

**Central Administrative Office of the  
Catholic Diocese of Arlington and  
Affiliate**

**Combined Financial Statements  
as of June 30, 2014 and 2013 and Report Thereon**

**Central Administrative Office of the Catholic Diocese  
of Arlington and Affiliate  
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June 30, 2014 and 2013**

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## INDEPENDENT AUDITORS' REPORT

Most Reverend Paul S. Loverde  
Bishop of the Catholic Diocese of Arlington  
Central Administrative Office of the Catholic Diocese  
Arlington, Virginia

We have audited the accompanying combined financial statements of the Central Administrative Office of the Catholic Diocese of Arlington and its affiliate (the Chancery), which comprise the combined statements of financial position as of June 30, 2014 and 2013, and the related combined statements of activities and cash flows for the years 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 financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditors' Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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 auditors' 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.

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 combined financial statements referred to above present fairly, in all material respects, the financial position of the Chancery as of June 30, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*CliftonLarsonAllen LLP*

**CliftonLarsonAllen LLP**

St. Cloud, Minnesota  
October 28, 2014



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**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Combined Statements of Financial Position  
As of June 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
<b>Assets</b>		
Cash and cash equivalents	\$ 9,828,762	\$ 13,602,550
Accounts receivable, net	1,782,586	1,259,285
Accrued interest receivable	157,131	161,468
Bishop's Lenten Appeal pledges receivable	3,771,899	2,994,979
Bequests and major gifts pledges receivable	10,779,755	2,006,037
Investments	200,950,676	164,087,337
Prepaid expenses and other assets	852,589	631,029
Unamortized bond costs	171,174	525,716
Bond defeasance escrow	-	22,849,681
Interest rate swap agreement	338,502	553,399
Demand notes and loans receivable		
Paul VI High School	3,798,634	4,028,557
200 North Glebe Road, Inc.	4,034,286	4,334,286
Property, equipment and land, net	106,710,155	108,388,031
Construction in progress and assets not yet placed in service	1,583,282	-
Land restricted for high school	14,500,000	14,500,000
Total assets	<u>\$ 359,259,431</u>	<u>\$ 339,922,355</u>
<b>Liabilities and Net Assets</b>		
<b>Liabilities</b>		
Deposits held in custody for others	\$ 1,683,260	\$ 1,295,753
Accounts payable and accrued expenses	5,444,284	4,971,094
Accrued interest payable	41,892	319,581
Unearned revenue	57,393	56,476
Notes payable, net of discount	103,130	164,087
Amounts held on behalf of other diocesan entities	89,131,460	70,169,109
Annuity payment liability	270,189	260,541
Arlington Diocese Educational Foundation (ADEF) funds		
held for schools	2,651,903	2,484,996
Accrued pension liability, priests	6,707,287	7,049,275
Postretirement health benefit obligation	8,677,709	7,484,062
Defeased bonds payable	-	22,070,000
Bonds payable	20,479,836	21,335,573
Total liabilities	<u>135,248,343</u>	<u>137,660,547</u>
<b>Net assets</b>		
<b>Unrestricted</b>		
Current operations	35,856,836	29,890,401
Invested in property, equipment and land	91,838,276	92,677,805
Functioning as endowment	11,761,241	9,625,921
Designated	10,395,939	10,706,051
Total unrestricted	<u>149,852,292</u>	<u>142,900,178</u>
Temporarily restricted	50,368,033	37,871,148
Permanently restricted	23,790,763	21,490,482
Total net assets	<u>224,011,088</u>	<u>202,261,808</u>
Total liabilities and net assets	<u>\$ 359,259,431</u>	<u>\$ 339,922,355</u>

*The accompanying notes are an integral part of these combined financial statements.*

