

Treasurer's Annual Report

to the Board of Trustees

Community Church of Chapel Hill Unitarian Universalist

Andrew Wright, CPA, Treasurer

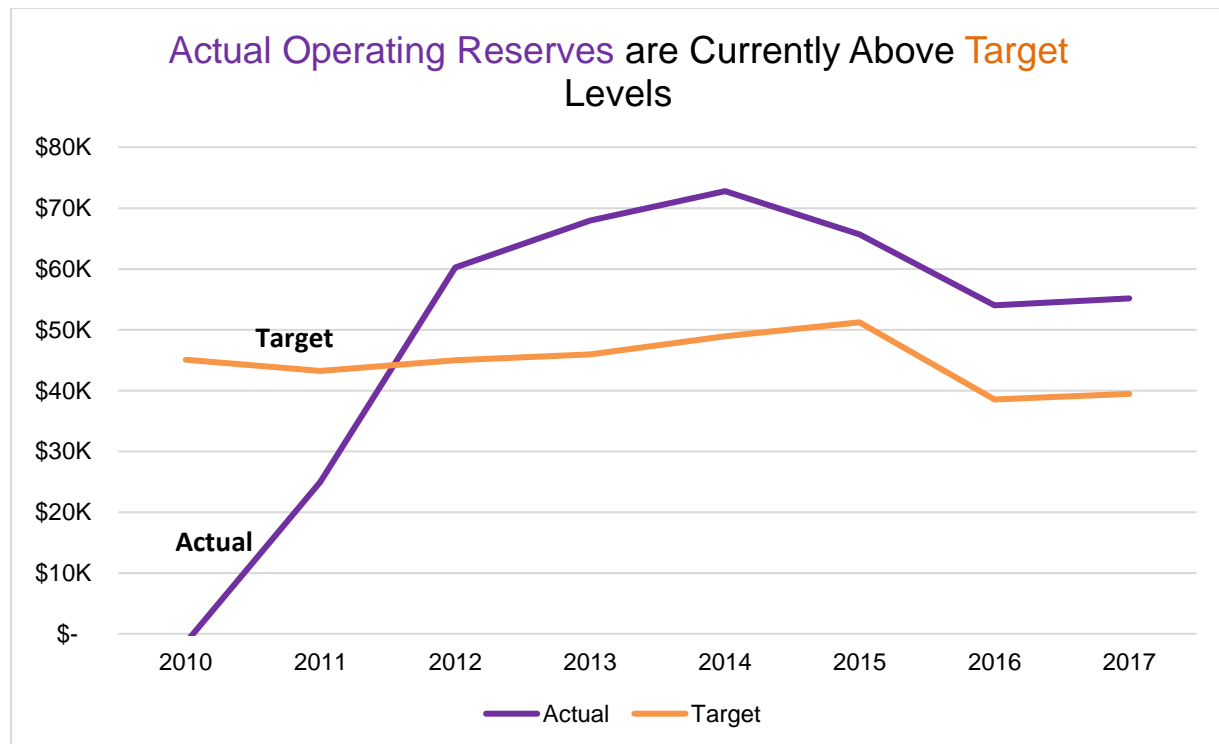
November 2017



Executive Summary

The financial health of the Community Church of Chapel Hill Unitarian Universalist (CCCHUU) was very strong during the fiscal year ending June 30, 2017 (FY2017). The Board of Trustees (BOT) considers a budget to be balanced if ending operating reserves are at or above the target set by the BOT, currently 6% of annual expenses. At the end of FY2017 actual operating reserves were 9.2% of FY2017 actual expenses and 8.4% of FY2018 budgeted expenses. Figure 1 shows actual operating reserves compared to target operating reserves for the past eight years.

Figure 1 – Actual Operating Reserves and Target Operating Reserve Amounts for the Last Eight Years



Income was up 4% as a result of new members and expenses were under budget.

