FINANCIAL MANAGEMENT OF LIBRARIES AND INFORMATION CENTERS

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Financial Management of Libraries and Information Centers

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Financial Management of Libraries and Information Centers

To my father,

Harold James Burger
(1910–1984),

who, as both a parent and an accountant, helped to bring
a modicum of order into this chaotic world

Acknowledgments

I began teaching library financial management at the University of Illinois at Urbana-Champaign Graduate School of Library and Information Science in the fall of 2010. My students in that course were remarkably patient with me in my attempts to bring both coherence and clarity to a subject woefully neglected in graduate schools of library and information science. During that first year, the idea for a textbook in library financial management took shape, and over the ensuing six years, it grew into this volume.

I am grateful to Ben Harvey (a member of that 2010 class), who is currently the manager of library operations at the Metropolitan Library System of Oklahoma County, for his careful editing of some of the early chapters. As the book neared its completion, I imposed on two friends and colleagues for their subject expertise and editorial excellence. Paula Kaufman, the former library director at the University of Tennessee at Knoxville and subsequently at the University of Illinois at Urbana-Champaign, with whom I worked closely for seven years and who now is a close friend, spent more hours than I care to admit in reading and commenting on many chapters. Scott Bennett, a friend of forty years and the former library director at Johns Hopkins and then at Yale, offered challenging and sometimes amicably trenchant, but always extremely helpful, comments on my style and content. It is impossible to overstate the debt I owe to these two for all their help and support in bringing this volume to print. They have both taught me much about financial management. However, I take full responsibility for any errors in the text.

I would be remiss if I did not also express my gratitude to several others who made this project come to fruition. Blanche Woolls of Libraries Unlimited was an ardent advocate and supporter of this book from my initial proposal. I am also most fortunate to have had the assistance of my daughters, Nell Kirst, Margaret Edwards, and Sarah Wilds, as contributors to this volume. Nell, a family physician, coauthored chapter 10 with me and has taught me much about this topic and thinking in general. Meg, a librarian who has taught and practiced library marketing, and Sarah, a speech language pathologist who also happens to have marketing experience in the corporate world, have both provided expertise in an area where I am a novice. They wrote chapter 24 on marketing. Finally, I am most grateful for my dear wife, Ann, who has sustained all of us these many years.

Introduction

Financial management has been widely neglected in library and information science (LIS) schools.[1] Although there are LIS schools that offer a financial management course, these usually focus on grantsmanship, currently a small portion of library revenue, or on cost accounting and cost-benefit analysis, or information economics. For the most part, these courses only deal with parts of a much larger and complicated whole. As a result, most library managers learn financial management on the job, often within the framework of a specific organization. This book is an attempt to formalize some of this financial management knowledge for library school students, librarians, and others, such as public library board members who want to become more knowledgeable about the financial management of libraries and information centers.

Financial management is "the planning, directing, monitoring, organizing, and controlling of the monetary resources of an organization."[2] This includes a basic understanding of financial statements and financial reporting, budgeting, and cost accounting. These broad rubrics also contain topics such as basic accounting, the time value of money, annuities and bonds, contract law, basic knowledge of descriptive and inferential statistics and sampling for use in the measurement and evaluation of library operations, cost accounting, techniques of cost estimation, the cost-benefit calculation of cooperative and collaborative ventures, and marketing.

Why should you care? Knowledge of financial management is fundamental to understanding the financial health of the library and how the library financial system actually works. If you want to demonstrate your financial competence to public library board members, or to library administrators or college and university administrators at budget time, or to the chief information officer, or to your school principal, you will be rewarded handsomely by focusing your attention on the following material. After all, you don't want to come across as an idiot when being interviewed for a job and a prospective employer asks you what you think the most important aspects of internal control are or how you think accounting for pensions under GASB GAAP can be improved. Of course, many employers don't know this either, but you get my point. Finally, an understanding of these basic concepts, even if you were unfortunate enough not to take a full-fledged financial management course, will help you with your own finances.

In most cases, when you first embark on your library career, you will probably be entrusted with spending relatively small sums of money from a "budget."[3] This spending may be in the area of collections, for example, purchasing materials on chemistry or children's literature, wages for student assistants or part-time employees, information and communications technology for computers, laptops, networking, Web filters, or interrelated areas such as collection development and information technology (e.g., electronic resources and their licenses). Knowledge of the basic structure of formal financial management can be helpful but is not central to the spending of your budget.

In another case, you might find yourself as a director or assistant director of a small public library. All of a sudden you are now responsible for the entire library's spending. Knowledge of the basic structure of formal financial management is now mandatory. So in whatever library position you find yourself, financial management will be crucial to your ability to perform.

Finally, decision making about finances using the information you have at hand is the main activity involved in financial management. If you are a prudent and deliberative decision maker, you will naturally ask about the veracity of that information, the manner in which it was obtained or produced, the reliability of that information and whether it was based on an estimate or actual evidence, and also what psychological factors may affect your decision. This introductory text will begin to address these decision-making questions and will also equip you with the knowledge to answer them or, at the very least, to ask other intelligent questions about them.