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Combined Statement of Activities**  
**For the year ended June 30, 2014**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Operating revenues and support				
Bishop's Lenten Appeal	\$ 16,244,788	\$ -	\$ -	\$ 16,244,788
Operational assessment	7,428,795	-	-	7,428,795
Investment income for operations	1,460,000	-	-	1,460,000
Transmittal fees	149,142	-	-	149,142
Contributions, bequests and major gifts	1,098,700	17,552,803	2,300,281	20,951,784
Program revenue	2,518,054	-	-	2,518,054
Other revenue and support	-	-	-	-
Satisfaction of temporary restrictions	10,731,374	(10,731,374)	-	-
Total operating revenues and support	<u>39,630,853</u>	<u>6,821,429</u>	<u>2,300,281</u>	<u>48,752,563</u>
Operating expenses				
Program services				
Pastoral	8,953,819	-	-	8,953,819
Religious personnel development	3,314,166	-	-	3,314,166
Education	10,374,890	-	-	10,374,890
Social services	4,170,585	-	-	4,170,585
Supporting services				
Diocesan administration and parochial support	11,838,556	-	-	11,838,556
Bishop's Lenten Appeal	783,085	-	-	783,085
Total operating expenses	<u>39,435,101</u>	<u>-</u>	<u>-</u>	<u>39,435,101</u>
Change in net assets from operations	<u>195,752</u>	<u>6,821,429</u>	<u>2,300,281</u>	<u>9,317,462</u>
Other changes in net assets				
Investment income less amount included in operations, net	8,298,281	7,201,456	-	15,499,737
Bond interest and related expenses	(1,273,900)	-	-	(1,273,900)
Unrealized loss on swap agreement	(214,897)	-	-	(214,897)
Insurance programs	318,199	-	-	318,199
Change in unfunded pension liability, priests	(1,158,012)	-	-	(1,158,012)
Change in unfunded postretirement health obligation	(1,193,647)	-	-	(1,193,647)
Net property gains	310,104	-	-	310,104
Rental income - diocesan properties	1,459,152	-	-	1,459,152
Loan reserve increase - related party	(1,314,918)	-	-	(1,314,918)
Satisfaction of temporary restrictions	1,526,000	(1,526,000)	-	-
Total other changes in net assets	<u>6,756,362</u>	<u>5,675,456</u>	<u>-</u>	<u>12,431,818</u>
Change in net assets	6,952,114	12,496,885	2,300,281	21,749,280
Net assets, beginning of year	142,900,178	37,871,148	21,490,482	202,261,808
Net assets, end of year	<u>\$149,852,292</u>	<u>\$ 50,368,033</u>	<u>\$ 23,790,763</u>	<u>\$ 224,011,088</u>

*The accompanying notes are an integral part of these combined financial statements.*

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
 Combined Statement of Activities  
 For the year ended June 30, 2013**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Operating revenues and support				
Bishop's Lenten Appeal	\$ 15,267,186	\$ -	\$ -	\$ 15,267,186
Operational assessment	7,108,859	-	-	7,108,859
Investment income for operations	1,145,000	-	-	1,145,000
Transmittal fees	149,078	-	-	149,078
Contributions, bequests and major gifts	386,592	13,928,769	3,016,198	17,331,559
Program revenue	2,441,211	-	-	2,441,211
Other revenue and support	21	-	-	21
Satisfaction of temporary restrictions	8,427,316	(8,427,316)	-	-
Total operating revenues and support	<u>34,925,263</u>	<u>5,501,453</u>	<u>3,016,198</u>	<u>43,442,914</u>
Operating expenses				
Program services				
Pastoral	7,861,238	-	-	7,861,238
Religious personnel development	3,166,738	-	-	3,166,738
Education	6,124,059	-	-	6,124,059
Social services	5,050,544	-	-	5,050,544
Supporting services				
Diocesan administration and parochial support	11,339,863	-	-	11,339,863
<i>Rooted in Faith - Forward in Hope, Inc.</i>	18,467	-	-	18,467
Bishop's Lenten Appeal	769,331	-	-	769,331
Total operating expenses	<u>34,330,240</u>	<u>-</u>	<u>-</u>	<u>34,330,240</u>
Change in net assets from operations	<u>595,023</u>	<u>5,501,453</u>	<u>3,016,198</u>	<u>9,112,674</u>
Other changes in net assets				
Investment income less amount included in operations, net	3,678,248	3,690,864	-	7,369,112
Bond interest expense	(1,108,103)	-	-	(1,108,103)
Unrealized gain on swap agreement	553,399	-	-	553,399
Insurance programs	1,850,761	-	-	1,850,761
Change in unfunded pension liability, priests	1,364,333	-	-	1,364,333
Change in unfunded postretirement health obligation	1,371,215	-	-	1,371,215
Net property gains	10,752	-	-	10,752
<i>Rooted in Faith - Forward in Hope, Inc.</i> contributions, net of bad debt losses	-	(682,043)	-	(682,043)
Rental income - diocesan properties	1,586,726	-	-	1,586,726
Loan reserve increase - related party	(1,542,957)	-	-	(1,542,957)
Satisfaction of temporary restrictions	34,570	(34,570)	-	-
Total other changes in net assets	<u>7,798,944</u>	<u>2,974,251</u>	<u>-</u>	<u>10,773,195</u>
Change in net assets	8,393,967	8,475,704	3,016,198	19,885,869
Net assets, beginning of year	134,506,211	29,395,444	18,474,284	182,375,939
Net assets, end of year	<u>\$142,900,178</u>	<u>\$ 37,871,148</u>	<u>\$ 21,490,482</u>	<u>\$ 202,261,808</u>