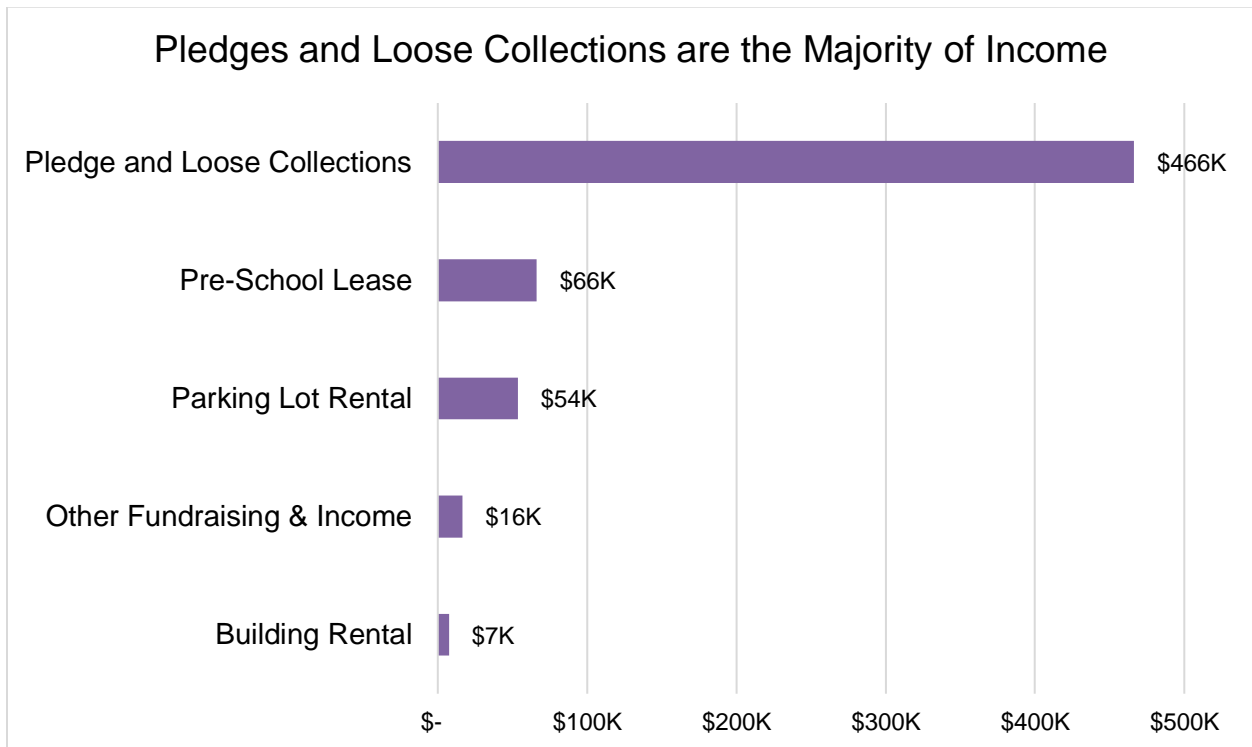
Looking ahead, the building project will put pressure on operating income. During the time that members are fulfilling both capital and operating pledges, if expenses increase it will put a strain on the budget and the BOT and Minister may decide to dip into operating reserves or make cuts to other expenses.

While we are entering a time of greater financial strain for the next several years due to the building project, we are entering with a strong financial picture. We also have the people and processes in place to maintain our financial position during the campaign.

Income

The primary source of income for CCCHUU is member pledges and loose collections, making up 76% of total income. Total income for FY2017 was \$610k as compared to \$586k in FY2016, a 4% increase. Figure 2 shows all sources of income.

