event such as a ski trip where the participants would pay money to the parish for tickets, and the parish would take the money collected and buy tickets.

There are two important things to remember about custodial accounts. First, the amount disbursed MUST be equal to the amount received. If there is a discrepency, a revenue or expense must be recorded. If a parish sends in more money for a special collection than was received from the parishioners, the excess must be recognized as Special Collection Expense.

The other important thing to remember is that these accounts are for custodial transactions only. If the money is given to the parish to be used for parish use, it is a revenue and should not be entered in the In-Out Account. One common error arises when someone donates money to the parish for a specific purpose, such as purchasing hymnals. Since the amount of the donation and the amount of the item purchased are the same, some bookkeepers are tempted to record this transaction in the In-Out Account. However, the money is being donated to the parish and should be recorded as a revenue. The item purchased is being purchased for the use of the parish and should be recorded as an expense.

## Petty Cash

Petty cash is an on-hand account that can be set up to cover small expenses. A small amount of cash is put into petty cash, which is kept in a drawer or box. This money is used to cover small expenses, such as stamps, instead of writing out a check. A record is kept of the money spent; either a voucher system, where a voucher is prepared for each withdrawal, or a simple list of who took money and what it was used for. Periodically, the petty cash is replenished. The total of the vouchers or disbursement list is computed and is compared to the amount remaining in the petty cash drawer. Money is put into the petty cash to bring it up to its original balance.

The following entries are made to maintain a petty cash account.

July 1: Check 515 is issued for $50 to establish the petty cash account.

This entry is made in the Cash Disbursements Journal. The account used is 1115000, the petty cash account. The cash is set aside in a locked drawer or box.

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 7/1 | 515 | Cash | establish petty cash | 1150000 | 50.00 |

When cash is taken out of petty cash, no entry is made. A record is kept of who took the cash and why it was taken.

July 10: The petty cash account is replenished. Totaling the vouchers results in the following figures: postage = $30 office supplies = $10. Check 531 is issued for $40 to bring petty cash up to its original total of $50.

The entry is made in the Cash Disbursements Journal. The account numbers used are the numbers for the expenses, NOT the petty cash account number. The petty cash account is currently recorded on the parish books at $50; this entry is simply restoring the fund to this amount. The petty cash account number is only used if you are increasing the base amount of the petty cash.

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 7/10 | 531 | Petty Cash | postage | 5530000 | 30.00 |
| | | | office supplies | 5510000 | 10.00 |

If the amount in the cash drawer is less than what should be on hand, this is called a cash short. If the cash drawer has more cash than it should, this is referred to as a cash over. Any amount short or over is recorded in 5904000, an expense account. If this account has a positive balance, that indicates a cash short; a negative balance indicates a cash over.

July 10: Everything is the same as the previous entry, so the amount of cash in the petty cash account should be $10 ($50 beginning balance - $30 postage - $10 office supplies). When the cash is counted, however, the amount is only $6. Thus, the check is written out for $44, the amount necessary to bring the total back to $50. Assuming that the reason for the discrepancy cannot be found, the entry is:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 7/10 | 531 | Petty Cash | postage | 5530000 | 30.00 |
| | | | office supply | 5510000 | 10.00 |
| | | | cash short | 5904000 | 4.00 |

July 10: Everything is the same as the previous entry, but the cash balance in the account is $14 instead of $6. Assuming that the reason for the discrepancy cannot be found, the entry is:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 7/10 | 531 | Petty Cash | postage | 5530000 | 30.00 |
| | | | office supply | 5510000 | 10.00 |
| | | | cash over | 5904000 | (4.00) |

July 31: It is decided that the amount in petty cash is too small. The total amount is raised to $90. Check 560 is issued for $40.

Since the total of petty cash is being increased, the petty cash account is used for the entry in the Cash Disbursements Journal:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 7/31 | 560 | Petty Cash | increase petty cash | 1150000 | 40.00 |

Control is very important when dealing with petty cash. Since it involves cash, loss due to theft or carelessness can easily occur. A limited number of people, preferably only one or two people, should be in charge of petty cash. The money should be kept in a locked box, with only one or two people having keys. Every withdrawal should be recorded when the cash is taken. See the section on internal controls for more information on petty cash security.

## Accrual Accounting

Although the Parish Accounting System is primarily a cash-based system, parishes may wish to accrue some items. This would be done to record the expenses when they are incurred, instead of when they are paid. Any bill that is still outstanding at the end of the period can be accrued. The parish should consider accrual for large bills that will not be paid for many months. The parish may want to consider accrual for items that will span fiscal years.

If the parish has a significant bill that will not be paid off within a short amount of time (a couple months or more), accrual should be considered. This will record the expense in the period it occurred, and also recognize the unpaid balance as a liability. As an example, let's look at the Diocesan billing, which is received monthly by the parish. On a cash basis, the expenses charged on this bill are not recorded until they are paid. If the unpaid balance gets large and is outstanding for a long period of time, the financial statements can become misleading. The parish may appear to be in great shape because it has a positive net income, but it may have $10,000 of unrecorded expenses and an unrecorded liability to the Diocese. When this bill is finally paid, which may not occur until the next fiscal year, the parish may show a large loss because many months' worth of charges are being expensed at once. The bookkeeper will also have to go through many months' worth of statements to determine what the outstanding balance consists of and which expenses need to be charged for this payment. Accruing these bills will have two benefits: 1) the expense will be recorded in the proper period and 2) the liability will be recorded on the balance sheet.

Expenses that are unpaid at the end of the fiscal year may also be accrued. If these expenses are not accrued, the expense will not show up until the next fiscal year.

A General Journal entry is done to accrue an expense. The entry is identical to the entry that would be done when the bill is paid, except that a payable account will be used instead of cash. Accrual entries can be charged to Accounts Payable, or a special payable can be set up if the item is recurring.

