

THE EPISCOPAL CHURCH IN THE  
DIOCESE OF CALIFORNIA

DECEMBER 31, 2012

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INDEPENDENT AUDITORS' REPORT

FINANCIAL STATEMENTS,

AND

SUPPLEMENTAL INFORMATION

# The Episcopal Church in the Diocese of California

## Independent Auditors' Report and Financial Statements

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## **Independent Auditors' Report**

THE BOARD OF DIRECTORS  
THE EPISCOPAL CHURCH IN THE  
DIOCESE OF CALIFORNIA  
San Francisco, California

## **Report on the Financial Statements**

We have audited the accompanying financial statements of **THE EPISCOPAL CHURCH IN THE DIOCESE OF CALIFORNIA (the Diocese)** which comprise the statement of financial position as of December 31, 2012, 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 consolidated 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 policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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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 Episcopal Church in the Diocese of California as of December 31, 2012, 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.

### **Report on Summarized Comparative Information**

We have previously audited the Diocese's December 31, 2011 financial statements, and we expressed an unmodified opinion on those audited financial statements in our report dated June 26, 2012. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2011, is consistent, in all material respects, with the audited financial statements from which it has been derived.

### **Report on Supplementary Information – Report on Changes in Fund Asset Balance**

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying changes in fund asset balance is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*Hood & Strong LLP*

San Francisco, California  
June 28, 2013

# The Episcopal Church in the Diocese of California

## Statement of Financial Position

December 31, (with comparative totals for 2011)

	2012					2011 Total
	Operating	Custodial and Unexpended Income	Endowment and Trust	Deferred Gifts	Total All Funds	
<b>Assets:</b>						
Cash and cash equivalents	\$ 2,336,099	\$ 1,708	\$ 19,411		\$ 2,357,218	\$ 3,572,421
Receivables, net	2,432,892				2,432,892	1,782,913
Investments	196,137		16,935,924	\$ 18,222,444	35,354,505	32,475,372
Notes receivable	2,803,307				2,803,307	2,627,445
Notes receivable held for investment, net		2,300			2,300	2,300
Equity interests in real property	43,949	100,000	1,087,500		1,231,449	1,231,449
Property and equipment, net	4,504,708				4,504,708	4,198,086
Due to/from other funds	(1,798,016)	559,436	1,238,580		-	
<b>Total assets</b>	<b>\$ 10,519,076</b>	<b>\$ 663,444</b>	<b>\$ 19,281,415</b>	<b>\$ 18,222,444</b>	<b>\$ 48,686,379</b>	<b>\$ 45,889,986</b>
<b>Liabilities and Net Assets</b>						
<b>Liabilities:</b>						
Accounts payable and accrued expenses	\$ 983,501				\$ 983,501	\$ 824,958
Accounts payable, related parties					-	340,519
Deferred revenue	53,921				53,921	12,966
Line of credit	3,129,001				3,129,001	2,718,945
Funds held in trusts for beneficiaries				\$ 14,930,953	14,930,953	14,203,237
<b>Total liabilities</b>	<b>4,166,423</b>			<b>14,930,953</b>	<b>19,097,376</b>	<b>18,100,625</b>
<b>Net Assets:</b>						
Unrestricted	5,894,734		\$ (652,316)		5,242,418	4,726,456
Unrestricted-board designated	457,919				457,919	470,679
<b>Total unrestricted</b>	<b>6,352,653</b>		<b>(652,316)</b>		<b>5,700,337</b>	<b>5,197,135</b>
Temporarily restricted		\$ 663,444	11,150,091	611,590	12,425,125	11,517,153
Permanently restricted			8,783,640	2,679,901	11,463,541	11,075,073
<b>Total net assets</b>	<b>6,352,653</b>	<b>663,444</b>	<b>19,281,415</b>	<b>3,291,491</b>	<b>29,589,003</b>	<b>27,789,361</b>
<b>Total liabilities and net assets</b>	<b>\$ 10,519,076</b>	<b>\$ 663,444</b>	<b>\$ 19,281,415</b>	<b>\$ 18,222,444</b>	<b>\$ 48,686,379</b>	<b>\$ 45,889,986</b>

The accompanying notes are an integral part of this statement.