*The accompanying notes are an integral part of these combined financial statements.*

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Combined Statements of Cash Flows**  
**For the years ended June 30, 2014 and 2013**

	<b>2014</b>	<b>2013</b>
Cash flows from operating activities		
Change in net assets	21,749,280	19,885,869
Adjustments to reconcile change in net assets to net cash and cash equivalents provided by operating activities		
Depreciation of property	2,622,656	2,617,602
Gain on sale of assets	(310,104)	(10,752)
Contributed real and personal property	(204,500)	-
(Decrease) in allowance for uncollectible accounts receivable	(1,246)	(1,820)
Increase (decrease) in discount on major gifts pledges receivable	430,654	(7,618)
Bad debt losses in <i>Rooted in Faith~Forward in Hope, Inc.</i> pledges receivable	-	750,000
Loan reserve - related party	1,314,918	1,542,957
Unrealized and realized (gains) on investments, net	(15,838,221)	(7,434,803)
Unrealized loss (gain) on interest rate swap	214,897	(553,399)
Increase in amounts held on behalf of other diocesan entities	4,127,511	2,112,216
(Increase) decrease in accounts receivable	(522,055)	135,788
Decrease (increase) in accrued interest receivable	30,135	(35,542)
(Increase) in BLA pledges receivable	(776,920)	(20,289)
(Increase) in bequests and major gift pledges receivable	(9,204,372)	(65,949)
(Increase) in prepaid expenses and other assets	(221,560)	(131,817)
Decrease in unamortized bond costs	354,542	24,183
Increase (decrease) in deposits held in custody for others	347,973	(299,453)
Increase in accounts payable and accrued expenses	390,604	765,285
(Decrease) in ADEF funds held for schools	(50,913)	(50,029)
(Decrease) increase in accrued interest payable	(277,689)	17,247
Increase (decrease) in unearned revenue	917	(69,215)
(Decrease) in accrued pension liability, priests	(341,988)	(1,364,333)
Increase (decrease) in postretirement health benefit obligation	1,193,647	(1,371,215)
Increase (decrease) in annuity payment liability	9,648	(11,596)
Net cash and cash equivalents provided by operating activities	5,037,814	16,423,317
Cash flows from investing activities		
Purchases of equipment	(2,469,478)	(362,890)
Proceeds from sale of property	338,607	32,500
Decrease in 200 North Glebe Road loan receivable	300,000	400,000
Loans to Saint John Paul the Great High School	(1,314,918)	(1,542,957)
Purchases of investments	(171,221,721)	(119,514,239)
Sales of investments	165,488,797	107,719,793
Net cash and cash equivalents (used in) investing activities	(8,878,713)	(13,267,793)
Cash flows from financing activities		
Decrease in Paul VI High School loan receivable	204,124	110,000
Repayments of notes payable	(60,957)	(42,338)
Repayments of bonds payable and defeasance of bonds	(22,925,737)	(1,052,945)
Proceeds from bonds payable	-	21,808,518
Deposits into bond defeasance escrow	-	(23,441,561)
Disbursements from bond defeasance escrow	22,849,681	591,880
Bond financing costs	-	(191,375)
Net cash and cash equivalents provided by (used in) financing activities	67,111	(2,217,821)
Net (decrease) increase in cash and cash equivalents	(3,773,788)	937,703
Cash and cash equivalents, at beginning of year	13,602,550	12,664,847
Cash and cash equivalents, at end of year	\$ 9,828,762	\$ 13,602,550

