

6 Steps to Maintain Your Church's Tax Exempt Status

Provided by Lauren Hunter

Maintaining a church's tax exemption status is huge; if your church is not thinking about this, or has never been concerned about the ramifications of losing your tax exemption status, pay attention and read on!

Church technology plays a huge role in how a church maintains their tax exemption status. Nearly every church employs some kind of church software—whether it is a desktop-based system or web-based church software system. Many of these helpful steps below come from the incredible body of expertise at [Icon Systems](#), maker of IconCMO, web-based church software.

Step 1 – Make sure your church accounting system (some are integrated with your church management system, some are stand-alone) has been audited by an external CPA firm.

For example, did your software company bring in one of the top 25 CPA firms in the country to analyze the accounting processes, audit trails and the reporting? This is an important question to ask them.

Step 2-Encourage accountability by making sure your church accounting software program gives the CFO or accounting volunteer the ability to guard access to the system.

It's important that access is not given to people who are unauthorized to make changes to accounting information.

Step 3-Know who has manipulated transactions in your accounting software.

It's really important that whatever accounting system you use record details on who inputted, edited, imported, or exported data to and from the system. These records help make sure that the system is being used correctly and that the information is trackable should a problem ever arise.

Step 4-Make sure payments to credit cards and other expenses are broken out by individual transactions to each fund, and not shown as one lump sum.

This makes the payroll and bill paying process manageable and provides clear details about what transactions have been executed.

Step 5 – Make sure the fund balances are NOT kept in the liabilities of the general ledger.

The simplest way to explain the way a fund should work is that they are to be treated the same as owner's equity in a for profit system. It is not money that is "owed" to someone else – as in a liability – but it is money that the owner or in this case the church "owns."

Step 6-Confirm that revenues and expenses are NOT the only accounts used to track funds within your general ledger.

Revenue and Expenses are used to track money coming in and out of an accounting system and not the balance (money left over). Additionally these accounts go back to zero at the beginning of every fiscal year, which is not what you want when there is a balance remaining. A perfect example of this is your personal checkbook at the end of the year – if this were to go to zero each year there would be plenty of mad people at their banks in January.

Warning: if your church accounting software is NOT doing any of these six steps, your church might be out of compliance.

I interviewed Karla, [Icon System's](#) internal CPA, in order to provide additional information for churches. I asked her to give a summary that affects churches and the major repercussions:

Compliance with standards is necessary for any and all churches no matter what the size. The Financial Accounting Standards Board (FASB) is a private, not-for-profit organization founded in 1973.

The FASB's job is to create the generally accepted accounting principles (GAAP) for organizations within the U.S. In order to establish accounting principles, the FASB issues pronouncements addressing general or specific accounting issues.

These pronouncements are usually issued in the form of Statements of Financial Accounting Standards (SFAS). These standards are recognized as authoritative by the Securities and Exchange Commission (SEC) and by the American Institute of Certified Public Accountants (AICPA). Standards issued by the FASB govern the preparation of financial reports for all nongovernmental entities and as such apply to financial reporting by churches.

Here are the primary FASB standards that are relevant to churches:

- SFAS No. 95 Statement of Cash Flows
- SFAS No. 116 Accounting for Contributions Received and Contributions Made
- SFAS No. 117 Financial Statements of Not-for-Profit Organizations
- SFAS No. 124 Accounting for Certain Investments Held by Not-for-Profit Organizations.

Non-compliance of the standards can have dire effects on the organization. A worst case scenario, the church may lose its tax exempt status if the Internal Revenue Service does an examination of the records of the church."

The IRS terms church records to mean "all corporate and financial records regularly kept by a church, including corporate minute books and lists of members and contributors." Please check the [IRS website](#) for detailed information on this topic.

If the church chooses to not follow the standards, the financial statements will not be able to be certified as "in accordance with generally accepted accounting principles." This could

result in members and others to question the integrity of the accounting system as a whole and may negatively impact future contributions by donors.

If the church has a loan with a bank, the bank will usually require financial statements that are in accordance with [GAAP](#). If statements are not prepared in this way, it may cause the church to incur additional expenses to restate the reports in the proper GAAP format by engaging outside accountants and CPAs.

As always, please consult with your CPA to determine if you are in compliance with [FASB](#) reporting standards or if you have additional questions.

I hope this article has been helpful to you – if you have any additional thoughts or questions on how your church has dealt with the issue of IRS compliance, please leave a comment for the benefit of everyone! 🇺🇸