# The Episcopal Church in the Diocese of California

## Statement of Activities

	2012					2011 Total
	Operating	Custodial and Unexpended Income	Endowment and Trust	Deferred Gifts	Total All Funds	
<b>Support and Revenue:</b>						
Parish and mission assessments	\$ 3,109,516				\$ 3,109,516	\$ 3,323,315
Gifts, grants and other	449,200	\$ 455,424	\$ 30,000		934,624	1,634,459
Change in value				\$ 383,054	383,054	(203,943)
Investment income, net	21,006		2,140,151		2,161,157	(1,047,693)
<b>Total support and revenue</b>	<b>3,579,722</b>	<b>455,424</b>	<b>2,170,151</b>	<b>383,054</b>	<b>6,588,351</b>	<b>3,706,138</b>
<b>Expenses:</b>						
Episcopate	582,871				582,871	518,984
Finance	507,426				507,426	469,487
Administration	889,635				889,635	848,079
Planned giving	210,724				210,724	176,308
Congregational development	494,839				494,839	305,336
Ministry development	160,282				160,282	177,699
Youth & young adult	140,643				140,643	78,847
Multicultural ministry	42,054				42,054	319,861
Communications	157,227				157,227	211,106
Support services-outside Diocese	711,000				711,000	746,741
Other ministry	139,994				139,994	139,911
Justice, peace, and integrity	24,735				24,735	25,489
Payments to beneficiaries and other custodial fund disbursements	727,279				727,279	790,315
<b>Total expenses</b>	<b>4,788,709</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>4,788,709</b>	<b>4,808,163</b>
<b>Changes in Net Assets Before</b>						
<b>Transfers &amp; Reclasses</b>	(1,208,987)	455,424	2,170,151	383,054	1,799,642	(1,102,025)
Interfund transfer		(436,226)	436,226		-	
Releases from Restrictions	1,224,650	(351,656)	(872,994)			
<b>Change in Net Assets</b>	<b>15,663</b>	<b>(332,458)</b>	<b>1,733,383</b>	<b>383,054</b>	<b>1,799,642</b>	<b>(1,102,025)</b>
<b>Net Assets, beginning of year</b>	<b>6,336,990</b>	<b>\$ 995,902</b>	<b>\$ 17,548,032</b>	<b>\$ 2,908,437</b>	<b>27,789,361</b>	<b>28,891,386</b>
<b>Net Assets, end of year</b>	<b>\$ 6,352,653</b>	<b>\$ 663,444</b>	<b>\$ 19,281,415</b>	<b>\$ 3,291,491</b>	<b>\$ 29,589,003</b>	<b>\$ 27,789,361</b>
<b>Fund Balances by Classification</b>						
<b>Net Assets, beginning of year</b>						
Unrestricted Net Assets	\$ 6,336,990	-	(1,139,855)	-	5,197,135	\$ 4,927,932
Temporarily Restricted Net Assets	-	995,902	9,934,247	587,004	11,517,153	13,126,070
Permanently Restricted Net Assets	-	-	8,753,640	2,321,433	11,075,073	10,837,384
<b>Net Assets, beginning of year</b>	<b>\$ 6,336,990</b>	<b>\$ 995,902</b>	<b>\$ 17,548,032</b>	<b>\$ 2,908,437</b>	<b>\$ 27,789,361</b>	<b>\$ 28,891,386</b>
<b>Changes in Net Assets:</b>						
Unrestricted Net Assets	\$ 15,663		\$ 487,539		\$ 503,202	\$ 269,203
Temporarily Restricted Net Assets		\$ (332,458)	1,215,844	\$ 24,586	907,972	(1,608,917)
Permanently Restricted Net Assets			30,000	358,468	388,468	237,689
<b>Changes in Net Assets</b>	<b>\$ 15,663</b>	<b>\$ (332,458)</b>	<b>\$ 1,733,383</b>	<b>\$ 383,054</b>	<b>\$ 1,799,642</b>	<b>(1,102,025)</b>
<b>Net Assets, end of year</b>						
Unrestricted Net Assets	6,352,653		(652,316)		\$ 5,700,337	\$ 5,197,135
Temporarily Restricted Net Assets		663,444	11,150,091	611,590	12,425,125	11,517,153
Permanently Restricted Net Assets			8,783,640	2,679,901	11,463,541	11,075,073
<b>Net Assets, end of year</b>	<b>\$ 6,352,653</b>	<b>\$ 663,444</b>	<b>\$ 19,281,415</b>	<b>\$ 3,291,491</b>	<b>\$ 29,589,003</b>	<b>\$ 27,789,361</b>

