

# The MinistryWatch.com 5 Star Ratings System

## Overview

First of all, the ratings attempt to measure financial efficiency. In layman's terms, this can be described as getting the most mission-related activity out of the least amount of financial resources. Although financial efficiency may not be the primary basis upon which donors make giving decisions, we believe that this information can be a relevant and useful stewardship tool.

Second, the ratings are objective. They are based entirely on financial ratios derived from information in an organization's IRS Form 990 or audited financial statements. The ratings do not consider program outcome measurements. Although program outcome measurements may be relevant to donors, they are not reported in a standard format that facilitates comparison of ministries with very different missions.

Third, the ratings are relative. No independent benchmarks are set for the financial ratios. Instead, the system compares the financial ratios of organizations to determine their relative financial efficiency.

Fourth, the ratings assess organizations in three separate areas of efficiency. Each area uses two ratios to determine efficiency, a risk ratio and a return ratio (similar to the idea of cost vs. benefit). An organization will score well in an area if its risk ratio is low relative to that of its peers and its return ratio is high relative to its peers.

## The Three Areas of Financial Efficiency

There are three separate efficiency areas for which each organization will receive an efficiency rating between 1 and 5 Stars (higher is better). An overall rating is also calculated based on each organization's percent rankings in each area (See section called "Calculating the Ratings" for more details about the calculation).

### **Fund Acquisition**

The Fund Acquisition efficiency rating uses ratios that relate to how the organization raises support.

<u>Risk/Return</u>	<u>Name</u>	<u>Calculation</u>
Risk (lower is better)	Fundraising Cost Ratio	Fundraising Expense/Total Revenue
Return (higher is better)	Contributions Reliance Ratio	Contributions/Total Revenue

### **Resource Allocation**

The Resource Allocation efficiency rating uses ratios that relate to how the organization spends its resources in the current period on mission-related activities.

<u>Risk/Return</u>	<u>Name</u>	<u>Calculation</u>
Risk (lower is better)	Spending Ratio	Total Expenses/Total Revenue
Return (higher is better)	Program Output Ratio	Program Expense/Total Revenue



## Asset Utilization

The Asset Utilization efficiency rating uses ratios that relate to how the organization uses its asset base to further its operations in the future.

<u>Risk/Return</u>	<u>Name</u>	<u>Calculation</u>
Risk (lower is better)	Degree of Long-Term Investment	Total Assets/Current Assets
Return (higher is better)	Current Asset Turnover	Total Expenses/Current Assets

## Calculating the Ratings

There are several steps to calculating the ratings for each organization.

1. The six individual ratios are calculated for each organization.
2. A population average is determined for each of the six ratios.
3. A ratio score is determined for each of a ministry's six ratios by dividing the ministry's ratio by the population average for that ratio. A score of 1 means the ratio equals the population average.
4. The risk score is subtracted from the return score to determine an efficiency score for each organization in each efficiency area.
5. A percent rank (percentile) is determined for each organization's efficiency scores based on their positions relative to the efficiency scores of all other organizations.
6. A rating of one to five stars is assigned to each organization in each efficiency area based on the following distribution:

90% - 100%	5 Stars
67.5% - 90%	4 Stars
32.5% - 67.5%	3 Stars
10% - 32.5%	2 Stars
0% - 10%	1 Star

To compute the overall 5 Star Rating (the MinistryWatch.com Efficiency Rating) of an organization, the following additional steps are performed:

1. A simple average of the three individual percent ranks (one for each of the three individual efficiency ratings) is calculated to get an average percent rank for each organization.
2. An overall percent rank (percentile) is determined for each organization based on the average percent rank statistic calculated above.
3. An overall rating (the MinistryWatch.com Efficiency Rating) of one to five stars is assigned to each organization based on the distribution above.