*Continued*

*The accompanying notes are an integral part of these combined financial statements.*

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Combined Statements of Cash Flows  
For the years ended June 30, 2014 and 2013**

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	<u>2014</u>	<u>2013</u>
Supplemental cash flow information		
Interest paid on debt	\$ 817,838	\$ 1,592,793
Supplemental schedule of non-cash investing and financing activities		
Equipment purchases in accounts payable	\$ 180,505	\$ 97,919
Equipment purchases financed with notes payable	\$ -	\$ 206,425
Contributed investment, real property and personal property	\$ 204,500	\$ -

*The accompanying notes are an integral part of these combined financial statements.*

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Notes to Combined Financial Statements  
For the years ended June 30, 2014 and 2013**

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**1. Nature of operations**

The content of these financial statements is limited to the Central Administrative Office of the Catholic Diocese of Arlington (the Chancery) and its affiliate *Rooted in Faith ~ Forward in Hope, Inc.* (the Campaign). Where applicable, the term “the Chancery” is used for disclosures related to the combined amounts of the Central Administrative Office and the Campaign. The Catholic Diocese of Arlington (the Diocese) consists of the 21 counties of the northern tier of Virginia, including the Northern Neck. The Chancery consists of various offices in order to organize events, monitor activities, coordinate efforts, and support the parishes and schools throughout the Diocese. The offices are classified into the following programs:

- Pastoral includes all offices primarily concerned with evangelization and communicating the Faith, such as the Office for Family Life, Office of Youth Ministry, Tribunal, Spanish Apostolate, Multicultural Ministries, Campus Ministries, the San Damiano Spiritual Life Center, and the St. Rose of Lima Priests’ Retirement Villa.
- Religious Personnel Development includes offices associated with the formational and educational needs of priests and deacons and related activities, including the Office of Vocations.
- Education includes offices associated with Catholic school administration and oversight of parish-based religious education programs.
- Social Services includes diocesan support of Catholic Charities of the Diocese of Arlington, the Campaign for Human Development, Rice Bowl, Office for Protection of Children and Young People and other charitable contributions.
- Diocesan Administration and Parochial Support includes offices concerned with the overall diocesan administration including the Chancery, Communications, Planning, Construction and Facilities, Finance and Accounting, Human Resources and Employee Benefits, Development and Information Services. These offices also provide services in support of the parishes and schools of the Diocese.
- Bishop’s Lenten Appeal (BLA) includes all expenses associated with the annual fundraising drive.

In fiscal year 2013, the Chancery launched the Leadership Gift Initiative (LGI), a targeted major gift campaign. The goal of the LGI is to raise a minimum of \$55 million by the year 2015 in support of the most critical needs of the diocese in the areas of Catholic education, New Evangelization, support for our retired priests, Catholic Charities programs and various capital improvements.

Rooted in Faith ~ Forward in Hope, Inc. (the Campaign) – A separately incorporated not-for-profit organization, created exclusively to raise and receive contributions for religious and charitable purposes of the Diocese.

## Central Administrative Office of the Catholic Diocese of Arlington and Affiliate

### Notes to Combined Financial Statements

#### For the years ended June 30, 2014 and 2013

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As of June 30, 2013, with the Rooted in Faith ~ Forward in Hope stated campaign goals met, remaining pledges receivable were written off to bad debt losses and remaining assets and liabilities transferred to the Central Administrative Office. The entity, *Rooted in Faith ~ Forward in Hope, Inc.*, will remain a separately incorporated organization available to raise and receive contributions for future initiatives, should the Bishop deem appropriate.