The accompanying notes are an integral part of this statement.

# The Episcopal Church in the Diocese of California

## Statement of Cash Flows

<i>Year Ended December 31, 2012 (with comparative totals for 2011)</i>	2012	2011
<b>Cash Flows from Operating Activities:</b>		
Changes in net assets	\$ 1,799,642	\$ (1,102,025)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	78,919	86,707
Net realized and unrealized (gain) loss on investments	(1,336,927)	1,462,567
Loss on disposal of fixed assets	1,646	
Change in charitable remainder unitrusts	(383,053)	517,782
Increase (decrease) in operating assets and liabilities:		
Receivables	(649,979)	(18,713)
Accounts payable and accrued expenses	158,543	(17,646)
Accounts payable, related party	(340,519)	137,282
Deferred revenue	40,956	(150,970)
Net cash (used) provided by operating activities	(630,772)	914,984
<b>Cash Flows from Investing Activities:</b>		
Purchases of investments	(551,331)	(21,424,030)
Proceeds from sale of investments	119,880	22,057,534
Principal payments received on notes receivable held for investments		118,124
Purchases of property and equipment	(387,174)	(45,459)
Borrowings from Line of Credit - net	234,194	91,500
Net cash (used) provided by investing activities	(584,431)	797,669
<b>Net (Decrease) Increase in Cash and Cash Equivalents</b>	(1,215,203)	1,712,653
<b>Cash and Cash Equivalents, beginning of year</b>	3,572,421	1,859,768
<b>Cash and Cash Equivalents, end of year</b>	<b>\$ 2,357,218</b>	<b>\$ 3,572,421</b>

The accompanying notes are an integral part of this statement.

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

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### Note 1 - Summary of Significant Accounting Policies:

a. Organization

The Episcopal Church in the Diocese of California (the Diocese) is a nonprofit entity that administratively supports Episcopal parishes and other ancillary institutions throughout the San Francisco Bay Area in the State of California. The Diocese is governed by the Executive Council which is the legal board of directors of the Diocesan Corporation.

b. Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting and, accordingly, reflect all significant receivables, payables, and other liabilities, including deferred revenue. The principles of “fund accounting” are utilized in order to provide a more detailed accountability for the funds entrusted to the Diocese.

c. Basis of Presentation

Financial statement presentation follows the recommendations of the Accounting Standards Codification (ASC) 958, *Not-for-Profit Entities*. Under ASC 958, the Diocese is required to report information regarding its financial position and activities according to three classes of net assets:

*Unrestricted Net Assets.* The portion of net assets that is neither temporarily restricted nor permanently restricted by donor-imposed stipulations.

*Temporarily Restricted Net Assets.* The portion of net assets whose use by the organization is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the Diocese.

