

Financial Report

Administrative Office Funds of the Roman Catholic Diocese of San Diego

June 30, 2017



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INDEPENDENT AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS

Most Reverend Bishop Robert W. McElroy
Bishop of the Roman Catholic Diocese of San Diego
Administrative Office Funds of
the Roman Catholic Diocese of San Diego
San Diego, California

We have audited the accompanying financial statements of the Administrative Office Funds of the Roman Catholic Diocese of San Diego, which comprise the statement of financial position as of June 30, 2017, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of significant estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Administrative Office Funds of the Roman Catholic Diocese of San Diego as of June 30, 2017, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis-of-Matter Regarding Legal Status

As discussed in Note 1 to the financial statements, the Administrative Office Funds of the Roman Catholic Diocese of San Diego is part of the Roman Catholic Diocese of San Diego and has no separate legal status or existence.

Report on Summarized Comparative Information

We have previously audited the Administrative Office Funds of the Roman Catholic Diocese of San Diego's 2016 financial statements, and our report dated October 26, 2016, expressed an unmodified audit opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2016, is consistent, in all material respects, with the audited financial statements from which it has been derived.



WEST RHODE & ROBERTS

San Diego, California
October 17, 2017

**ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO**

STATEMENT OF FINANCIAL POSITION

June 30, 2017

(With Summarized Financial Information for June 30, 2016)

	2017	2016 (Note 18)
ASSETS		
Cash and cash equivalents	\$ 15,287,873	\$ 15,664,750
Accounts receivable:		
Parishes and schools, net of \$100,000 allowance	380,715	629,640
Pledges receivable, net of \$40,000 allowance	966,950	772,700
Note receivable	6,480,000	6,480,000
Prepaid expenses and other assets	150,000	10,000
Pooled income funds, CGAs and CRTs	414,497	447,686
Long-term investments	43,649,490	35,619,905
Funds on deposit with Catholic Community Foundation of San Diego	11,100,192	10,505,863
Property and equipment, net	12,396,216	12,350,637
Property available for sale	-	1,700,000
Total assets	\$ 90,825,933	\$ 84,181,181
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable and accrued liabilities	\$ 1,555,012	\$ 984,453
Accrued vacation	413,969	427,638
Self-insurance reserve for claims incurred but not received	3,050,000	3,150,000
Due to Catholic Account for Parishes and Schools	14,446,166	18,192,847
Funds on deposit:		
Other diocesan entities funds	30,193,157	24,833,131
Priest retirement plan liability	-	215,045
Total liabilities	49,658,304	47,803,114
Net assets:		
Unrestricted	26,586,872	22,491,870
Temporarily restricted	10,941,098	10,259,142
Permanently restricted	3,639,659	3,627,055
Total net assets	41,167,629	36,378,067
Total liabilities and net assets	\$ 90,825,933	\$ 84,181,181

**ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO**

**STATEMENT OF ACTIVITIES
Year Ended June 30, 2017**

(With Summarized Financial Information for the Year Ended June 30, 2016)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	2016 (Note 18)
REVENUES AND SUPPORT					
Parish assessments	\$ 9,720,932	\$ -	\$ -	\$ 9,720,932	\$ 9,459,973
Self-insurance revenue	25,644,666	-	-	25,644,666	25,782,117
Contributions and bequests	1,287,579	8,709,874	12,604	10,010,057	7,885,410
Rental income	260,896	-	-	260,896	237,118
Administrative fees	177,045	-	-	177,045	162,767
Interest and other investment income	1,139,564	882,112	-	2,021,676	(154,274)
Parish and employee insurance agency funds, net	42,615	-	-	42,615	184,034
Gain on sale of assets	1,613,970	-	-	1,613,970	6,566,173
Other revenue	111,793	-	-	111,793	83,025
Net assets released from restrictions:					
Satisfaction of program restrictions	3,478,509	(3,478,509)	-	-	-
Satisfaction of time restrictions	5,431,521	(5,431,521)	-	-	-
Total revenues and support	<u>48,909,090</u>	<u>681,956</u>	<u>12,604</u>	<u>49,603,650</u>	<u>50,206,343</u>
EXPENSES					
Self-insurance expenditures	22,787,449	-	-	22,787,449	22,484,972
Programs	11,237,481	-	-	11,237,481	10,109,710
Administrative	4,284,141	-	-	4,284,141	3,738,134
Expenditure of restricted donations	2,237,764	-	-	2,237,764	1,897,044
General:					
Subsidies to parishes and schools	1,770,840	-	-	1,770,840	450,000
Operating expenses	577,805	-	-	577,805	555,706
Contributions and outside charitable programs	500,000	-	-	500,000	500,000
Depreciation	479,733	-	-	479,733	432,571
Assessments	366,407	-	-	366,407	423,899
Interest expense	347,789	-	-	347,789	491,605
Professional and legal fees	224,679	-	-	224,679	155,938
Total general	<u>4,267,253</u>	<u>-</u>	<u>-</u>	<u>4,267,253</u>	<u>2,004,013</u>
Total expenses	<u>44,814,088</u>	<u>-</u>	<u>-</u>	<u>44,814,088</u>	<u>41,239,579</u>
Change in net assets	4,095,002	681,956	12,604	4,789,562	8,966,764
NET ASSETS AT BEGINNING OF YEAR	<u>22,491,870</u>	<u>10,259,142</u>	<u>3,627,055</u>	<u>36,378,067</u>	<u>27,411,303</u>
NET ASSETS AT END OF YEAR	<u>\$ 26,586,872</u>	<u>\$ 10,941,098</u>	<u>\$ 3,639,659</u>	<u>\$ 41,167,629</u>	<u>\$ 36,378,067</u>

**ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO**

STATEMENT OF CASH FLOWS

Year Ended June 30, 2017

(With Summarized Financial Information for the Year Ended June 30, 2016)

	2017	2016 (Note 18)
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ 4,789,562	\$ 8,966,764
Adjustments to reconcile change in net assets to net cash from operating activities:		
Change in value of split-interest agreements	39,862	506,665
Interest and other gains on long term investments	(1,637,404)	(217,325)
Depreciation	479,733	432,571
Gain on sale of property	(1,613,970)	(6,566,173)
Allowance for doubtful accounts	(25,000)	-
Changes in operating assets and liabilities:		
Receivables	79,675	(54,453)
Prepaid expenses and other assets	(140,000)	-
Planned gifts receivable	(6,673)	133,290
Accounts payable and accrued liabilities	556,890	(165,377)
Self-insurance reserve for claims incurred but not received	(100,000)	(5,932)
Net cash provided by operating activities	2,422,675	3,030,030
CASH FLOWS FROM INVESTING ACTIVITIES		
Net proceeds from long-term investments, net	(6,392,181)	11,559,043
Change in funds on deposit with Catholic Community Foundation of San Diego	(594,329)	(10,505,863)
Funds on deposit	5,144,981	35,277
Proceeds from sale of surplus property	3,313,970	676,250
Purchase of property and equipment, net	(525,312)	(154,032)
Net cash provided by investing activities	947,129	1,610,675
CASH FLOWS FROM FINANCING ACTIVITIES		
Note payable principal payments	-	(1,575,118)
Net change in CAPS borrowing	(3,746,681)	(5,239,666)
Net cash used in financing activities	(3,746,681)	(6,814,784)
Change in cash and cash equivalents	(376,877)	(2,174,079)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	15,664,750	17,838,829
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ 15,287,873	\$ 15,664,750
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash paid for interest	\$ 347,789	\$ 491,605
Note receivable in exchange of property	\$ -	\$ 6,400,000

ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO
NOTES TO FINANCIAL STATEMENTS

Note 1. Organization and Significant Accounting Policies

Organization and Activities

The Administrative Office Funds of the Roman Catholic Diocese of San Diego (the Administrative Office) coordinates educational, religious, community, and human development programs in addition to the administration of the Diocese and the Catholic Account for Parishes and Schools (CAPS).

The Administrative Office has no separate legal status or existence. It is part of the Roman Catholic Diocese of San Diego, which is incorporated as the Roman Catholic Bishop of San Diego (the Diocese), a corporation sole.

The accompanying financial statements present the Administrative Office activities only and exclude the assets, liabilities, and operations of other diocesan entities (i.e., Holy Cross Catholic Cemetery, Mater Dei Catholic High School) as well as parishes, schools, and other separately incorporated Catholic organizations and programs in San Diego and Imperial Counties.