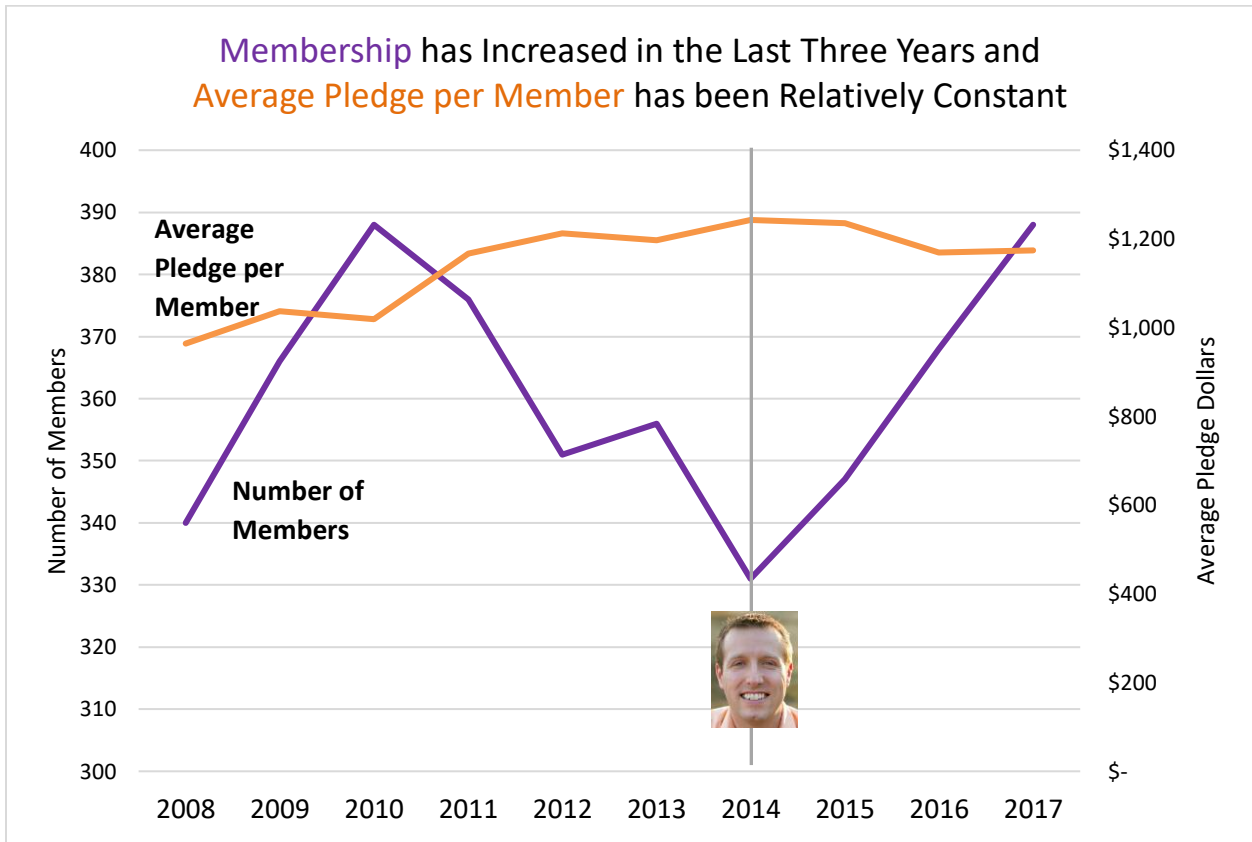
Figure 2 – FY2017 Sources of Income



The Pre-School Lease is scheduled to end in December 2018, after which a comparable reduction in expenses must be found. The church is planning to offset this loss of income with elimination of the existing debt, whose payments approximately equal the pre-school income, net of related janitorial expenses.

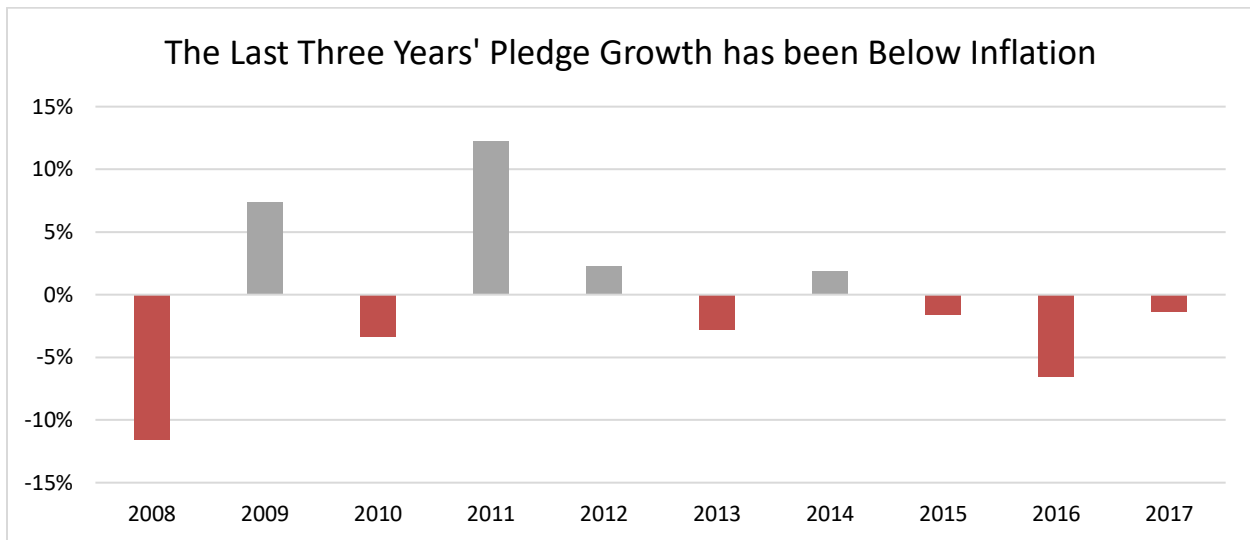
The total income from member pledges is a function of number of members and average pledge per member. There is a great deal of variability in pledges per member, but looking at an average is a valid way to evaluate income. After falling from 2010 to 2014, membership has been increasing in the last three years back to 2010 levels. It should be noted that 2014 is the year that our current minister, Thom Belote, joined the church. Average pledge per member has been relatively constant. Figure 3 shows the trend of these two numbers.