*Permanently Restricted Net Assets.* The portion of net assets whose use by the organization is limited by donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of the Diocese.

d. Cash and Cash Equivalents

For purposes of the Statement of Cash Flows, cash and cash equivalents include time deposits and all highly liquid debt instruments with original maturities of three months or less.

e. Receivables

Receivables consist of amounts due to the Diocese from parishes that are within the Diocese of California and represent assessments, reimbursable expenses, and other receivables. The Diocese records bad debts using the allowance method.



# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

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f. Fair Value Measurements

The Diocese carries certain assets and liabilities at fair value. Fair value is defined as 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. The Diocese classifies its financial assets and liabilities according to three levels, and maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value.

Level 1 – Quoted market prices (unadjusted) in active markets for identical assets or liabilities that the entity has the ability to access at the measurement date.

Level 2 – Observable inputs other than quoted prices included within Level 1 for the asset or liability, either directly or indirectly.

Level 3 – Unobservable inputs for the asset or liability that are not corroborated by market data.

g. Notes Receivable Held for Investment

Notes receivable held for investment consists of notes to several churches. The notes bear interest at prime rates and are due through 2016. The notes are secured by property or unsecured and are recorded net of an allowance related to interest accruals.

h. Equity Interest in Real Property

Equity interest in real property consists of property owned by the Diocese, and amounts funded by the Diocese for the purchase of property by related parties. The Diocese has an equity interest in the property for the amount of the purchase price funded by the Diocese. This interest is recorded at cost.

i. Property and Equipment

Purchased property and equipment is recorded at cost. Donated property is valued at fair value at time of donation. Depreciation is provided on a straight-line basis over the estimated useful lives (five to thirty years) of the related assets. Maintenance and repairs are charged to expense as incurred. Significant betterments and renewals are capitalized. The Diocese has elected not to depreciate its real property and has determined that the effect on the financial statements is not material as of December 31, 2012.

j. Deferred Revenue

Deferred revenue consists of assessments, payroll, and benefits received from parishes in advance of the period to which they relate.

k. Recognition of Support and Revenue

Current year parish and mission assessments have been prepared on the accrual basis of accounting.

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

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Gifts and grants are recognized when the donor makes an unconditional promise to give to the Diocese. Donor-restricted gifts and grants are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets.

Investment income is recognized as revenue when earned. Investment income earned on permanently restricted net assets is recorded as an increase or decrease in temporarily restricted net assets unless specifically restricted as permanent by the donor.

l. Income Taxes

The Diocese is a tax exempt organization under the provision of the Internal Revenue Code, Section 501(c)(3), and the related state provisions. Accordingly, no provision for income taxes has been reflected in these financial statements.

The Diocese follows the guidelines of the Financial Accounting Standards Board (FASB) ASC Topic 740 for accounting for uncertainty in income taxes. As of December 31, 2012, management evaluated the Diocese's tax positions and concluded that the Diocese had maintained its tax exempt status and has taken no uncertain tax positions that require adjustment to the financial statements. Therefore, no provision or liability for income taxes has been included in the financial statements.

m. 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 reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

n. Subsequent Events

The Diocese has reviewed the changes in net assets for the period of time from December 31, 2012 through June 28, 2013, the date the financial statements are available to be issued, and have determined that no adjustments are necessary to the amounts reported in the accompanying financial statements nor subsequent events have occurred, the nature of which would require disclosure.

o. Comparative Financial Information

The financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with GAAP. Accordingly, such information should be read in conjunction with the Diocese's financial statements for the year ended December 31, 2011, from which the summarized information was derived.