Significant Accounting Policies

Method of Accounting – The financial statements of the Administrative Office have been prepared on the accrual basis of accounting.

Basis of Presentation – Net assets and revenues, gains, and other support are classified as unrestricted, temporarily restricted, and permanently restricted based on the existence or absence of donor restrictions on when and how the Administrative Office is to use the net assets. Accordingly, the net assets of the Administrative Office and changes therein are classified and reported as follows:

Unrestricted net assets – Net assets that are not subject to any donor-imposed stipulations.

Temporarily restricted net assets – Net assets subject to donor-imposed restrictions on their use that may be met either by actions of the Administrative Office or the passage of time.

Permanently restricted net assets – Net assets subject to donor-imposed restrictions requiring that the principal be maintained permanently by the Administrative Office. Generally, the donors permit the Administrative Office to use all or part of the income earned for either general or donor-specified purposes.

Revenue Recognition – Contributions are recognized as revenue when they are unconditionally pledged or when all conditions have been met.

The Administrative Office reports contributions as restricted if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted revenues are reclassified to unrestricted revenues and reported in the statement of activities as revenues released from restrictions. Contributions with donor restrictions requiring the principal gift to be held in perpetuity are reported as permanently restricted. The income earned from such assets is generally restricted to the purpose designated by the donor. Gifts not designated for a specific purpose are reported as increases in unrestricted net assets.

Cash and Cash Equivalents – Cash not needed for the daily operations of the Diocese is invested in an institutional money market fund. The Administrative Office retains a petty cash fund.

Investments – Marketable securities, consisting primarily of investments in equities, corporate debt and government debt, are carried at market value, as measured principally by market quotations. Accordingly, the carrying amount of the securities is adjusted for unrealized gains and losses. The investments are managed by separate money managers. These money managers are monitored by an independent investment consulting firm as well as the Investment Committee of the Diocesan Finance Council. The investment portfolio is guided by an investment policy statement approved by the Diocesan Finance Council.

ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO
NOTES TO FINANCIAL STATEMENTS

Funds on Deposit with Catholic Community Foundation of San Diego (CCFSD) – The Administrative Office has funds on deposit with CCFSD. The CCFSD's investments follow the Socially Responsible Investment Guidelines adopted by the United States Conference of Catholic Bishops. The funds are reported at fair value and changes in the value of the fund are reported as gains or losses in the statement of activities.

Accounts Receivable – Accounts receivable consists mainly of amounts due from parishes and schools. All accounts receivables are reviewed for collectability and reserves for uncollectible amounts are recorded based on previous experience and history with the family. Accounts are written off against the allowance for doubtful accounts when deemed uncollectible. Management has determined that an allowance of \$100,000 is needed for the year ended June 30, 2017.

Property and Equipment – Property and equipment is recorded at cost or, if donated, at fair market value on the date of donation. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets. Buildings are depreciated over forty years, furniture and fixtures over ten years, and computers over five years. Property and equipment is depreciated on a straight-line basis as follows:

Buildings and improvements	40 years
Furniture and equipment	5 to 10 years
Technology	5 years

Depreciation expense totaled \$479,733 for the year ended June 30, 2017.

Agency Transactions – At times the Administrative Office receives funds that are for other organizations. These funds are recorded as increases in assets and liabilities.

Income Taxes – The Administrative Office is part of the Roman Catholic Bishop of San Diego which has received notice from the Internal Revenue Service and the California Franchise Tax Board that, as an agency of the Roman Catholic Church, it is exempt from income taxes. It qualifies for exemption under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Franchise Tax Code. It is also exempt from federal unemployment tax and certain property taxes. The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 740-10, *Accounting for Uncertainties in Income Tax*, sets a minimum threshold for financial statement recognition of the benefit of a tax position taken or expected to be taken in a tax return. The Administrative Office has reviewed its position for all open tax years and has determined that it has no uncertain tax positions requiring accrual or disclosure.

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The primary estimates included in the financial statements are depreciation, allowances for uncollectable receivables and self-insurance claims incurred but not received.