## 2. Basis of presentation and summary of significant accounting policies

### Basis of presentation and combination

The financial statements include the accounts of the Chancery, the Campaign (the Affiliate), and centralized administrative and diocesan functions under the control of the Bishop of Arlington (the Diocesan Bishop). They do not include the accounts for the Catholic Charities of the Diocese of Arlington (Catholic Charities), the Arlington Catholic Herald, 200 North Glebe Road, Inc. Arlington Diocesan Investment and Loan Corporation (DIAL Corp), The Foundation for the Catholic Diocese of Arlington, Inc. (The Foundation), or the Diocese of Arlington Scholarship Foundation, Inc. (Scholarship Foundation), over which the Diocesan Bishop exercises control, and are reported separately. All intercompany transactions and balances have been eliminated.

The financial statements also do not include the accounts of organizations within the Diocese such as parishes, parish schools, diocesan high schools, cemeteries, homes, and offices and other institutions owned and operated by religious orders of men and women. These organizations may or may not be separate corporations under civil law; however, each is an operating entity distinct from the Chancery, maintains separate accounts and carries on its own services and programs. Transactions between the Chancery and such organizations are recorded on bases agreed upon by the parties.

All properties of parishes and other diocesan-owned entities are legally titled to the Diocesan Bishop and his successors in office. The cost of new properties for future parish sites and diocesan high schools is included in these financial statements. At the time approval is given to proceed with formal planning of construction of a new parish, the parish is granted free use of the property by the Diocesan Bishop. Although civil ownership resides with the Diocese, the parish, a separate canonical entity, receives ownership of the property at the time of donation from the Chancery. Proceeds of the sale of any excess property shall accrue to the Diocese.

### Basis of accounting

The Chancery's combined financial statements are presented on the accrual basis of accounting in accordance with generally accepted accounting principles in the United States of America.

### Classification of net assets

The Chancery's net assets have been grouped into the following three categories:

*Unrestricted Net Assets* - Net assets that are not subject to donor-imposed restrictions.

*Temporarily Restricted Net Assets* - Assets whose use is subject to explicit or implicit donor-imposed restrictions that either expire by the passage of time or can be fulfilled and removed by actions of the Chancery pursuant to these donor restrictions.

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Notes to Combined Financial Statements  
For the years ended June 30, 2014 and 2013**

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Permanently Restricted Net Assets - Net assets that are subject to explicit or implicit donor-imposed restrictions that require the original contribution be maintained in perpetuity by the Chancery, but permits the use of the investment earnings for general or specific purposes.

Unrealized and realized gains and losses and dividends and interest from investing in income-producing assets may be included in any of these net classifications depending on donor restrictions related to the principal investment.

**Unrestricted net assets**

To ensure observances of internally designated limitations and restrictions placed on the use of the resources available to the Chancery, the net assets of the Chancery are maintained in distinct subgroups, whereby, resources for various purposes are classified for accounting and reporting purposes into funds determined in accordance with the internally designated nature and purpose of such funds as follows:

Current operations include all resources available for support of Chancery operations.

Invested in property, equipment and land includes depreciated amounts invested in real property, computer hardware and software, office equipment and furniture and property held for future projects and parish sites, as well as construction in progress, net of outstanding bonds and accounts payable used for these investments.

Functioning as endowment are quasi-endowment funds available for investment as the Diocesan Bishop designates and includes original patrimony of the Diocese. Income from these investments can be used at the discretion of the Diocesan Bishop.

Designated includes monies for the priests' mutual aid fund, medical and property insurance fund, scholarship fund and the Bishop Keating fund.

**Cash and cash equivalents**

Cash and short-term investments with maturities at dates of purchase of three months or less are classified as cash equivalents, except that any such investments with cash held in trusts or by external endowment investment managers are classified with the deposits and investments, respectively. Cash equivalents are carried at cost which approximates fair value.

**Accounts and loans receivable**

Accounts and loans receivable are stated at the amount management expects to collect from outstanding balances. The Chancery provides for probable uncollectible amounts through a provision for bad debt expense and an adjustment to a valuation allowance based on its assessment of the current status of accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and credit to accounts and loans receivable.