Example: The parish receives the monthly statement from the Diocese. On the bill are the following charges: assessment=$500 priest's health insurance=$200 priest's life\ltd insurance=$15.

General Journal

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 10/01 | 102 | Accrue amounts owed to Diocese | 5912000 | 500.00 | |
| | | | 5192000 | 200.00 | |
| | | | 5192000 | 15.00 | |
| | | | 2191000 | | 715.00 |

The above entry would be made every month when the parish receives their bill. Assuming the parish had been paid in full prior to this billing, the balance sheet would show a $715 liability to the Diocese.

When this amount is paid, the liability account will be reduced. This amount is in parenthesis, because it is a reduction of the amount owed.

Cash Disbursements Journal

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 11/27 | 905 | Diocese of Crookston | pay balance | 2191000 | (715.00) |

## Transfer of Amounts Between Asset Accounts

Transfers between accounts occur when money is moved from one account to another. To demonstrate these entries, we will record a transfer of $1000 from the savings account to the checking account.

The transfer can be recorded in one of three places:

General Journal

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 11/01 | 101 | Transfer from savings to checking | 1110000 | 1000.00 | |
| | | | 1120000 | | (1000.00) |

The Cash Receipts Journal of the account the deposit is being made into.

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 11/01 | Transfer from Savings to Checking | 20 | 1120000 | (1000.00) |
| | | 21 | 1110000 | 1000.00 |

Or the Cash Disbursements Journal of the account the money is being transferred from.

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 11/01 | | Transfer to Checking | | 1111000 | 1000.00 |

The transfer can be recorded in any of these journals, but make sure that the transaction is only recorded once!!

## Correction of Errors

One common error that is made is recording the wrong dollar amount for a transaction. This is normally due to a transposition error or a math error. However, these errors are usually caught and corrected immediately, since they result in the journal being out of balance.

The most common error that needs to be corrected with a journal entry is a coding error, a transaction that has been recorded in the wrong account. To correct a coding error, an entry would be made to reverse the incorrect entry and record the amount in the proper account.

EXAMPLE: Check 226, written to Chris's Plumbing for repair work at the rectory, was incorrectly coded to Church Repairs and Maintenance.

When this check was written, Church Repairs and Maintenance was incorrectly debited. The correcting entry in the General Journal would cancel the incorrect entry by crediting Church Repairs and Maintenance. The correct account, Rectory Repairs and Maintenance, would be debited.

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 4/30 | 101 | Correct error made on check 226 | 5351000 | 50.00 | |
| | | | 7351000 | | (50.00) |

## NSF and Voided Checks

If the parish deposits a check then has it returned because of non-sufficient funds, an entry is made in the General Journal to reverse the entry made when the check was deposited. The credit goes to the asset account the check was originally deposited into. The debit goes to the other account used when the check was received. If a check for $10 from an adult envelope contribution was returned, the entry would be:

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 2/14 | 101 | To record NSF check | 4111000 | (10.00) | |
| | | | 1110000 | | (10.00) |

If a parish writes a check and records it in the Cash Disbursements Journal, then has to void that check, an entry would be made in the General Journal that would reverse the original transaction. The asset account the check was written out of would be debited. The other account(s) used in the entry would be credited.

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 4/12 | 101 | Void check 4586 | 1110000 | 450.00 | |
| | | | 6710000 | | (450.00) |

## Loans

Occasionally the parish will borrow money from a bank, the diocese, or parishioners. Borrowing money creates an obligation on the part of the parish to repay the money. This is shown by using a liability account.

Cash Receipts Journal

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 1/25 | Loan proceeds from bank | 15 | 2211000 | 10,000.00 |
| | | 16 | 1110000 | 10,000.00 |

Payments made on the loan have two components: an interest payment and a principal payment. The interest payment is an expense of the parish. The principal payment reduces the balance of the loan, and is charged to the liability account.

Cash Disbursements Journal

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 2/15 | 5133 | Hometown Bank | Loan Payment-principal | 2211000 | 100.00 |
| | | | Loan Payment-interest | 5920000 | 50.00 |

# Financial Statements

There are two financial statements that a parish should produce at the end of each month: the balance sheet and the income statement. If the parish submits reports on a monthly basis to the Office of Parish Administration, that office will produce these reports. If a parish handles its own bookkeeping, it will use its accounting program to produce these reports.

In addition to the two main reports, there are two other reports that are produced by the Parish Accounting Office, the trial balance and the general ledger. A parish that is doing their own bookkeeping does not need to print these reports, but might find them useful.

All four reports are described below.

## Balance Sheet

The balance sheet is a report of the parish's assets, liabilities, and fund balance as of a certain date. The balance sheet is also known as the statement of financial position.

By looking at this report, you can see the amount of cash the parish has in its various bank accounts. You can also see the liabilities of the parish. The net income for the current fiscal year is usually reported in the fund balance section of the balance sheet.

The balance sheet produced by the Parish Accounting Office shows the balances for the current month, the previous month, and one year ago; this allows you to see the change in assets and liabilities over the past month and year. A sample balance sheet is shown on page 37.

## Income Statement

The income statement is a list of the revenues and expenses of the parish for a specific time period, usually a month. It is also known as the income and expense statement, profit and loss statement, or the statement of financial activity. An income statement is shown on page 38.

The income statement produced by the Parish Accounting Office shows the following information:

- Total for the current month
- Total for the current fiscal year-to-date
- Previous fiscal year-to-date
- Budget amounts
- The percent of the budgeted amount remaining

This statement provides a wealth of useful planning and control information. A parish can tell how much it is spending or receiving in certain areas, and what the parish's net income is for the month and the fiscal year.