Subsequent Events – Subsequent events are events or transactions that occur after the statement of financial position date but before financial statements are available to be issued. The Administrative Office recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at that date, including the estimates inherent in the process of preparing financial statements. The Administrative Office's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statement of financial position, but arose after that date and before the financial statements are available to be issued.

The Administrative Office has evaluated subsequent events through October 17, 2017, which is the date the financial statements are available for issuance, and concluded that there were no events or transactions that needed to be disclosed.

ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO
NOTES TO FINANCIAL STATEMENTS

Note 2. Fair Value Measurements

Due to the short-term nature of cash equivalents, receivables, prepaid expense, accounts payable and accrued liabilities, fair value approximates carrying value. In accordance with Financial Accounting Standards Board Codification No. 820 (FASB ASC 820), fair value is defined as the price that the Administrative Office would receive upon selling an asset or transferring a liability in an orderly transaction to an independent buyer in the principal or most advantageous market of the asset

FASB ASC 820 establishes a three-tier hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs and to establish the classification of fair value measurements for disclosure purposes. Inputs refer broadly to the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available. The standard describes three-tier hierarchy of inputs that may be used to measure fair value as follows:

Level 1: Quoted prices (unadjusted) of identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, and other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect the Administrative Office's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Assets and liabilities measured at fair value on a recurring basis are summarized below:

	Fair Value Measurements at June 30, 2017, Using:		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:			
Long-term investments			
Funds on deposit with Catholic Community Foundation of San Diego	\$ 43,649,490	\$ -	\$ -
	11,100,192	11,100,192	-
Total assets	<u>\$ 54,749,682</u>	<u>\$ 11,100,192</u>	<u>\$ -</u>

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices.

*ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO
NOTES TO FINANCIAL STATEMENTS*

Note 3. Long-Term Investments

Long-term investments consist of the following at June 30, 2017:

	<u>Market Value</u>	<u>Cost</u>
CUIT equity funds	\$ 15,060,112	\$ 13,043,290
Corporate obligations	6,831,949	6,789,522
Government obligations	7,361,693	7,397,529
CUIT bond funds	3,223,047	3,175,888
Mutual funds	3,825,193	3,800,628
Cash and cash equivalents	7,347,496	7,347,494
	<u>\$ 43,649,490</u>	<u>\$ 41,554,351</u>

Note 4. Annual Catholic Appeal Donations

The Annual Catholic Appeal (ACA) is a Diocesan-wide fundraising campaign in which each parish is assessed an amount based on its financial capabilities. Amounts raised in excess of the assessed amount are rebated back to the parish.

The ACA campaign runs from February to December each year. The funds received from the 2016 campaign were designated for use by the Diocese during the year ending June 30, 2017. Similarly, pledges made and donations received during the 2017 campaign are reported as temporarily restricted funds and will be used in fiscal year 2018. Pledges receivable included in the accompanying statement of financial position represent amounts pledged for the 2017 campaign to be received in fiscal year 2018. All pledges are due within one year.

Note 5. Pooled Income Funds, Charitable Gift Annuities and Charitable Remainder Trusts

The Administrative Office is the beneficiary of various pooled income funds, charitable gift annuities and charitable remainder trusts. These provide for the payment of distributions to designated beneficiaries over the trusts' terms (usually the designated beneficiary's lifetime). At the end of the terms, the remaining assets are available for the Administrative Office. The assets are recorded as temporarily restricted contributions at their present value, which is calculated using applicable mortality tables and discount rates.

Note 6. Catholic Account for Parishes and Schools (CAPS)

The Administrative Office administers the Catholic Account for Parishes and Schools (CAPS) as a separate program administered by the Roman Catholic Bishop of San Diego (the Diocese). CAPS exists to finance the construction and renovation of parish and school facilities and to provide a safe investment for excess parish and school funds. The assets of CAPS consist of investments and loans made to Catholic parishes and schools within San Diego and Imperial Counties. The liabilities of CAPS consist of deposits made by Catholic parishes and schools within San Diego and Imperial Counties. The assets and liabilities of CAPS are separate from the Administrative Office and are therefore not included in the accompanying financial statements.

The Administrative Office has borrowed from CAPS which is recorded as a liability on the accompanying financial statements. The amount due to CAPS is \$14,446,166 at June 30, 2017.

ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO
NOTES TO FINANCIAL STATEMENTS

Note 7. Property and Equipment

Property and equipment consist of the following at June 30, 2017:

Buildings	\$ 11,731,435
Land	4,725,585
Furniture, fixtures and equipment	<u>4,726,369</u>
	21,183,389
Less accumulated depreciation	<u>8,787,173</u>
	<u>\$ 12,396,216</u>

Note 8. Restricted Net Assets

Temporarily restricted net assets consist of the following at June 30, 2017:

Annual Catholic Appeal - rebates payable and donations to be used in fiscal year 2018	\$ 5,189,220
Temporarily restricted endowment assets	4,639,351
St. Francis Center Improvements	210,207
Donahue Trust - for needy students	154,511
Blessing Our Future	96,886
Bishop Flores Memorial Fund	89,064
Other restricted deposits	<u>561,859</u>
	<u>\$ 10,941,098</u>

Permanently restricted net assets consist of the following at June 30, 2017:

St. Francis Endowment Fund - income used for the operating expenses of St. Francis Center	\$ 2,986,401
Sacred Heart - James E. Spain Family Fund - advised fund for projects within the Diocese of San Diego	<u>653,258</u>
	<u>\$ 3,639,659</u>

Note 9. Net Assets Released from Restriction

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors.

Net assets released from restriction consist of the following at June 30, 2017:

Satisfaction of time restrictions:	
Annual Catholic Appeal - rebates payable and donations to be used in fiscal year 2017	<u>\$ 5,431,521</u>
Satisfaction of program restrictions:	
Valley Parish Development Fund	1,514,742
Mission Cooperation Plan	849,108
Endowment Distributions	386,613
FIAT Consortium	256,267
Bishop Flores Memorial Fund	153,840
Other restricted deposits	<u>317,939</u>
	<u>3,478,509</u>
	<u>\$ 8,910,030</u>

ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO
NOTES TO FINANCIAL STATEMENTS

Note 10. Endowment

The Administrative Office follows the standards codified in FASB ASC 958-205-65, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds*, which provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the 2006 Uniform Prudent Management of Institutional Funds Act (UPMIFA). The Administrative Office's endowment consists of three permanently restricted and one temporarily restricted fund. The funds primarily benefit the seminary.

Interpretation of Relevant Law – The Administrative Office has interpreted the UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Administrative Office classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Administrative Office in a manner consistent with the standard of prudence prescribed by UPMIFA.

Endowment Investment and Spending Policies – The Administrative Office has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Administrative Office must hold in perpetuity. The Administrative Office expects its endowment funds, over time, to provide an average rate of return of approximately 6 percent annually. Actual returns in any given year may vary from this amount. The funds have been deposited in the Catholic Community Foundation of San Diego.

To satisfy its long-term rate-of-return objectives, the Administrative Office relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Administrative Office targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

The Administrative Office has a policy of appropriating for distribution each year 2-4 percent of its endowment fund's average value over the prior fiscal year. In establishing this policy, the Administrative Office considered the long-term expected return on its endowment. Accordingly, over the long term, the Administrative Office expects the current spending policy to allow its endowment to grow at an average of 1-2 percent annually. This is consistent with the Administrative Office's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

**ADMINISTRATIVE OFFICE FUNDS OF
THE ROMAN CATHOLIC DIOCESE OF SAN DIEGO
NOTES TO FINANCIAL STATEMENTS**

Donor-restricted endowment net asset composition as of June 30, 2017, is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 169,912	\$ 4,129,993	\$ 3,627,055	\$ 7,926,960
Investment return:				
Investment return	-	847,779	-	847,779
Total investment return	-	847,779	-	847,779
Contributions	-	48,192	12,604	60,796
Transfer from unrestricted	-	-		
Appropriation of assets for expenditure	(169,912)	(386,613)	-	(556,525)
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 4,639,351</u>	<u>\$ 3,639,659</u>	<u>\$ 8,279,010</u>

Note 11. Long-Term Debt

Long-Term Debt – The Administrative Office has a \$10,000,000 revolving loan facility available at 1.35 percent plus LIBOR, but no amounts were drawn under the facility at June 30, 2017. The revolving loan is an 80 percent advance on security value maintained.