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Notes to Combined Financial Statements**  
**For the years ended June 30, 2014 and 2013**

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**Property, equipment and land**

Property, equipment and land are carried at cost or, in the case of donated or bequeathed property, at fair value at date of donation. Property, equipment and land include real property, equipment, land and the original buildings and grounds of four regional high schools and other affiliated organizations under the control of the Diocesan Bishop. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, generally over 3 to 50 years. The cost of repairs and maintenance is expensed as incurred. It is the general policy of the Chancery to capitalize all expenditures for property and equipment in excess of \$5,000.

**Investments and investment valuation**

Investments are stated at fair value, as described in Note 8, *Fair value measurements*. Investments consist of money market funds, U.S. Government and sponsored enterprises securities, corporate bonds and equities, and alternative investments.

**Investment income and expense**

Realized gains and losses on investment transactions are recorded on the average cost method and are included in investment income in the statement of activities. Changes in unrealized appreciation and depreciation for the year are similarly reported. Interest and dividend income are recorded on the accrual basis.

**Investment pools**

The Chancery maintains master investment accounts for long-term assets, including certain reserves held on behalf of DIAL Corp and endowments, including those amounts held on behalf of Catholic Charities and The Foundation. Realized and unrealized gains and losses from securities in the master investment accounts are allocated monthly to the individual participants based on the relationship of the market value of each participant to the total market value of the master investment accounts, as adjusted for additions to or deductions from those accounts.

**Derivative instruments**

A derivative financial instrument is used to manage a variable interest rate on long-term debt. The Chancery has entered into an interest rate swap agreement to reduce the impact of changes in the variable interest rate. The Chancery recognizes the interest rate swap agreement as a net asset or liability at fair value on the combined statements of financial position. Changes in fair value on this agreement are recorded in the statement of activities as non-operating gains or losses.

**Unearned revenue**

Income from program activities received in advance is deferred and recognized in the period the event is held.

**Contributions**

Contributions are recognized when the donor makes an unconditional promise to transfer assets. These contributions are recorded as unrestricted, temporarily restricted, or permanently restricted revenue depending on the existence or nature of any donor restrictions.

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Notes to Combined Financial Statements**  
**For the years ended June 30, 2014 and 2013**

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Contributions that are restricted by the donor are reported as increases in unrestricted net assets in the fiscal year in which the restrictions expire or are satisfied. All other donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When restrictions are satisfied, temporarily restricted net assets are released to unrestricted net assets.

Contributions received by the Chancery on behalf of other related entities are not recorded as contributions on the Chancery's combined statement of activities. Rather these amounts are agency transactions since the other related entities carry the variance power and not the Chancery.

**Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported 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.

**Concentration of credit risk**

Financial instruments which potentially subject the Chancery to a concentration of credit risk principally consist of cash and cash equivalents, accounts receivable, and investments. The Chancery maintains cash and investments with several financial institutions. The Chancery performs periodic evaluations of these institutions for relative credit standing. The total deposits at these institutions at times exceed the amount guaranteed by federal agencies and therefore bear some risk since they are not collateralized. Cash on deposit with financial institutions exceeded the federally insured limit by \$3,753,739 and \$5,157,297 as of June 30, 2014 and 2013, respectively. The Chancery also invests excess funds in overnight investment agreements which are not federally insured but are collateralized by U.S. treasuries or mortgage-backed securities of U.S. government-sponsored enterprises. Amounts held in overnight investments as of June 30, 2014 and 2013 were \$5,746,201 and \$8,869,801 respectively. Pledges receivable, which have been adjusted for doubtful accounts, are due from individuals, corporations, and foundations. The amount due from one contributor comprises 60% of the total bequest and major gifts pledges receivable balance at June 30, 2014. To date, no permanent losses or impairments have been experienced due to concentration in these areas.

**Income taxes**

The Chancery and the Campaign are exempt from federal and state income tax under the provisions of Section 501(c)(3) of the Internal Revenue Code and related provisions of the Commonwealth of Virginia. They are not subject to the filing requirements of the Form 990. The Chancery may be subject to tax to the extent it has taxable unrelated business income. The Chancery has no unrelated business income and accordingly, no provision for income taxes is provided in the accompanying combined financial statements. The Chancery believes that it has appropriate support for any tax provisions taken, and as such, does not have any uncertain tax positions that are material to the financial statements.