Figure 3 – Membership and Average Pledge for the Last 10 Years



In general, new members pledge at lower rates than older members, so it is not surprising to see downward pressure on the average pledge as there is an increase in net new members. Therefore I am not worried about the growth rate of average pledge per member not keeping pace with inflation. Figure 4 shows the growth rate of average pledges as compared to inflation. Above the 0 line means that average pledges grew more than inflation by that percent, while below the line means that they grew by that percent less than inflation. Over the long term we would like to see more years above the line than below.

Figure 4 – Pledge Growth Rate Compared to Inflation



Again, this is a trend to watch over the long run but I am not worried about it at this time given the increase in net new members.

Expenses

There are two ways the congregation spends money.

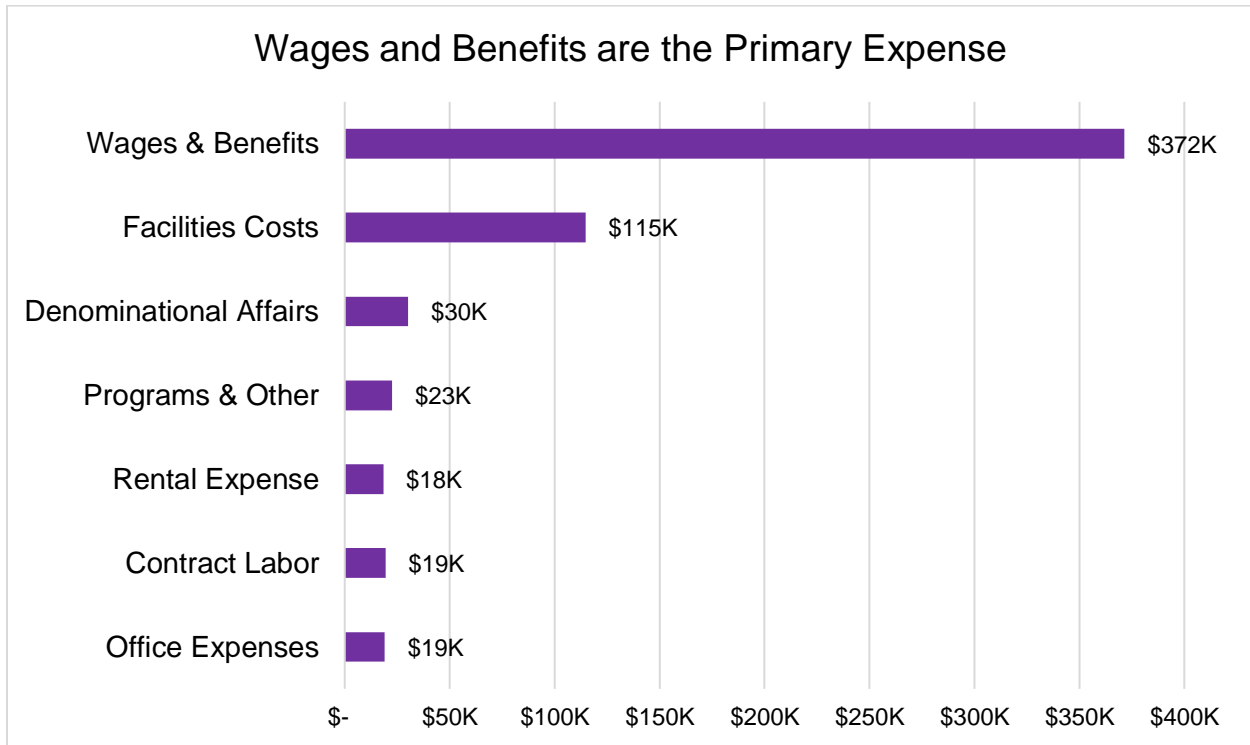
- The Operating Budget is funded from the income described earlier, primarily member pledges. These expenses are primarily paying staff and maintaining the facilities in support of the core mission of the church.
- Restricted Funds are self-contained categories which have separate sources of income not described above and their own expenditures. These expenditures are specific to the fund.
 - An example is the Share the Plate (STP) Sunday fund. All collections during a STP Sunday are earmarked for that STP recipient. None of the STP collections are counted in the income described in the earlier section for our operating budget, and the BOT and/or church staff cannot spend those receipts on anything other than the purpose of the fund. This is why neither the income nor the expenditures show up in the operating Income Statement, and any balance left at year end shows as Temporarily Restricted in the operating Balance Sheet.
 - See Table 4 for a full listing of Restricted Funds, including their receipts and expenditures.

Figure 5 shows operating expenses by type of expense for the operating budget only. Wages and benefits for our staff make up the majority of our operating expenses, at 62%. Facilities costs consist of putting money away for repairs into the Maintenance Reserves, interest on our existing debt¹ from the last building project, janitorial expense not related to the pre-school, and

¹ The principal portion of debt payments are a balance sheet transaction, are not expensed, and are therefore not included in Figure 5.

other building costs. Facilities costs made up 19% of operating expenses in FY2017. All other items in the operating budget made up the remaining 19% of expenses.