Letter of Credit – The Administrative Office has one outstanding standby letter of credit totaling \$3,457,432 at June 30, 2017, related to the self-insured worker’s compensation insurance which is secured by investments (see Note 16).

The Administrative Office is subject to compliance with certain debt covenants, including restrictions on additional indebtedness. At June 30, 2017, management believes (and certified that) the Administrative Office is in compliance with these covenants.

Note 12. Guarantees of Indebtedness of Others

The Diocese of San Diego guarantees the bonds of Catholic Secondary Education – Diocese of San Diego, Incorporated, through a Private Placement Agreement that was entered into between the Administrative Office and Union Bank, N.A. A Guarantee Agreement was entered into between the Roman Catholic Bishop of San Diego, a corporation sole, and Union Bank, N.A. to provide that the obligations guaranteed include the obligations of the Administrative Office under the Private Placement Agreement. The outstanding amount of the bonds was \$20,100,000 at June 30, 2017.

Several parishes have refinanced construction loans with the Knights of Columbus. The Knights of Columbus provides fixed interest long term financing that is guaranteed by the Administrative Office. At June 30, 2017, six loans have been refinanced by parishes for a total of \$23,453,397. The total amount guaranteed by the Roman Catholic Bishop of San Diego, a corporation sole is approximately \$19,297,000 at June 30, 2017.

Note 13. Commitment

Power Purchase Agreement – The Administrative Office entered into a power purchase agreement with SolarCity Corporation in January 2016, whereby SolarCity began to install their solar electricity generating equipment on Administrative Office’s parking lot in October 2016. The system size is 200.88 DC kW. Upon completion of the equipment installation expected in late 2016, the Administrative Office committed to purchase all of the energy generated by the solar system from SolarCity. Under the terms of the agreement, the Administrative Office will pay SolarCity for use of the generated power for a period of 20 years with an option for up to three additional terms of five years each. However, at the end of the 6th and 10th contract years, and at the end of the initial term and each additional 5 year term, the Administrative Office has an option to purchase the solar electricity generating equipment at its then fair market value. Payments for energy will be included in the Administrative Office’s utility expenses account and consolidated in operating expenses in the financial statements.

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Note 14. Lay Employee Multiple Employer Pension Plan

Diocese of San Diego Pension Plan for Lay Employees – As of June 30, 2017, the date of the latest actuarial report, the defined benefit pension program for lay employees had assets of \$195.1 million and an actuarial present value of accumulated benefits of \$271.4 million, resulting in a net liability of \$76.3 million, which, under accounting guidance for multiple employer pension plans, is not reported as a liability in these financial statements. Lay employees working for the Administrative Office account for 5 percent of the participants in this plan. The obligation for the remaining participants under the multiple employer plan continues to be the proportionate responsibility of each diocesan entity.

The plan provides for retirement benefits to employees working at least 20 hours per week, after five years of participation in the Lay Plan the employee is 100 percent vested. Besides the Administrative Office, the Lay Plan includes employees of the parishes, schools, Catholic Charities (which has maintained employee contributions), and other Catholic entities operating within the Diocese.

The Administrative Office made an annual contribution equal to 12 percent of eligible wages totaling \$546,823 during the year ended June 30, 2017.

Note 15. Priest Defined Benefit Plans and Charitable Trust

The Administrative Office participated in a defined benefit retirement plan for priests and a plan that provides post-retirement benefits for priests. These plans are supported by contributions and a charitable trust established in 1997.

San Diego Diocesan Charitable Trust for Retired and Disabled Priests – This trust was started with an initial \$10 million dollar campaign and now has a balance of over \$17.4 million. The income from this trust can be used to support the Diocese of San Diego's priest pension responsibilities and post-retirement benefits. Management believes the funds in the trust would offset the present value of the priest pension obligations at June 30, 2017. These funds in the trust are considered part of the Multiple Employer pensions and are not reported as assets in the accompanying financial statements.