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

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### Note 2 - Description of Funds:

a. Operating Fund

This fund is used to account for all expenditures related to unrestricted support and revenue. The Board of Directors of the Diocese has set aside certain donor unrestricted funds for certain designated uses. These funds are included in the operating fund as board designated.

b. Custodial and Unexpended Income Fund

This fund is used to account for gifts and grants designated for specific projects or programs by donors. The fund balance is classified as temporarily restricted on the statement of financial position.

c. Endowment and Trust Fund

This fund is used to account for assets contributed by donors that are subject to various restrictions, both temporary and permanent. The Diocese is responsible to assure that distributions be made in accordance with the provisions of each trust. When the market value of permanently restricted funds fall below the historical value, the deficiency is reflected as unrestricted net assets. At the end of 2012, this deficiency decreased to \$652,316. The permanently restricted net assets represent the historic value of additions to the endowment, and the temporarily restricted net assets represent appreciation of the endowment and the trust fund balances.

d. Deferred Gifts Fund

This fund is used to account for funds held in trust and administered by the Diocese, the income of which is payable to individual beneficiaries. Income earned but not paid to beneficiaries is treated as a liability, which is included with "Funds Held in Trust for Beneficiaries". Upon the expiration of the income beneficiaries' interest, the principal will be distributed in accordance with the conditions prescribed by the Charitable Remainder Unitrust agreements. Any principal that will ultimately be distributed to third party beneficiaries has been recorded as a liability, "Funds Held in Trust for Beneficiaries." The remainder is distributable to the Diocese and is stated at the estimated present value, which is calculated based on the actuarial life expectancy of the donor or designees. The discount rate used, ranging between 5% and 6.5%, approximates the 30 year U.S. Treasury Bond rate in the year of origination. The fund balances are a combination of permanently restricted net assets and temporarily restricted net assets on the statement of financial position.

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

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### Note 3 - Receivables:

Receivables consist of the following at December 31, 2012 and 2011:

	2012	2011
Assessments	\$ 241,384	\$ 151,024
Reimbursable expenses from related entities, net of allowance	1,812,172	1,195,763
Other receivables	379,336	436,126
	<hr/>	<hr/>
	\$ 2,432,892	\$ 1,782,913

### Note 4 - Investments:

The fair value of investments at December 31, 2012 and 2011 is as follows:

	2012	2011
Mutual funds	\$ 17,132,061	15,363,698
Charitable trusts	18,222,444	17,111,674
	<hr/>	<hr/>
	\$ 35,354,505	\$ 32,475,372

Investment income for the years ended December 31, 2012 and 2011 consists of the following:

Interest and dividends, net of management fees	\$ 316,347	\$ 402,155
Realized gains and losses	252,781	(360,532)
Unrealized gains and losses	1,592,028	(1,089,316)
	<hr/>	<hr/>
	\$ 2,161,156	\$ (1,047,693)

Investment income is included in:

Unrestricted net assets	\$ 508,546	\$ (588,623)
Temporarily restricted net assets	1,652,610	(459,070)
	<hr/>	<hr/>
	\$ 2,161,156	\$ (1,047,693)

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

The table below presents the balances of assets measured at fair value at December 31, 2012 on a recurring basis:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>
Investments:			
Mutual Funds:			
Intermediate Duration			
Institutional	\$16,935,924	\$16,935,924	
Emerging Markets Fund	196,137	196,137	
Charitable Trusts:			
Cash & Equivalents	595,068		\$ 595,068
Domestic REIT	1,422,369		1,422,369
Emerging Markets Stocks	660,546		660,546
High Quality Bond Funds	2,223,978		2,223,978
High Quality Bonds	221,396		221,396
High Yield Bond Funds	396,468		396,468
International Bond Funds	845,614		845,614
International REIT	962,740		962,740
International Stocks	2,431,297		2,431,297
International Small Co. Stocks	431,312		431,312
Investment Grade Bond Funds	1,905,427		1,905,427
Large Co. Stocks	4,864,690		4,864,690
Small Co. Stocks	1,261,539		1,261,539
Total assets measured at fair value	\$35,354,505	\$17,132,061	\$18,222,444

There are no investments measured at level 3.

### *Financial Investments not Measured at Fair Value*

Some of the Diocese's financial instruments are not measured at fair value on a recurring basis but nevertheless are recorded at amounts that approximate fair value due to their liquid or short-term nature. Such assets and liabilities include: Cash and cash equivalents, receivables, other investments, notes receivable, equity interest in real property, payables, deferred revenue and line of credit.