Figure 5 – FY2017 Operating Expenses by Type of Expense



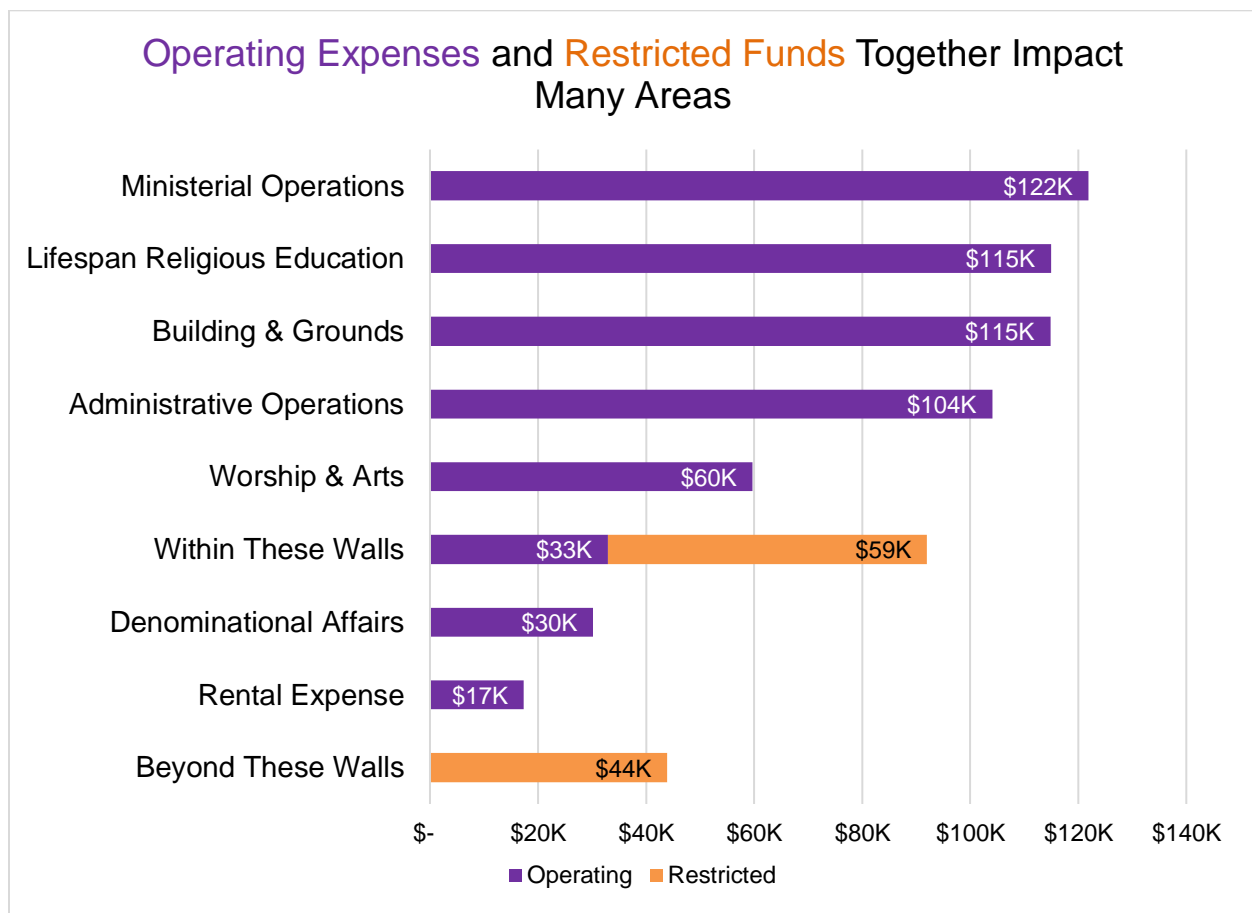
Another way to look at how we spend money is to categorize it by what impact it has or what purpose. For this we will add together both the operating budget and expenditures by the restricted funds, to get a complete picture of the impact of our congregation. The Restricted Fund Expenditures have been grouped together into either Within These Walls or Beyond These Walls. Note that we will exclude the Capital Fund as it is discussed later.

When looking at the purpose of the expense, we spend money in several ways.