So let's press on and see what the basics really are.

Notes

1. See Robert H. Burger, Paula T. Kaufman, and Amy L. Atkinson, "Disturbingly Weak: The Current State of Financial Management Education in Library and Information Science Curricula," *Journal of Education for Library and Information Science* 56(3): 190–197.
2. www.BusinessDictionary.com, accessed May 26, 2015.
3. The term *budget* is in quotes because it can sometimes carry several ambiguous meanings. Here it refers to an allocation of funds for a specific purpose. It serves as a limit of the amount of money that can be spent and at the same time as a demand that it is also an expected amount to be spent. So, yes, a budget places you between a rock and a hard place.

Contents

Section I
Financial Statements

In the following chapters, we will examine some general principles of financial management and financial statements. This will include separate chapters on financial statements in general, the accounting process, the peculiarities of governmental financial statements, and auditing and internal control.

1

Financial Management as Information Management

Context

What This Chapter Covers

This chapter lays out the unifying framework of this introductory text on library financial management, which we define as information management coupled with decision making based on the information managed.

Why This Material Is Important

The material in this chapter provides a preview of what is to come and grounds the material solidly in the field of information science as a unifying framework for understanding.

What You Should Learn from This Chapter

After finishing this chapter, you should be aware that financial management is very much like information management. Financial information is produced as a result of transactions and delivered in the form of financial statements and budgets. Both external and internal users depend on this information and make decisions based on what they assume is accurate and true.

Introduction

The first thing to realize is that financial management is essentially another form of information management. As you are either becoming, or already are, a specialist in this field, no matter what your concentration, this is common ground. The second thing to realize is that although information professionals make decisions about how to manage information, they don't usually use the information managed to make decisions. That is, librarians in a public library may acquire, catalog, and circulate materials and also provide reference services using them, but in that role, they do not usually use the information so managed to make decisions about how to carry out these activities in a more effective and efficient manner. Instead, they will use information about the processes, the community's needs, and interactions with patrons to do this. The financial manager, however, is not only involved in the production and presentation of financial information but also directly uses this information to manage financial resources.

Like any information system, the financial information system can be conceptualized as a cycle. Information is produced and delivered to the user, often mediated by an information specialist. The user verifies the accuracy and veracity of the information and, once satisfied with its accuracy and veracity, proceeds to use that information to make decisions. Broadly defined, users can be classified either as an external user (external to the producer of the information) or as an internal user (part of the entity that produces the information). The information is presented in a standard format, according to national standards, so that it can be compared with information that is similar. So let's unpack this to understand more completely what is being described. After an introductory explanation, we'll look at some "real financial information" and proceed to understand where it came from, whether we can trust it, and the decisions we will make as a result of it as managers (internal users). The goal is for you to be able to read and understand financial statements, know a bit more about budgeting than you are personally familiar with, and learn how to make choices based on financial information using cost accounting and other techniques and approaches.

The First Stage of the Financial Information Cycle: Recording and Presentation of Financial Information

Every library and the entity of which it is a part, whether it be a municipality, college, university, or school, produces reports of the financial transactions that occur each period. Broadly speaking, these reports are called **financial statements**. These statements summarize the monetary aspects of all financial transactions that occurred during the previous period. A **financial transaction** occurs whenever a book is purchased, an employee is paid, someone's sick leave balance is charged, a utility or phone bill is paid, and when tax revenue or money from a patron for a fine is received. That is, it is an event that happens at a given instant involving the transfer of money from others to the library or to others from the library. These transactions are recorded by the bookkeeper or accountant and then periodically brought together and summarized at the end of a specific period (e.g., a month, quarter, or year) in the form of a financial statement. So in our metaphor of financial management as an information system, the information is produced as a result of transactions and delivered in the form of financial statements. For example, at the Fitzbergen Public Library, the following transactions occurred during the month of July 2011:

- The library paid salaries to each employee. Each payment to an individual employee is a transaction. The total amount for salaries during July was $25,678.00. This is a summary figure.
- The library bought a new book truck from a library equipment vendor for $435.00. This purchase is a transaction.
- The library received its annual payment of tax revenue of $756,987.00 from the City of Fitzbergen. This receipt of funds is a transaction.

- The library collected \$472.35 in fines from 321 patrons. Each payment of a fine by an individual is a transaction, however small it may be. This is a summary figure.

These transactions will then be reported as summaries in a financial statement for the month of July. The statement of activities, a financial statement that presents expenditures made and revenues received looks like this:

Fitzbergen Public Library
Statement of Activities
for the Period July 2011

Revenues	
Tax Revenue	\$756,987.00
Fines	472.35
Total Revenues	**\$757,459.35**
Expenses	
Salaries	\$25,678.00
Equipment	435.00
Total Expenses	**\$26,113.00**
Excess of Revenues over Expenses	**\$731,346.35**

The amounts reported in the financial statements are summaries, but we can find out the individual components of these summaries, the individual transactions, by asking the business manager to produce them. This is a relatively straightforward process because of the way in which each individual transaction is recorded. In chapter 4, we will examine how this is carried out.