The comparison information is also very important. Knowing that the parish has $50,000 in adult envelope revenue is important, but also needs to be considered in context. This amount should be compared to both the budget and the previous year's total to determine how the parish is doing financially.

## Trial Balance

The trial balance is a list of all accounts, their beginning and ending balances, and the net change in their balances during the month. The main purpose of the trial balance is to ensure that debits equal credits. The Parish Accounting Office only sends this report out if the bookkeeper requests it, since this same information is presented in a more expanded form on the general ledger.

## General Ledger

The general ledger is a printout of the transactions for the month, grouped by account. For each account in the chart of accounts it shows the beginning balance, a list of all transactions that occurred in that account for the month, and the ending balance. A section of the general ledger showing the checking account is shown below. Looking at this report, you can see how the balance in an account changed and what transactions caused that change.

| | | | | |
|---|---|---|---|---|
| 1110000 Checking Account | | | Beginning Balance | 21,000.00 |
| Deposit to Checking | 10/09 | 800.00 | | |
| Deposit to Checking | 10/16 | 1300.00 | | |
| Deposit to Checking | 10/23 | 1700.00 | | |
| Deposit to Checking | 10/30 | 1500.00 | | |
| Total Cash Disbursements | 10/31 | -5000.00 | | |
| 1110000 Checking Account | | | Ending Balance | 21,300.00 |

This report is a valuable supplement to the balance sheet and income statement because it groups transactions by account. If the income statement figure for Repairs and Maintenance Expense seems too high, a quick look at the general ledger will show a breakdown of the expenses for that account.

The general ledger is also useful for finding coding errors. By reviewing the general ledger, you can quickly find entries that were recorded in the wrong account. For example, if you look under Adult Envelopes and find an entry labeled loose plate, this is an obvious error. The bookkeeper should go over this report carefully every month.

Balance Sheet as of 08/31/1998
3: Cemetery Fund

| | | Current Month | Prior Month | Prior Year |
|---|---|---|---|---|
| | Assets | | | |
| 1310000 | Checking Account | 0.00 | 0.00 | 0.00 |
| 1320000 | Savings Account | 0.00 | 0.00 | 0.00 |
| 1330000 | CD's | 0.00 | 0.00 | 0.00 |
| 1340000 | CCF Account | 0.00 | 0.00 | 0.00 |
| | Total Assets | 0.00 | 0.00 | 0.00 |
| | Liabilities/Fund Balance | | | |
| | Liabilities | | | |
| | Notes Payable | | | |
| 2311000 | Notes Owed to Bank | 0.00 | 0.00 | 0.00 |
| 2312000 | Notes Owed to Diocese | 0.00 | 0.00 | 0.00 |
| 2314000 | Notes Owed/Parishoners | 0.00 | 0.00 | 0.00 |
| 2319000 | Notes Owed to Others | 0.00 | 0.00 | 0.00 |
| | Total Notes Payable | 0.00 | 0.00 | 0.00 |
| | Total Liabilities | 0.00 | 0.00 | 0.00 |
| | Fund Balance | | | |
| 3100000 | Fund Balance | 0.00 | 0.00 | 0.00 |
| 3600000 | Revenues over Expenses | 0.00 | 0.00 | 0.00 |
| | Total Fund Balance | 0.00 | 0.00 | 0.00 |
| | Total Liab./Fund Balance | 0.00 | 0.00 | 0.00 |

Income Statement as of 08/31/1998

2: Capital Fund

| | | Current Month | Current YTD | Prior YTD | Budget | Percent | Remaining |
|---|---|---|---|---|---|---|---|
| | Revenues | | | | | | |
| 4610000 | Donations | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| 4620000 | Interest Income | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| 4630000 | Building Collection | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| 4640000 | Fund-Raisers | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| 4650000 | Grants | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| 4660000 | Gain on Sale of Assets | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| 4680000 | Transfer from Other Funds | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| | Total Revenues | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| | Expenses | | | | | | |
| 9210000 | Fund-Raising Costs | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| 9220000 | Interest Expense | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| | Depreciation Expense | | | | | | |
| 9231000 | Depreciation Exp-Bldgs | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| 9235000 | Depreciation Exp-Equipmnt | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| | Ttl Depreciation Expense | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| 9260000 | Loss on Sale of Assets | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| | Total Expenses | 0.00 | 0.00 | 0.00 | 0.00 | 0.0 | 0.00 |
| | | | | | Revenue over Expense | | 0.00 |

# Section 3: Fund Accounting

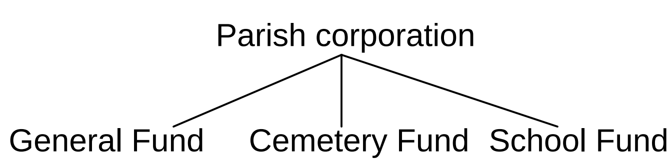
## What is Fund Accounting?

Fund accounting is a theory unique to non-profit accounting. It allows the non-profit organization to divide its financial statements into funds to keep track of different aspects of its organization. Under a fund accounting system, separate funds are set up to account for different aspects of parish activity.

Think of the many activities a parish could be performing. There are the everyday activities of the parish, such as running education classes and holding mass. The parish must acquire capital assets such as buildings and equipment to carry out these functions. The parish may also have a cemetery to take care of and a school to run. Each of these functions needs to be kept separate in order to be managed correctly; how can you determine the financial health of the school if its activities are not kept separate from other parish functions? A Fortune 500 corporation would form departments to handle these different functions. Each department would be a part of the corporation, but would keep track of its own assets, liabilities, revenues, and expenses. The parish corporation can create separate funds to handle these items. Funds, then, can be thought of as "subsidiaries" or "departments" of the parish.