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**Subsequent events**

In preparing these financial statements, the Chancery has evaluated events and transactions for potential recognition or disclosure through October 28, 2014, the date the financial statements were available to be issued.

**3. Accounts receivable**

The Chancery bills the parishes, schools, other related entities and individuals on a monthly basis for various items paid by the Chancery or covered under the diocesan structure. These include the retirement programs for priests and lay employees, diocesan tuition assistance program, unemployment compensation, and health and property insurance. The Chancery also bills the parishes on a monthly basis for the operational assessment, a percentage of the parish offertory income to help offset the administration of diocesan programs. Accounts receivable are not collateralized.

Accounts receivable are as follows as of June 30:

	<u>2014</u>	<u>2013</u>
Parishes	\$ 537,778	\$ 535,534
Schools	1,095,414	602,255
Other diocesan entities	90,941	146,379
Employee advances	4,315	4,758
Due from brokers	74,326	46,561
Miscellaneous	<u>101,737</u>	<u>46,969</u>
Total accounts receivable	1,904,511	1,382,456
Less: allowance for doubtful accounts	<u>(121,925)</u>	<u>(123,171)</u>
Total accounts receivable, net	<u>\$ 1,782,586</u>	<u>\$ 1,259,285</u>

**4. Bishop's Lenten Appeal pledges receivable**

As of June 30, 2014 and 2013, contributors to the Bishop's Lenten Appeal (BLA) have unconditionally promised to give \$3,771,899 and \$2,994,979. As the Bishop's Lenten Appeal is an annual campaign, the pledges are due within one year.

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**5. Bequests and major gifts pledges receivable**

Unconditional promises to give are as follows as of June 30:

	<u>2014</u>	<u>2013</u>
Receivables due in one year or less	\$ 400,000	\$ 323,000
Receivables due in one to five years	<u>10,847,013</u>	<u>1,719,642</u>
Total unconditional promises to give	11,247,013	2,042,642
Less: discount to present value	<u>(467,258)</u>	<u>(36,605)</u>
 Pledges receivable	 <u><u>\$ 10,779,755</u></u>	 <u><u>\$ 2,006,037</u></u>

Pledges receivable include amounts related to the Leadership Gift Initiative campaign (Note 1). Unconditional promises to give due in more than one year are discounted at rates ranging from 1.24% to 2.62%.

**6. Investments**

Investments are stated at fair value. The cost of investments and related fair values at June 30, 2014 and 2013 consist of the following:

	<u>2014</u>		<u>2013</u>	
	<u>Cost</u>	<u>Fair Value</u>	<u>Cost</u>	<u>Fair Value</u>
Short-term investments	\$ 10,994,157	\$ 10,994,157	\$ 9,579,340	\$ 9,579,340
U.S. Government and sponsored enterprises securities	3,645,317	3,600,885	3,880,756	3,894,299
Corporate, municipal and foreign bonds and other fixed instruments	36,950,904	40,567,661	30,426,502	33,258,571
Equities, including publicly traded REITs	107,203,509	137,603,974	92,622,588	111,637,190
Real property held for investment	2,908,599	2,908,599	2,366,000	2,366,000
Alternative investments	<u>4,307,516</u>	<u>5,275,400</u>	<u>2,874,297</u>	<u>3,351,937</u>
	<u><u>\$ 166,010,002</u></u>	<u><u>\$ 200,950,676</u></u>	<u><u>\$ 141,749,483</u></u>	<u><u>\$ 164,087,337</u></u>

Also included in investments at June 30, 2014 and 2013 is \$457,872 and \$397,087, respectively, representing the fair market value of assets held under split interest agreements for which the Chancery is the trustee. Monthly, quarterly or semiannual distributions are made to the donors. The ultimate beneficiaries are the Chancery, Catholic Charities and parishes. The proceeds are expected to be received in three to nineteen years, based on published actuarial tables, and are calculated using discount rates which represent the risk-free rates in existence at the date of the gift. Amounts due to annuitants and related parties are disclosed as annuity payment liability in the accompanying combined statements of financial position.