The Pension Plan and Pension Trust for the Priests of the Dioceses of San Diego and San Bernardino – As of June 30, 2017, the date of the latest actuarial report, the defined benefit pension program for priests had a market value of \$24.5 million (\$14.5 million pertains to the San Diego Diocese). An actuarial present value of accumulated benefits of \$42.2 million (\$26.7 million pertains to the San Diego Diocese), resulted in a net liability of \$17.7 million (\$12.2 million pertains to the San Diego Diocese). Under accounting guidance for multiple employer pension plans, this obligation is not reported as a liability in these financial statements. Priests working for the Administrative Office account for 9 percent of the participants in this plan. The obligation for the remaining participants under the multiple-employer plan continues to be the proportionate responsibility of each diocesan entity.

The plan provides for retirement benefits to priests working in the Dioceses of San Diego and San Bernardino, after ten years of participation in the Priest Plan the employee is 100 percent vested. Besides the Administrative Office, the Priest Plan includes priests of the parishes, schools, and other Catholic entities operating within the Dioceses of San Diego and San Bernardino.

San Diego Diocese Post-Retirement Benefit Plan for Priests – As of June 30, 2017, the date of the latest actuarial report, the defined benefit pension program for priests had an actuarial present value of accumulated health benefits of \$11 million. Under accounting guidance for multiple employer pension plans, this obligation is not reported as a liability in these financial statements. Priests working for the Administrative Office account for 9 percent of the participants in this plan. The obligation for the remaining participants under the multiple employer plan continues to be the proportionate responsibility of each of the diocese respective entities.

The plan provides for post-retirement benefits for priests that have reached retirement age. These benefits consist primarily of supplemental health insurance, assisted living and automobile insurance. For fiscal year 2017, these costs totaled \$1,212,292. Besides the Administrative Office, the San Diego Post-Retirement Benefit Plan includes priests of the parishes, schools, and other Catholic entities operating within the Diocese.

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The Administrative Office collected agency funds for priest pension and post-retirement benefits from parishes, schools and other entities totaling \$1,729,031 during the year ended June 30, 2017.

Note 16. Self-insurance

The Administrative Office provides insurance for Diocesan parishes, schools, other Catholic entities and the Administrative Office. The Administrative Office treats insurance that is provided by a third party vendor as an agency transaction and records the net amount of funds received and premiums paid on behalf of the various parishes and schools.

The Administrative Office provides insurance in the form of self-insurance plans for workers' compensation, unemployment benefits and a portion of health insurance. The Administrative Office reports these premiums received at the gross amounts and records expense for actual claims and an estimate of claims incurred but not received.

The Administrative Office provides the following self-insurance:

Workers' Compensation – The Administrative Office maintains a self-insured workers' compensation program for the Diocese, parishes, schools and other Catholic entities in San Diego and Imperial Counties. The Administrative Office bills each entity a premium based on salaries and job classifications. A third-party administrator reviews and processes the workers' compensation claims. The amount collected by the Administrative Office is used to purchase excess liability insurance and to pay claims, fees, and administrative costs. The Administrative Office has established a liability for claims incurred but not yet paid of \$1,450,000. This estimate is based on information provided by the third-party administrator.

Unemployment Benefits – The Administrative Office maintains a self-insured unemployment insurance program for the Diocese, parishes, schools, and other Catholic entities in San Diego and Imperial Counties. The Administrative Office bills each entity a premium based on salaries and job classifications. The Administrative Office has established a liability for estimated unemployment claims of \$100,000.

Health and Other Personal Insurance – In April 2010, the Administrative Office began self-insuring for a portion of health and dental. The Diocese is reinsured for catastrophic claims. This insurance is provided for the Diocese, parishes, schools and other Catholic entities. Premiums are based on the coverage provided. The Administrative Office has established a liability for estimated claims incurred but not reported in the amount of \$1,500,000. This estimate was based on information provided by the plan administrator.

Note 17. Legal Matters

There are routine claims and suits that are pending against the Diocese which are being defended by the Diocese's insurance company. The Diocese believes the insurance coverage should be adequate to pay any prospective judgment or settlement. There are no known judgments or settlements at June 30, 2017, and no amounts have been accrued in the financial statements.

Note 18. June 30, 2016 Financial Information

The financial statements include certain prior year summarized comparative information in total, but not by net asset class. Such prior year information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Administrative Office's financial statements for the year ended June 30, 2016, from which the summarized information was derived.

Certain reclassifications have been made to the summarized 2016 financial information to conform to the classifications adopted for the 2017 financial statements. These reclassifications had no effect on the change in net assets.