An example will demonstrate the usefulness of funds. Say that a parish reports a net income of $50,000 for the year, and has $220,100 in assets on their balance sheet. Sounds like the parish is in good shape, right? But the parish is currently raising money to build a new rectory, and raised $60,000 that year for the building project. When you remove that income from consideration, the parish is left with a net loss of $10,000 on their regular operations. And that $220,100 in assets doesn't seem quite as impressive when you realize that $220,000 is restricted for the building project, and the parish only has $100 on hand to pay the regular bills! Fund accounting would clarify this situation by reporting the building project transactions in a separate fund. The Capital Fund would report $220,000 of assets and $60,000 of net income, while the financial statements for the General Fund would show a net loss of $10,000 and $100 in assets.

There are a number of different funds a parish may want to establish. The General Fund is used to keep track of the normal day-to-day operations of the parish, such as offertory income and the religious education program. The Capital Fund accounts for the acquisition of capital assets such as land, buildings, and equipment. The Cemetery Fund handles all transactions involving the cemetery. The Endowment Fund handles the parish's endowments. The Custodial Fund keeps track of money the parish receives that is to be forwarded to another organization, such as diocesan special collections. The School Fund keeps track of the day-to-day operation of the parish school. Parishes may also want to set up funds to keep track of large religious education programs, hot lunch programs, or anything else that involves restricted money or is not part of the general operating activities of the parish.



Each fund has its own chart of accounts and its own set of financial statements. For a cemetery fund, the balance sheet would show assets available only for use by the cemetery fund. This recognizes the fact that these assets are restricted in nature. All liabilities related to the cemetery would also be shown on the balance sheet. The income statement would show only cemetery-related revenues and expenses, such as money from lot sales and grounds upkeep expenses.

It is recommended that parishes set up multiple funds as needed. However, there is no requirement to do this. The Master Chart of Accounts is set up to allow parishes to operate with either a single fund or multiple funds. If the parish only uses a single fund, the chart of accounts will have separate sections for transactions that would normally be recorded in separate funds. The restricted items are still kept somewhat separate, but not to the degree that they are in a multi-fund system.

## Why Use Multiple Funds?

The advantage of using multiple funds is that it allows a parish to keep special operations separate from the general operations of the parish. The construction of a new church gives rise to large revenues and expenditures that, if recorded with other parish operations, would make it difficult to determine how the parish is doing on a day-to-day basis. Under fund accounting, the construction project would show up in a different fund, separate from the regular operations of the parish.

Fund accounting can also be used to highlight restrictions on assets. Money placed in an endowment cannot be spent; its only purpose is to generate revenue. This can be emphasized by placing the endowment in it own fund and keeping it separate from the general assets of the parish.

## Commonly-Used Funds

A parish should set up funds for anything it thinks should be kept separate from its general operations. The following commonly-used funds are discussed in the sections below: General Fund, Capital Fund, Cemetery Fund, Endowment Fund, Custodial Fund, and School Fund.

## The Checking Account

It is recommended that the parish set up a separate checking account for each fund. It may seem like extra work at first, but it will make things much less complicated in the long run.

If the parish has only one checking account, the balance of that account could be split up among three different funds. The bookkeeper would need to keep track of how the checking account is allocated among each fund. A checking account with a $5000 balance may show up as $2500 in the General Fund, $1200 in the Capital Fund, and $1300 in the Cemetery Fund. Having a separate checking account for each fund would eliminate this.

Transfers between funds will also be less complicated with multiple checking accounts. Assume that the Capital Fund needs an extra $3000 to buy a new piece of equipment. If there are multiple checking accounts, the parish does a transfer from one account to the other. If there is only one checking account, the bookkeeper must do a

General Journal entry to record a transfer from one fund to another, even though no money is actually moving. Transfers between funds are covered on page 46.

## Note about Fund Account Numbers

Each fund has a fund number associated with it. The General Fund is Fund 1, the Capital Fund is Fund 2, the Cemetery Fund is Fund 3, and so on. When the parish has more than one fund, the fund number should be included in the account number. The checking account in the General Fund would be 1-1110000, the Capital Fund checking would be 2-1210000, the Cemetery checking account would be 3-1310000, and so on.

## The General Fund

The General Fund handles the day-to-day operations of the parish. Sunday collections, donations, and payments of regular expenses go here. All assets available for general use are recorded here. If one of the other funds needs more cash, the money normally comes out of this fund.

Restricted funds can appear as assets in the General Fund if they are restricted for general operating purposes. A $10,000 grant restricted for use in the religious education program would show up in the General Fund because the money is being used to pay for religious education, which is part of the regular operations of the parish.

If the parish has only one fund, all transactions are recorded here, including cemetery transactions and building projects. Under no circumstances are capital assets (land, buildings, and equipment) recorded here. If the parish wants these assets recorded, a Capital Fund must be established.

## The Capital Fund

The Capital Fund is used to keep track of capital assets owned by the parish. Land, buildings, and equipment are recorded in this fund. Depreciation on these assets is also recorded here. Money set aside for the purchase of these assets belongs in the Capital Fund.

The biggest difference between this fund and the General Fund is that acquisitions of assets are capitalized. That means that the value of the item is set up as an asset, and the cost is expensed over the lifetime of the object. If the parish does not have a capital fund and purchases a computer for $2000, it would record an expense of $2000. If the parish has a capital fund, it would not record any expense for this purchase. Instead, it would record a capital asset of $2000. The cost would then be divided over the lifetime of the asset through depreciation; for the computer, the parish might record Depreciation Expense of $400 a year for 5 years.

The income/loss numbers for this fund may seem deceiving because it is a departure from the cash basis that is used in the rest of the accounting system. A parish may collect $500,000 in building donations and spend $600,000 to build a new church. Under cash basis accounting, this would result in a net loss of $100,000. But the capital fund would show a $500,000 net income. The $600,000 spent on the new church is recorded as an asset, not an expense.