- Ministerial Operations - primarily salary and benefits for our minister
- Lifespan Religious Education (LRE) - expenses for Director of LRE and the LRE Assistant and expenses for education programs for all ages
- Building and Grounds - putting money into our maintenance reserves, interest on our existing debt, janitorial services, insurance, utilities and other maintenance
- Administrative Operations - expenses for Congregational Administrator and Office Assistant, office equipment and technology
- Worship & Arts - compensation for Director of Music and the Accompanist, and music expenses

- Within These Walls - the operating budget funds the Membership Director, Sunday hospitality and expenses for some programs, while the Restricted Funds spend money primarily on children and youth ministries and musical activities
- Denominational Affairs - payments to the national/regional Unitarian Universalist organizations
- Rental Expense - expenses needed to generate income from the pre-school (janitorial expense) and parking lot (taxes paid on the income)
- Beyond These Walls - distributions by Share the Plate and other restricted funds

Figure 6 – FY2017 Operating Expenses and Restricted Funds by Purpose of Expense (excludes Capital Fund)



Maintenance Reserves

Included in Figure 5 under Facilities Costs, and in Figure 6 under Building & Grounds is an expense for maintenance reserves of \$37k. This is where the operating budget sets aside money to the balance sheet in a line called Maintenance Reserves. BOT policy for FY2017 was that 6% of total income be set aside as maintenance reserves, which are to be used for maintenance expenses more than \$1k in any year needed. The idea is to show an expense

each year, even if we don't have any major maintenance expenditures, so that when a major issue comes up it does not impact the operating budget all in one year. The minister maintains a 10-year maintenance plan of forecasted expenditures.

During FY2017 the church set aside \$37k for maintenance reserves and spent only \$2k out of maintenance reserves related to the Manse sewer. The ending balance can be found in Table 1.

Capital Campaign and Building Project

Three events influenced the decision by the BOT and congregation to pursue a capital campaign.

- The pre-school lease is set to expire on December 31, 2018. Income from the preschool, net of related janitorial expense, was \$56k in FY2017.
- When the pre-school leaves CCCHUU there will be the need to refurbish the space it occupied to make it usable for religious education, and there is the opportunity to expand the Jones building to accommodate the needs of various groups to meet in the church.
- After the conclusion of the prior building project to renovate the sanctuary in 2006, the congregation decided to carry debt to fund a portion of that project (referred to as the "existing debt"). Payments on the existing debt are \$48k per year, split between interest and principal. The debt comes due on December 25, 2018, when the church must either pay a balloon payment for the remaining principal of approximately \$130k², or refinance the remaining principal and continue to make payments.

Either an increase in pledges or a reduction of expenses would be needed starting in January 2019 to maintain a balanced budget. Paying off the existing debt was identified as a solution to reducing expenses by a similar amount to the loss of preschool income. A capital campaign that would raise money for the dual purposes of paying off the existing debt and funding the renovation and expansion of the Jones building was explored over the course of the past several years and was approved by the BOT in FY2017.

As part of the capital campaign, the BOT created several task forces including a Finance Task Force (FTF). The FTF is managing the budget, expenses, and financial policies of the capital campaign. Other task forces include the Capital Campaign Task Force, Communications Task Force, and Building Task Force. Capital Fund transactions can be found in Table 4.

In FY2017 the expenditures in the Capital Fund consisted of payments toward our existing debt (\$260k), payments for a financial feasibility study (\$12k), and other pre-construction costs (\$8k).

At the end of FY2017, the Capital Campaign cash account, included in the Checking/Savings amount in the balance sheet had a balance of \$28k. Pre-construction expenses of \$15k have been approved by the BOT and not yet spent, meaning the Capital Campaign is solvent for now.

² This estimate of the remaining principal is as of November 2017 and reflects \$260k of principal paid down by the Capital Fund in FY2017, the estimate assumes the capital campaign does not make any more payments to principal before the debt is due in December 2018.

The campaign is scheduled to conclude in May 2018, after which the task forces will reconcile the pledges with the expected construction costs and remaining debt. The congregation will approve a plan in June 2018 and construction is expected to begin in early 2019.

With regard to the operating budget, during the time that members are fulfilling pledges to a capital campaign a church should not expect average pledges to rise at all. This is normally a three year period but the financial strain on members can be as long as five years. If average pledges do not rise for five years, this will put a strain on the operating budget.

Financial Risks and Other Considerations

In December 2016 the current treasurer (at that time assistant treasurer) performed a financial review which looked at controls and financial processes at CCCHUU. In January 2017 we engaged the services of an outside CPA, Mig Sistrom, to also review the financial processes. Those two reviews resulted in a series of recommendations which will benefit the congregation by strengthening controls. The recommendations are in the process of being implemented, with some completed and some underway during FY2017. In general the controls were good prior to the reviews, and these changes will strengthen them.

The capital campaign will put downward pressure on operating income for the next five years as described previously. If CCCHUU does not continue to attract new members and retain existing members, income may not keep pace with expense inflation.