The Second Stage of the Financial Information Cycle: Verification of the Accuracy and Veracity of Financial Statements

So how do we know whether the information delivered in the form of financial statements is both true and accurate? If we are going to make decisions on the basis of these financial statements, we have to be assured that our decisions are based on information that is both accurate and true. We can never be absolutely sure of this, but there are several mechanisms that should give us confidence.

National standards prescribe how financial transactions are recorded and how financial statements are produced and presented. These are called **generally accepted accounting principles**, or **GAAP** (pronounced like the word "gap"). The people who record transactions and produce financial statements are required to abide by these principles. There is second set of standards called **generally accepted auditing standards**, or **GAAS**, which are published and revised by the American Institute of Certified

Public Accountants. These standards prescribe how audits to verify the veracity and accuracy of an organization's financial statements are to be conducted. For our purposes, **internal control** is the most important principle within these auditing standards. Internal control consists of the mechanisms used in the process of recording financial transactions that ensure their accuracy and verifiability. That is, they ensure that the transactions are not inadvertently or deliberately made in error. Finally, financial statements are audited by an auditor who is not part of the organization being audited. The auditor applies a set of extensive processes to verify that GAAP was followed and that internal control is working and robust. If the statements are audited, we should have a greater confidence in their accuracy, validity, and reliability.

The Third Stage of the Financial Information Cycle: Financial Decisions by External and Internal Stakeholders

Decisions of an External Stakeholder

An external stakeholder (i.e., a granting agency, bond-rating agency, prospective donor, accreditation board, or even another library) may want to see your library's financial statements. Why? They may be thinking of giving you some money, and if they do not like the information they see in the financial statements or if you cannot provide reasonable explanations for items that worry them, they may pass you by for more transparent and reliable prospects. Or, the library may want to finance a renovation of its building, most commonly by selling bonds to investors. Investors generally do not invest in just any bond that comes along. They will want to see whether the library is on a sound financial footing, whether it has engaged in deficit financing, and whether it has paid its bills on time. They can obtain most of this information from the library's financial statements. They also need to know whether the statements are accurate and reliable. The auditor's report is one seal of approval upon which they rely for this assurance. Library materials vendors may also wish to see the library's financial statements to be assured that the library has the ability to pay them promptly for materials supplied.

Therefore, external stakeholders are one of the main audiences for this financial information. They base their own decisions on the information presented in these financial statements. Stakeholders internal to the library also use these statements to make decisions.

Decisions of an Internal Stakeholder

Generally speaking, managers and the public library board are the primary internal stakeholders and users of the financial statements. These stakeholders use the statement that shows revenues and expenses over a specific period of time, coupled with the budget for that period, to monitor actual expenses and revenues. If, for example, the library had expected utility bills of $1,250 for January (a budgeted amount) and the actual bill for utilities for January was $2,500, the director and board members would naturally want to know the reason for the discrepancy. Had the temperature been colder than usual? Were employees turning the heat up too high? Does the library need to be better insulated? Was the predicted amount of $1,250 an error?

Posing these questions and answering them is one of the primary ways that internal stakeholders monitor the expenditure and receipt of funds under their charge. On the basis of these questions and the answers they receive, they will make decisions relating to these anomalies and discrepancies. This is just one way in which these financial statements can be used. We will explore other uses as we progress through this text.

Summary

This chapter has shown that the financial statements are produced to provide information about past financial transactions. If the library's procedures are produced in accordance with the generally accepted accounting principles and auditing standards (GAAP and GAAS), the statements will more likely be accurate, verifiable, and reliable. They need to be so because both external and internal users of these statements rely on them to make decisions.

Before we explore what these financial statements are called, what they contain, and how they differ one from another, we will examine a budget and the responsibilities for spending and managing it that you can expect in the beginning of your library career.

Web Exercise

Look up your hometown public library on the Internet and see what kinds of financial information they provide on their Web site. If they do not make any available, try googling "[your hometown] Public Library financial statements." If this is a bust, go to the Web site of the town in which your library resides and see whether you can find the municipal financial statements; within those, look for anything to do with the public library.

Once you find the statements, examine them to find out how much the library spent last year in total and how much tax and other sources of revenue it received. Were these amounts more or less than the amounts budgeted for these items?

Conceptual Questions

1. Explain to another librarian how financial management is information management.
2. Explain briefly how financial information is produced.
3. External and internal stakeholders make decisions based on the information contained in financial statements. In what ways can they be confident that their decisions are based on accurate and true information? Do you think this confidence is well placed? What does this confidence depend on?