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

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### Note 5 - Charitable Remainder Unitrusts:

The Diocese is the trustee for various charitable remainder unitrusts, which have been invested. These investments represent gifts received subject to certain restrictions on the distribution of income and the assets of the unitrust. The unitrust agreements specify the beneficiaries of the income and the assets.

The charitable remainder unitrust agreements provide for annuity payments to donors of 5% to 10%. The Diocese records this investment at fair market value. The estimated liability is based upon the annuity payments and donor life expectancy using a discount rate of 5% to 6.5% (as of gift receipt date) and is classified as funds held in trust for beneficiary.

The investments in charitable remainder unitrusts consist of the following at December 31, 2012 and 2011:

	2012	2011
Funds (See Note 4)	\$ 18,222,444	\$ 17,111,674
Less funds held in trust for beneficiaries	(14,930,953)	(14,203,237)
	<u>\$ 3,291,491</u>	<u>\$ 2,908,437</u>

The contribution revenue and changes in value of charitable remainder trusts recognized under such agreements for the year ended December 31, 2012 and 2011 are the following:

	2012	2011
Change in value	\$ 383,054	\$ (203,943)
Net change in unitrusts	<u>\$ 383,054</u>	<u>\$ (203,943)</u>

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

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### Note 6 - Equity Interests in Real Property:

Equity interests in real property, which are recorded at cost, consist of the following at December 31, 2012 and 2011:

	2012	2011
24% equity interest in real property owned by Bayani Rico	\$ 43,949	\$ 43,949
31% equity interest in real property owned by the Culmers	160,000	160,000
22% equity interest in real property owned by the Mission Clergy Person, Sue Thompson	100,000	100,000
50% equity interest in real property owned by the former Bishop	927,500	927,500
	<hr/>	<hr/>
	\$ 1,231,449	\$ 1,231,449

### Note 7 - Property and Equipment:

At December 31, 2012 and 2011, property and equipment consisted of the following:

	2012	2011
Diocesan House	\$ 1,071,447	\$ 1,047,630
S. F. Campus Center partial interest	30,000	30,000
Computers/server	104,036	112,303
Other furniture and equipment	95,884	82,240
Automobile	27,108	27,108
Hearst Street, Berkeley	649,669	649,669
Bishop's Residence	1,112,605	1,112,605
Bishop's Residence Improvements	405,850	72,707
Construction in Progress	-	9,744
	<hr/>	<hr/>
	3,496,599	3,144,006
Less accumulated depreciation	(808,104)	(762,133)
	<hr/>	<hr/>
	2,688,495	2,381,873
Land	1,816,213	1,816,213
	<hr/>	<hr/>
	\$ 4,504,708	\$ 4,198,086

Depreciation expense for the years ended December 31, 2012 and 2011 was \$78,919 and \$86,707, respectively.

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

### Note 8 - Line of Credit:

The Diocese has an unsecured line of credit agreement with Union Bank of California under which the Diocese may borrow up to \$9,500,000; bearing interest at the prime rate (3.25%); interest payable monthly; principal due on October 1, 2014.

Total principal payments due to Union Bank on the line of credit are \$3,129,001 at December 31, 2012. This debt is incurred by the Diocese on behalf of various parishes and missions as follows:

<i>December 31, 2012</i>	Line of Credit and Other Notes Payable	Corresponding Receivable
<b>Parishes:</b>		
Lafayette, St. Anselm's	\$ 3,704	\$ 3,704
Pleasanton, St. Clare's	577,427	577,427
San Francisco, St. Aidan's	31,800	31,800
San Leandro, All Saints'	28,937	28,937
Pleasant Hill, Resurrection	20,966	20,966
Danville, St. Timothy's	557,913	557,913
Concord, St. Michael and All Angels	59,500	59,500
Berkeley, St. Mark's	253,855	253,855
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Total parishes	1,534,102	1,534,102
<b>Other Properties:</b>		
Berkeley Emergency Food and Housing	120,195	120,195
Episcopal Community Services	250,000	250,000
Episcopal Diocese	325,694	
St. Dorothy's Rest	899,010	899,010
<hr/>		
Total other properties	1,594,899	1,269,205
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Total	\$ 3,129,001	\$ 2,803,307



# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

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### Note 9 - Endowment Funds:

The Diocese's endowments consist of 103 individual funds, established to fund general operations of the Diocese or specific congregations and programs in the Diocese. Its endowment includes donor-restricted endowment funds and funds designated by the Executive Council to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the Executive Council to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

In 2008, the Diocese implemented ASC 958-205 *Reporting Endowment Funds* which was effective for fiscal years ending after December 15, 2008. The state of California adopted a version of the Uniform Prudent Management of Institutional Funds Act as its State Prudent Management of Institutional Funds Act (SPMIFA) which is applicable to funds established on or after January 1, 2009 and funds established prior to January 1, 2009 only with respect to actions taken after January 1, 2009.

SPMIFA moves away from the concept of corpus with its "historical dollar value" in an endowment. Charities are encouraged to develop spending policies that are responsive to short term fluctuations in the value of the fund, preserve the value of the fund for future use, and honor the charitable purpose of the fund. The Diocese will continue to balance the endurance of its funds and the needs of the community in its spending policy and practices.

#### *Interpretation of Relevant Law*

The Diocese considers the fair value of its endowment funds to be the value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary.

The Diocese 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 organization in a manner consistent with the standard of prudence prescribed by SPMIFA.

In accordance with SPMIFA, the organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) The duration and preservation of the fund, (2) The purposes of the organization and the donor-restricted endowment fund, (3) General economic conditions, (4) The possible effect of inflation and deflation, (5) The expected total return from income and the appreciation of investments, (6) Other resources of the organization, (7) The investment policies of the organization.

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

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From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or SPMIFA requires the Diocese to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were \$ 652,316 and \$1,139,855 as of December 31, 2012 and 2011, respectively.

### *Return Objectives and Risk Parameters*

The Diocese has adopted investment and spending policies for endowment assets that will ultimately provide a predictable stream of funding to provide support for the various programs and ministries of the Diocese of California. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity as well as board-designated funds. Under this policy, as approved by the Executive Council, the endowment assets are invested in a manner that is intended to realize a competitive rate of return comparable to index benchmarks.

### *Strategies Employed for Achieving Objectives*

To satisfy its long-term rate-of-return objectives, the Diocese relies on a diversified asset investment strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Diocese 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.

### *Spending Policy and How the Investment Objectives Relate to Spending Policy*

The Diocese is expecting to provide annual distributions of 5% of the market value of the portfolio as calculated on a 3 year rolling average. The investment managers are required to invest funds so as to ensure that required distributions of income or principal are met.

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

Net changes in endowment funds for the year ended December 31, 2012 were as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Net Assets, December 31, 2011	\$ (1,139,855)	\$ 9,934,247	\$ 8,753,640	\$ 17,548,032
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Investment Return:				
Income		569,786		569,786
Net appreciation	487,539	1,082,824		1,570,365
<hr/>				
Total investment return	487,541	1,652,610		2,140,151
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Contributions			30,000	30,000
Depreciation of endowment assets		(986,464)		(986,464)
Interfund transfer		549,698		549,698
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Endowment Net Assets, December 31, 2012	\$ (652,316)	\$ 11,150,091	\$ 8,783,640	\$ 19,281,415

### Note 10 - Net Assets:

Temporarily restricted net assets are restricted for specific purposes as of December 31, 2012.