Medical expenses are the primary expense concern of the treasurer, as they tend to rise faster than inflation. The UUA announced November 1, 2017 that premiums will not increase at all in 2018, which is a great relief, however what will happen in the years after 2018 is still a concern.

Maintenance costs, especially for the aging Manse building, are also a concern.

Acknowledgements and Sources

The data in this report is from our Congregational Administrator, Andrea Sordean-Mintzer, who is not responsible for any of my errors of interpretation.

Editing and data visualization assistance by Demia Wright.

Thanks to Laurence Kirsch for training and for allowing me to plagiarize parts of last year's Treasurer's Annual Report.

Thanks to Bill Poteat for insights and training.

Thanks to Scott Provan and the Sunday counters for their help in managing the collections.

Inflation data from Federal Reserve Bank of St Louis, <https://fred.stlouisfed.org/series/GDPDEF>.

Financial Statements

The financial statements are on an accrual basis.

Notes on Table 1 - Balance Sheet

Fixed Assets are not depreciated currently but that is an area I plan to research. Normally an organization would depreciate fixed assets in order to show the expense as a reduction of net income and reduce their tax liability. Being tax-exempt, CCCHUU has not depreciated fixed assets in the past. I will see if we are able to claim any of the parking lot repaving expense as depreciation specifically against our parking lot business which is considered taxable. If we are able to claim a portion of that expenditure to reduce our net income from the parking lot rental, we could save money on taxes.

Maintenance Reserves ending FY2017 were \$35k due to not spending any material amounts during the year. The Manse will require a sewer replacement in the next year so we expect to spend the maintenance reserves in FY2018.

Long-Term Liabilities consists entirely of the existing loan which remained after the conclusion of the prior building project in 2006. This loan is due in December 2018, so the majority would really be considered a current liability, however for comparative purposes I am presenting the debt consistent with prior years in Long-Term Liabilities so you can see what the true balance of the loan is over time. The large reduction in balance is due to some early donations from the capital campaign.

Notes on Table 2 – Income Statement

Table 2 presents the income and expenses of the operating budget.

Notes on Table 3 – Reconciliation of Operating Reserves

Table 3 connects the income statement to the balance sheet by showing the beginning balance of operating reserves at the end of the prior fiscal year, adding net income from FY2017, subtracting principal paid by the operating budget on the existing debt, and arriving at the operating reserve amount at the end of FY2017.

Notes on Table 4 – Restricted Funds

Table 4 shows activity within the Restricted Funds, which are self-contained and separate from the operating budget. The ending balance matches the Temporarily Restricted Funds on the Balance Sheet.

Table 1
Balance Sheets at the End of Each Fiscal Year
(unaudited)

ASSETS	<u>Jun 30, 14</u>	<u>Jun 30, 15</u>	<u>Jun 30, 16</u>	<u>Jun 30, 17</u>
Current Assets				
Checking/Savings	211,644	196,206	248,906	260,098
Other Current Assets	4,617	15,648	11,591	18,608
Total Current Assets	216,261	211,854	260,497	278,705
UU Common Endowment Fund	144,970	144,818	159,638	181,653
Fixed Assets	3,112,731	3,112,731	3,112,731	3,112,731
TOTAL ASSETS	<u>3,473,962</u>	<u>3,469,402</u>	<u>3,532,866</u>	<u>3,573,089</u>
LIABILITIES & EQUITY				
Liabilities				
Current Liabilities				
Payroll Liabilities	11,171	12,971	22,706	30,005
Accrued Payables	2,323	4,380	4,605	3,077
Unearned Income	25,555	43,133	49,032	61,605
Total Current Liabilities	39,049	60,484	76,343	94,687
Long Term Liabilities	544,790	522,305	497,157	225,267
Total Liabilities	583,839	582,789	573,500	319,953
Equity				
Financial Reserves				
Operating Reserves	72,777	65,631	54,041	55,122
Maintenance Reserves	24,798	13,085	122	35,072
Ministerial Transition Res.	3,178	5,865	9,865	13,865
Total Financial Reserves	100,753	84,581	64,027	104,058
Illiquid Equity	2,567,941	2,590,426	2,615,574	2,888,556
Permanently Restricted Funds	149,220	145,340	160,846	182,961
Temporarily Restricted Funds	72,210	66,267	118,919	77,561
Total Equity	2,890,124	2,886,613	2,959,366	3,253,136
TOTAL LIABILITIES & EQUITY	<u>3,473,962</u>	<u>3,469,402</u>	<u>3,532,866</u>	<u>3,573,089</u>

Table 2
Income Statements for Fiscal Years Ending June 30
(unaudited)