The parish will need to set a policy establishing which assets should be capitalized. Obviously any buildings and land owned by the parish would be capitalized. A parish car would be too. But what about the overhead projector or the new phone in the parish office? The two main factors to consider are cost and expected useful life. The parish may decide that any asset with a value of at least $500 and an expected useful life of at least 5 years will be capitalized. Use discretion though; a purchase of $1000 worth of paper clips would not be capitalized, even though they may last 10 years. (The Diocese of Crookston uses the following standard for its Capital Fund: "Only furnishings and equipment costing more than $250 are carried as assets.")

All acquisitions of capital assets are recorded in this fund. This includes acquisition by purchase, donation, and construction. All assets are recorded at cost. If a cost is not determinable (such as a donated asset), the item is recorded at fair market value on the day the asset was received. Any debt associated with these acquisitions is also recorded here. Revenues for this fund come from four main sources: special collections and other donations, grants, interest, and gains on the sale or conversion of assets. Expenses include interest paid on loans, losses on the sale or conversion of assets, and depreciation.

Most of the bookkeeping for a Capital Fund is similar to the General Fund. A donation to the Capital Fund is recorded in the same way as a donation to the General Fund. Special transactions relating to the Capital Fund are described below.

Recording a New Asset

The parish buys a new car for $10,000. The transaction in the Cash Disbursements Journal for the Capital Fund is:

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 5/15 | 5454 | Sullivan Motors | Purchase car | 2-1275000 | 10,000.00 |

If the car was received as a donation, the value of the car should be recorded as revenue for the parish. The value of the car would be the fair market value on the day the car was donated. The following entry would be made in the General Journal:

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 5/15 | 101 | New car donated | 2-1275000 | 10,000.00 | |
| | | | 2-4610000 | | 10,000.00 |

If the parish was building a new church, the parish would charge all the costs of the building to the Church asset account. When construction is complete, the balance of this account should be the total construction cost of the building.

Depreciation

Depreciation is one area where parish accounting moves away from the cash basis that is used elsewhere in the system. Assets in the Capital Fund are used over a period of time. The cost of buying these assets should therefore be spread over their life. The car used in the entries above is expected to be in use for 10 years. It would not be accurate to record a $10,000 expense for the car in one year and nothing for the other nine years. Instead the parish should recognize an expense of $1000 a year over the life of the car. This makes even more sense when you look at a building such as a church. Should the parish have the entire cost of the church as an expense when it's constructed? The building isn't even being used then. This allocation of expense is done through depreciation.

There is one exception to the rule of depreciating capital assets: land is never depreciated. Depreciation represents a "using up" of assets, and land can never be used up.

Calculation of depreciation involves three factors: the cost of the asset, its expected useful life, and its salvage value. The expected useful life of an asset is an estimate of how long the asset will last. A car may be depreciated over 7 years, while a church may be depreciated over 40 years. The salvage value is an estimate of how much the asset will be worth at the end of its useful life.

There are many different methods that can be used to calculate depreciation, and some of them can get very complicated. One common method is **straight-line depreciation**. To compute depreciation under a straight-line method, subtract the salvage value from the asset's cost to determine the total amount of depreciation over the life of the asset. Then divide this number by the life of the asset.

EXAMPLE: The parish buys a car for $8000. The car is expected to last 7 years and be worth $1000 at the end of that time. Depreciation is calculated as follows:

8000 (cost of asset) - 1000 (salvage value) = 7000 (total amount of depreciation)

7000 / 7(useful life) = $1000 depreciation expense per year

The Diocese of Crookston computes depreciation using the following formulas:
Buildings=0.2% of cost per month until salvage value of 5% is reached
Furnishings/equipment=0.9% of cost per month until salvage value of 5% is reached

Using these percentages, depreciation on the car is:

Salvage Value = 8000 X 5% = $400

Depreciation = 8000 X .9% = $72 per month

Depreciation can be recorded on a monthly basis, or can be updated at the end of the fiscal year.

The entry to record depreciation is made in the General Journal. The debit is to Depreciation Expense. The credit is to an asset account called Accumulated Depreciation. Continuing the above example, we have the following journal entry to record depreciation expense at the end of the month:

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 6/30 | 101 | Depreciation-Automobile | 2-9235000 | 72.00 | |
| | | | 2-1275100 | | (72.00) |

The car appears on the Balance Sheet as follows:

| | |
|---|---|
| Parish Car | $8000 |
| Less Accumulated Depreciation | $72 |

Notice that the asset will always appear on the balance sheet at cost. The difference between the cost and accumulated depreciation is called **book value**. The book value of the above car is $7928. The fair market value of the asset does not appear on the balance sheet.

Sale or Disposal of Assets

The sale or disposal of an asset may result in a gain or loss, depending on the book value of the asset. To determine gain or loss, compare the book value with the amount it was sold for. If the book value exceeds sale price, a loss will be recognized; if book value is less than sale price, a gain will occur.

*Note: before the entry is made to record the sale, depreciation must be brought up to date.*

Example: The parish sells its car for $7500. The car has a purchase price of $8000 and $1300 accumulated depreciation. The entry in the cash receipts journal must remove the car from the asset account and the depreciation account. The sale price of $7500 is higher than the book value of $6700, so a gain of $800 will be recognized.

Cash Receipts Journal

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 10/21 | Sale of parish car (remove depr) | 1 | 2-1275100 | 1300.00 |
| | (remove cost of asset) | 2 | 2-1275000 | (8000.00) |
| | (recognize gain on sale) | 3 | 2-4660000 | 800.00 |
| | (recognize receipt of cash) | 4 | 2-1210000 | 7500.00 |

EXAMPLE: The same car is sold for $6500. This will result in a $200 loss.