	Custodial	Endowment	Deferred Gifts	Total
Support Diocese	\$ 322,750	\$ 3,474,856	\$ 443,874	\$ 4,241,480
Education		52,812	45,377	98,189
Congregational Support		1,710,136	110,673	1,820,809
Congregational Development	125,498	1,927,264		2,052,762
Social Ministry	24,387	2,166,148	11,666	2,202,201
Scholarships	190,809	1,818,875		2,009,684
<hr/>				
	\$ 663,444	\$ 11,150,091	\$ 611,590	\$ 12,425,125

Net assets were released from donor restrictions by incurring expenses satisfying the purpose of the restriction for the year ended December 31, 2012 and 2011.

# The Episcopal Church in the Diocese of California

## Notes to Financial Statements

Permanently restricted net assets are invested in perpetuity with the income available to support the programs of the Diocese as of December 31, 2012 are as follows:

	Endowment	Deferred Gifts	Total
Support Diocese	\$ 5,955,735	\$ 774,947	\$ 6,730,682
Education	217,197	326,630	543,827
Congregational Support	1,565,080	618,397	2,183,477
Congregational Development	318,952	172,124	491,076
Social Ministry	525,860	787,803	1,313,663
Scholarships	200,816		200,816
	<u>\$ 8,783,640</u>	<u>\$2,679,901</u>	<u>\$ 11,463,541</u>

### Note 11 - Retirement Plans:

The Diocese funds defined contribution pension plans covering lay employees. The Diocese contributes between 5% and 9% of employee compensation depending upon the employee contribution. The 2012 and 2011 contribution by the Diocese to the defined contribution pension plans approximated \$54,763 and \$50,302, respectively.

The Diocese also provides pension benefits for the clergy through a national plan. The plan is a defined benefit pension plan funded by specific assessments charged to the Diocese based on a specified percentage of compensation. In 2012 and 2011, the Diocese contributed approximately \$114,706 and \$135,698 (18% of compensation), respectively, to the clergy defined benefit pension plan.

### Note 12 - Concentrations of Credit Risk:

The Diocese has identified its financial instruments which are potentially subject to credit risk. These financial instruments consist principally of cash and cash equivalents, investments in securities, and notes receivable held for investment.

The Diocese invests its cash deposits with three financial institutions. Periodically, throughout the year, the Diocese has maintained balances in operation and money market accounts in excess of federally insured limits.

Investments in securities are diversified into various equity instruments and other investment securities in order to limit the concentration of market risk.

The Diocese bills and collects assessment revenue from the various parishes. Assessment revenues comprised 70% of all non investment revenue the Diocese received in 2012.

## The Episcopal Church in the Diocese of California

### Changes in Fund Asset Balance (See Independent Auditors' Report on Changes in Fund Asset Balance)

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*Year Ended December 31, 2012*

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	Operating	Custodial and Unexpended Income	Endowment and Trust	Deferred Gifts	Total All Funds
<b>Beginning Balance - December 31, 2011</b>	\$ 6,336,990	\$ 995,902	\$ 17,548,032	\$ 2,908,437	\$ 27,789,361
<b>Income:</b>					
Assessment income	3,109,516				3,109,516
Gifts and grants	449,200	455,424	30,000		934,624
Investment income, net	21,006				21,006
Realized and unrealized gains			2,140,151	383,054	2,523,205
<b>Expenses:</b>					
Operating departments (exclude payments to beneficiaries and other custodial)	(4,061,429)				(4,061,429)
<b>Interfund Transfer:</b>					
Endowments Fund to Operating Fund	872,994		(872,994)		
Less: payments to beneficiaries	(385,585)				(385,585)
Custodial Funds to Operating Fund	351,656	(351,656)			
Less: payments to beneficiaries	(341,695)				(341,695)
Custodial Fund to Endowment Fund		(436,226)	436,226		
<b>Ending Balance - December 31, 2012</b>	\$ 6,352,653	\$ 663,444	\$ 19,281,415	\$ 3,291,491	\$ 29,589,003

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