Income	<u>Jun 30, 15</u>	<u>Jun 30, 16</u>	<u>Jun 30, 17</u>
Collections			
Member Pledges	428,595	430,207	455,459
ID Contributions	3,688	5,241	3,266
Loose Collection	7,029	7,250	7,718
Total Collections	<u>439,312</u>	<u>442,698</u>	<u>466,443</u>
Other Income			
General Operating Fundraising	7,705	15,979	16,029
Other Income - Other	547	1,554	432
Total Other Income	<u>8,252</u>	<u>17,533</u>	<u>16,462</u>
Rental Income			
Building Rental	5,328	6,566	7,427
Parking Lot Rental	52,211	55,267	53,546
Pre-School Lease	61,155	64,045	66,287
Total Rental Income	<u>118,694</u>	<u>125,878</u>	<u>127,260</u>
Total Income	<u>566,257</u>	<u>586,109</u>	<u>610,165</u>
Expense			
Administrative Operations	101,045	102,240	104,091
Building & Grounds	105,071	109,721	114,834
Denominational Affairs	25,332	29,300	30,216
Lifespan Religious Education	100,836	108,812	114,971
Ministerial Operations	124,661	118,732	121,899
Rental Expense	17,729	18,463	17,346
Within These Walls	24,663	29,097	32,910
Worship & Arts	51,582	56,187	59,699
Total Expense	<u>550,919</u>	<u>572,552</u>	<u>595,966</u>
Net Income	<u>15,339</u>	<u>13,558</u>	<u>14,199</u>

Table 3

Reconciliation of Operating Reserves for Fiscal Years Ending June 30

(unaudited)

Reconciliation of Operating Reserves:	<u>Jun 30, 15</u>	<u>Jun 30, 16</u>	<u>Jun 30, 17</u>
Beginning Operating Reserves	72,777	65,631	54,041
Net Income	15,339	13,558	14,199
Payment of Loan Principal ³	(22,485)	(25,148)	(13,119)
Ending Operating Reserves	<u>65,631</u>	<u>54,041</u>	<u>55,122</u>

³ The Capital Campaign fund paid the principal for the last six months of FY2017, making the amount paid by the operating budget approximately half of what it would have been. This policy was ended on June 30, 2017 when it became clear that the ending date of the pre-school was extending to fall 2018 and the operating budget could support the full debt payments.

Table 4
Activity in Temporarily Restricted Funds, FY2017
(unaudited)

<u>Fund</u>	<u>Balance at 6/30/16</u>	<u>Receipts</u>	<u>Expenditures</u>	<u>Other⁴</u>	<u>Balance at 6/30/17</u>
<u>Within These Walls</u>					
Art Resources Fund	3,382	685	0	0	4,067
Benevolence Fund	3,188	0	(800)	862	3,250
Campus Ministry Activity Fund	369	0	(250)	0	119
Capital Fund ⁵	56,837	251,277	(280,421)	(90)	27,602
Children Ministry Activity Fund	2,311	3,018	(3,447)	0	1,882
Church Fellowship	(60)	134	0	0	74
Concert Series	12,939	17,450	(22,988)	0	7,401
Francis Brewer Flower Fund	1,956	0	(223)	0	1,732
IT Fund	29	0	0	0	29
Memorial Rock Fund	6,024	400	(800)	0	5,624
Minister Discretionary Fund	3,805	2,512	(3,246)	952	4,023
Music Activity Fund	(765)	2,126	(3,487)	39	(2,087)
Quilting Group Clearing Fund	877	0	(315)	0	562
Sanctuary for Dialogue	1,205	0	0	0	1,205
Sarah Insch Youth Leadership	3,725	0	(3,470)	524	779
SEA Activity Fund	1,216	0	0	0	1,216
Services Auction Fund	150	80	(50)	0	180
Youth Ministry Activity Fund	7,243	17,634	(20,022)	1,672	6,527
Total Within These Walls	104,431	295,316	(339,520)	3,959	64,186
<u>Beyond These Walls</u>					
Community Service Ministry	14	225	(2,010)	2,251	479
Faith in Action	(55)	0	0	0	(55)
Habitat Fund	5,230	101	(4,000)	4,192	5,523
Peace & Justice Clearing Fund	2,096	0	(475)	0	1,621
Share the Plate Sunday	10	36,472	(25,072)	(11,409)	0
Social Concerns/Special Project	7,194	260	0	0	260
SOSL Ministry Team Fund	7,194	10,632	(12,327)	48	5,547
Total Outreach	14,489	47,689	(43,884)	(4,919)	13,375
 Total Restricted Funds	 118,919	 343,005	 (383,404)	 (960)	 77,561

⁴ Other is primarily transfers, such as Share the Plate transferring its receipts to Habitat Fund.

⁵ See the section titled Capital Campaign and Building Project on pages 6-7 for more details.