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 10/21 | Sale of parish car (remove depr) | 1 | 2-1275100 | 1300.00 |
| | (remove cost of asset) | 2 | 2-1275000 | (8000.00) |
| | (recognize loss on sale) | 3 | 2-9260000 | 200.00 |
| | (recognize receipt of cash) | 4 | 2-1210000 | 6500.00 |

If the asset is disposed of and no cash is received (the asset is "junked") a General Journal entry is made to remove the asset and its depreciation from the books. The book value is shown as a loss.

EXAMPLE: The parish gets rid of a car. The car had a purchase price of $8000 and was depreciated down to its salvage value of $500.

General Journal

| Date | Ref # | Explanation | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 8/16 | 101 | “Junk” car (remove depr) | 2-1275100 | 7500.00 | |
| | | (recognize loss) | 2-9260000 | 500.00 | |
| | | (remove asset) | 2-1275000 | | (8000.00) |
| | | | | | |

Major repairs

Work must always be done to keep assets in good condition; oil changes, fixing broken windows, painting, etc. However, a distinction must be made between general maintenance and major repairs that increase the value of the asset. The guidelines used for acquired assets are also used here: any maintenance that is over a certain amount and increases the life of the asset is added to the value of the asset. Putting a new door on the parish would not be capitalized; putting on a new roof would. General maintenance is recorded as an expense in the Operating Fund; major repairs are added to the value of the asset in the Capital Fund.

The entry for a major repair is pretty straightforward. If a new engine is installed in the parish car, the Car asset account is debited and cash or a payable is credited.

Although the total value of the church and roof is recorded in one account, their depreciation is computed separately. The Church may be depreciated over 30 years at a rate of $3000 a year; a roof added when the church was 15 years old may be depreciated over 20 years. Therefore the roof would still be depreciated after the church had been totally depreciated. All improvements are depreciated separately, with each having a salvage value.

## The Cemetery Fund

Canon 1243 states "Appropriate norms are to be enacted by particular law for the management of cemeteries". Statutes of the Diocese of Crookston 404.15 state that in respect to cemeteries "The assets and the revenues thereof shall neither be held nor used for the benefit of the parish." These citations stress the importance of keeping cemetery monies separate from the other assets of the parish. If the parish is using a single-fund system, there should be separate asset, liability, revenue, and expense sections for items related to the cemetery to keep them separate. However, to fully comply with the above requirements, a cemetery fund should be established.

The perpetual care account and any other assets set aside for use in the cemetery would be recorded in the cemetery fund. Any liabilities associated with the cemetery are also recorded in this fund. Revenues from sales of lots or special cemetery collections are recorded here, as well as expenses associated with the upkeep and operation of the cemetery.

## The Endowment Fund

The Endowment Fund is used to keep track of any endowments the parish establishes. An endowment is money that must be invested and cannot be spent. Only the interest from the endowment can be used; the principle must remain untouched. An endowment is beneficial because it provides a regular income stream for the parish.

Separate asset accounts should be used for each endowment. Each endowment may have sub-accounts if the endowment is invested in different places. If the interest is reinvested, it is recorded in this fund. Otherwise, the interest is recorded in the fund where the money is used.

## The Custodial Fund

The Custodial Fund is used for money the parish receives that it is holding until it passes the money to the appropriate party. Think of the Custodial Fund as an In-Out Fund.

This fund replaces the In-Out Account and the Diocesan Special Collection accounts in the General Fund. When this money is received, it is recorded in the Custodial Fund until it is forwarded to the appropriate party.

This fund has no revenues or expenses because the only money that comes into the fund is owed to another source, and is thus a liability.

## The School Fund

If a parish has a school, a separate fund is required to account for the school. The School Fund can be thought of as a General Fund for the school. All transactions that affect the day-to-day operations of the school are recorded here. Any capital assets and endowments associated with the school are recorded in the appropriate funds.

## Transfers Between Funds

Occasionally it will be necessary to transfer money from one fund to another. A transfer is recorded as an expense in the fund transferring the money because that fund no longer has the money available for use. It is recorded as a revenue in the fund receiving the money.

If the parish has separate bank accounts, the bookkeeper simply does a transfer from one account to the other. An entry is made in the cash disbursements journal in the fund transferring the money and the cash receipts journal in the fund receiving the money.

EXAMPLE: The parish transfers $3000 from the General Fund to the Capital Fund to buy a new piece of equipment. A transfer is done from the General Fund checking account to the Capital Fund checking account. The following entries would be made:

Cash Disbursements Journal, General Fund

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 2/16 | 5133 | Capital Fund Checking | Transfer | 1-9920000 | 3000.00 |

Cash Receipts Journal, Capital Fund

| Date | Description | Ref # | Acct # | Amount |
|---|---|---|---|---|
| 2/16 | Transfer From General Fund | 5 | 2-4680000 | 3000.00 |
| | Deposit to Checking Account | 6 | 2-1210000 | 3000.00 |

Another option would be to make an entry in the General Journal.

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 2/16 | 101 | Transfer to Capital Fund | 1-9920000 | 3000.00 | |
| | | | 1-1110000 | | (3000.00) |
| | | Transfer from General Fund | 2-1210000 | 3000.00 | |
| | | | 2-4680000 | | 3000.00 |

If the parish has only one checking account that is shared by the various funds, journal entries must be made to record the transfer even though no money is actually being moved. Entries are made in the general journal.

EXAMPLE: The same transfer is made as above, but the parish has only one checking account.

General Journal

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 2/16 | 101 | Transfer to Capital Fund | 1-9920000 | 3000.00 | |
| | | | 1-1110000 | | (3000.00) |
| | | Transfer from General Fund | 2-1210000 | 3000.00 | |
| | | | 2-4680000 | | 3000.00 |

Another common situation is where the General Fund will purchase a capital asset directly out of the general checking account. This should be recorded in the Cash Disbursements Journal of the General Fund as a transfer to the Capital Fund. The Capital Fund will have a journal entry recorded the value of the asset and recognizing a transfer from the General Fund.

Cash Disbursements Journal, General Fund

| Date | Check # | Payee | Purpose | Acct # | Amount |
|---|---|---|---|---|---|
| 3/16 | 5313 | Sullivan Motors | Purchase Car | 1-9920000 | 3000.00 |

General Journal

| Date | Ref # | Description | Acct # | Debit | Credit |
|---|---|---|---|---|---|
| 3/16 | 101 | Car purchased by General Fund | 2-1275000 | 10,000.00 | |
| | | | 2-4680000 | | 10,000.00 |

# Section 4: Planning and Budgeting

For the purposes of this discussion, planning is the process of establishing goals and objectives of the parish. Budgeting is the process of estimating future revenues and allocating them to future expenses. The main focus here is on budgeting, since it is a function of a good accounting system. However, without planning there can really be no budgeting. So let us start with a discussion of planning.

## Planning

Planning is a four-step process.

1. Perceive the needs of the parish
2. Set and prioritize goals to meet these needs. Goals are the broad ends the parish hopes to achieve. Improving family life in the parish is an example of a goal.
3. Set objectives to achieve these goals. Objectives are the measures taken to achieve the goals. They are specific, concrete, and definable. Forming a family life committee to improve family life in the parish is an objective.
4. Evaluating progress toward these goals on an ongoing basis.

Step 4 is an important step that is often overlooked. The parish needs to continuously look at what it is doing and see if it is achieving its goals. The parish may find that its goals or needs have changed over time. Effective planning is an ongoing process.

## Budgeting

The budget grows out of the planning process. The objectives are ways to meet the goals, and the budget is the way to meet the objectives, defined in dollars. Every parish is required to submit a budget to the Office of Parish Administration each year.

A budget provides a number of benefits for the parish:

- The budgeting process forces the parish to take a long-term look at its financial position.
- The parish can compare its anticipated revenues with its anticipated expenses and recognize possible future deficits.
- The parish is forced to make resource allocation decisions. The parish must decide how to best use its limited resources to achieve its desired goals.
- Comparing actual results to the budget can help the parish recognize problem areas. If one area is way over budget only halfway through the year, the parish can compensate by raising more money or cutting back in other areas.

A number of people should have input into the budget process. The pastor, finance council, pastoral council, bookkeeper, and other parish employees should all be involved in the preparation of the budget.

When preparing a budget, looking at the previous years' figures can be useful. The previous year's budget figures can be a good starting point in the budget process. By comparing these figures to the actual figures for that year, the parish can get a good idea of how accurate their budget was. This will give the parish some idea on which areas need to be increased or decreased.

A well-prepared budget isn't worth much if it isn't compared to the actual results of operations. The budget and actual figures should be compared on a regular basis to see if the budget is being adhered to. If actual revenues are falling short of predictions, then expenditures will need to be cut back to compensate. If the parish is going over budget on an expense item, they will need to cut back in other areas to avoid a potential loss.

<u>The Effect of Liabilities on the Budget Process</u>

If the parish has notes or other debts that they are making payments on, these need to be taken into consideration when preparing the budgets. Repayments of loans do not appear as expenses on the income statement, but still need to be considered when budgeting. The parish has to budget enough revenue to cover not only budgeted expenses, but also the principal payments for any loans the parish has.

<u>Budgeting issues</u>

Every parish should strive for a balanced budget, one where budgeted expenses equal budgeted revenues. But the most important trait of a budget is accuracy, and this should not be sacrificed to provide a balanced budget. If the parish has accurately and realistically anticipated their revenues and expenses, and the result is an unbalanced budget, then so be it. The parish should resist the temptation to “fix” the budget to make it balance.

A negative budget (one where budgeted expenses exceed budgeted revenues) could be easily explainable. If the parish has a massive remodeling project planned for this year, this will result in a negative budget (unless the parish has a capital fund). If the budgeted loss is due to an extraordinary expense, and the parish has a plan for covering the shortfall (drawing money out of savings or getting a loan), then a negative budget is acceptable.

If the budgeted loss is not due to some extraordinary expense, this is a sign of a potential problem in the parish. The parish will need to find some way to increase revenues and/or decrease expenses to avoid continued losses in the future. The main purpose of a budget is to detect these kinds of situations. “Fixing” the budget to make it balance will hide this problem, but will not make it go away.

Another temptation parishes may encounter is the temptation to make the financial statements “fit” the budget. A parish may classify a purchase of stamps as Office Supplies Expense because the Postage Expense is already over-budget. This may make the income statement look good because nothing is over-budget, but it is deceptive and hides the problem of overspending on postage. This will prevent the parish from taking proper action to correct the problem and could lead to the same problem next year. Instead, the expense should be allowed to go over budget, which will then send out a red flag indicating that Postage Expense should be examined more closely. The parish may find that they are spending too much on postage and will have to look at ways to cut back in this area. Or maybe the amount budgeted for postage is just too small, and will need to be increased next year. Maybe there's no "problem" at all–the parish just had a large one-time mailing that caused postage to go over its budgeted amount.

# Section 5: Internal Controls

Internal controls are an important part of the parish's bookkeeping system. Internal controls are the parish's policies dealing with the safeguarding of assets. The goals of the internal control system are to provide operational efficiency and effectiveness, financial reporting reliability, and compliance with laws.

One important component of internal control is division of duties. There should be at least two people involved in any process. At least two people should count the offertory collections. The person who signs checks should not be the same person who writes the checks and does the bookkeeping. This division of duties provides a system of checks and balances, because you always have one person verifying the work that the other is doing. This reduces the risk of errors and employee dishonesty.

Another important internal control concept is authorization. No transaction should take place without proper authorization. Expenditures should only be made by authorized parties; janitors should not be authorizing the purchase of new RE books. All expenditures should be supported by proper documentation, usually an invoice with a description of the expenditure.

Establishing internal controls is the responsibility of parish management: the pastor, finance council, and pastoral council. Management must work to establish the internal control policies of the parish, and monitor those policies to make sure they are being followed.

The following checklist will be helpful in implementing sound internal controls in the parish. Any negative responses indicate a potential weakness in the parish's internal control system.

## General Controls

☐ Are budgets prepared and approved by the pastor and the finance council, after consultation with the pastoral council?

☐ Are monthly financial statements prepared and submitted to the appropriate members of parish management? This gives management the most up-to-date information on the financial condition of the parish, allowing them to take action if need be.

☐ Do monthly financial statements contain comparisons with the budget? The income and expense figures need to be compared to the budgeted amounts to determine how well the parish is meeting their financial goals.

☐ Is the pastoral council consulted before important management decisions are made?

☐ Is an appropriately detailed list of bookkeeping procedures maintained on a current basis? The procedures should detail everything a new bookkeeper would need to know when taking over from the current bookkeeper. This would allow someone to take over if the current bookkeeper was unable to perform his/her duties due to sickness, sudden termination, etc.

☐ Are yearly financial statements prepared and distributed to members of the parish?

## Cash Controls

☐ Are all bank accounts and check signers authorized by the pastor?

☐ Are all bank accounts reported in the monthly financial statements? If the parish has bank accounts that are not being reported on the balance sheet, they are not presenting an accurate picture of the parish's financial condition. An exception is small accounts belonging to parish organizations such as the ladies' guild and the youth group. However, if any of these accounts have a large balance the parish should include them on the financial statements.

☐ Are all cash disbursements made by check (except petty cash disbursements)? Checks provide authorization–someone must sign the check and therefore approve the expenditure. Expenditures made with cash may be made by someone with no authority to spend parish funds. Checks also provide a permanent record of payment.

☐ Are checks dated and recorded when prepared?

☐ Are pre-numbered checks used for all bank accounts? This ensures that all checks are accounted for.

☐ Do procedures prohibit drawing checks to "cash"? Checks should only be written to a specified party. If the check is written to "cash", there is no indication of the purpose of the check, which makes authorization difficult.

☐ Do procedures prohibit signing blank checks? Once a blank check has been signed, that gives anyone the ability to fill in the payee and amount of the check. It completely negates the whole point of check signing, which is to authorize a specific expenditure.

☐ Are bank accounts reconciled each month? This serves two purposes: it ensures that the parish is reporting the correct balance on its financial statements, and it catches any errors the bank may make on the parish's accounts.

☐ Is there a group of persons, on a rotating basis, involved with the counting of the Sunday Offertory collection? Having a group of people counting the offertory increases the accuracy of the count. It also serves as a deterrent to theft.

☐ Does the parish approve reimbursements to employees for travel and other expenses on the basis of adequate documentation? All expenses should only be paid after adequate documentation has been provided to verify the disbursement.

☐ Is more than one person involved with the check writing and check signing? One person should not have the power to prepare checks, sign checks, and handle the bookkeeping. There should be at least one more person involved in the disbursement process.

☐ Does the person who signs the checks review the invoice from which payment is being made? The check signer should not approve any disbursement without documentation verifying the expenditure.

☐ Are payments made to vendors only on the basis of original invoices? Statements show only the amount owed, and do not provide a description of the items being paid. Only an invoice detailing the expenditure is sufficient documentation.

☐ Are all supporting documents marked as "paid" once a disbursement has been made? This prevents double-payment of a bill.

☐ Are all incoming checks immediately endorsed as "For Deposit Only"? This prevents other parties from cashing the checks if the checks are lost or stolen.

☐ Are amounts deposited matched to the cash receipts journal entry at the time of deposit? This verifies that the actual deposit matches the entry made in the parish's accounting records.

☐ Are restrictions on cash adhered to (building fund donations used only for building fund purposes, grant money used only for intended purposes, etc.)? If a donor gives money to a parish for a specific purpose, the parish is legally obligated to use that money for that purpose.

## Petty Cash Controls

☐ Are there adequate physical safeguards over the petty cash fund? The money should be kept in a locked box, with only one or two people having access to the funds.

☐ Are vouchers prepared for all petty cash expenditures? Vouchers provide a record of all withdrawals, including information on the reason for the withdrawal and the person requesting the withdrawal.

## Investment Controls

☐ Are investment securities and other negotiable instruments in the possession of an authorized person? If not, are they kept under lock and key or in a safe deposit box?

☐ Is a detailed record maintained of all investments by a person other than the designated custodian of the securities? The physical and accounting control of all assets should be separated. If one person controls both of these functions, that creates the potential for errors and employee dishonesty,

☐ Are all securities in the name of the parish? All securities and bank accounts should be in the name of the parish, never an individual.

## Payroll Controls

☐ Are W-4 forms filed for each employee? This form is the documentation to support the federal tax withholdings from the employees' paychecks.

☐ Is the Chancery notified of all changes in employee status? contact: Diocesan Benefit Administrator When an employee is hired, the Office of Parish Administration must be notified immediately so that they can ensure that the employee receives all the benefits he/she is entitled to. The Office of Parish Administration must also be notified when an employee terminates employment; there are a number of federal and state laws that determine an employee's insurance rights upon termination, and it is the responsibility of this office to see that terminating employees are informed of those rights. Increases in pay also need to be promptly reported to this office, because many of the employees' benefits are based on their estimated annual pay.

☐ Are salary changes approved by the pastor and the finance council?

☐ Are W-2 forms prepared at year-end for all employees?