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Investments are held for the following purposes:

	<u>2014</u>	<u>2013</u>
Current operations and programs	\$ 53,835,493	\$ 47,108,688
Long-term purposes, including endowments	53,984,128	42,921,250
Assets held on behalf of other diocesan entities, including DIAL Corp	88,878,601	70,136,442
Arlington Diocese Educational Fund (ADEF)	4,252,454	3,920,957
Total	<u>\$ 200,950,676</u>	<u>\$ 164,087,337</u>

Investments in the amount of \$168,622,515 and \$133,178,487 as of June 30, 2014 and 2013, respectively, are held in a pool under a trust agreement with a bank in which participants share in allocated investment income and loss.

Investment income is reported on the statement of activities as follows:

	<u>2014</u>	<u>2013</u>
For Operations	\$ 1,460,000	\$ 1,145,000
In Other changes in net assets	15,499,737	7,369,112
Net investment gains - Chancery	<u>\$ 16,959,737</u>	<u>\$ 8,514,112</u>

Investment income represented in operating revenue represents the amount included in the approved budget based on a spending rate formula.

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Total net investment income for the years ended June 30, 2014 and 2013, respectively, consists of the following:

	<u>2014</u>	<u>2013</u>
<b>Chancery</b>		
Interest, dividends and other investment income	\$ 1,762,968	\$ 1,613,766
Realized gains, net	9,038,901	4,031,807
Unrealized gains, net	6,799,320	3,402,996
Less - investment management expenses	<u>(641,452)</u>	<u>(534,457)</u>
Net investment gains - Chancery	<u>\$ 16,959,737</u>	<u>\$ 8,514,112</u>
<b>Funds held for diocesan entities</b>		
Investment income allocated to diocesan entities	\$ 16,028,808	\$ 8,752,824
Total net investment gains - Chancery and funds held for diocesan entities	<u>\$ 32,988,545</u>	<u>\$ 17,266,936</u>

The Chancery invests in a variety of investment securities and therefore, is subject to various risks such as interest rate, credit and overall market volatility risk. Due to continuing market risk and fluctuations, it is reasonably possible that significant changes in investment values will occur in the near term that could materially affect the amounts reported in the statement of financial position and the results of operations.

**7. Fair value of financial instruments**

Estimated fair values of the Chancery's financial instruments (all of which are held for nontrading purposes) are as follows:

	<u>2014</u>		<u>2013</u>	
	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Cash and cash equivalents	\$ 9,828,762	\$ 9,828,762	\$ 13,602,550	\$ 13,602,550
Investments	\$ 200,950,676	\$ 200,950,676	\$ 164,087,337	\$ 164,087,337
Bond defeasance escrow	\$ -	\$ -	\$ 22,849,681	\$ 22,849,681
Interest rate swap agreement	\$ 338,502	\$ 338,502	\$ 553,399	\$ 553,399
Demand notes and loans receivable	\$ 7,832,920	\$ 7,395,381	\$ 8,362,843	\$ 7,844,648
Defeased bonds payable	\$ -	\$ -	\$ 22,070,000	\$ 22,070,000
Bonds payable	\$ 20,479,836	\$ 20,479,836	\$ 21,335,573	\$ 21,335,573

The carrying amount for cash and cash equivalents approximates fair value.

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The fair value of demand notes and loans receivable are based on quoted market rates of debt securities with similar repayment terms.

In December 2012, the Chancery obtained bank qualified tax-exempt financing which provided funds for defeasance of the 2003 bonds payable (Note 11). The carrying value of the defeased bonds payable and the 2012 bonds, which accrues interest at a floating market rate, approximates the market value.

Investments and interest rate swap agreements are carried at fair value as described in Note 8.

**8. Fair value measurements**

The Chancery measures fair value using a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability. Inputs may be observable or unobservable and refer broadly to the assumptions that market participants would use in pricing the asset or liability. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from sources independent of the reporting entity. Unobservable inputs reflect the reporting entity's own assumptions about the assumptions that market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The objective of a fair value measurement is to determine 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 (an exit price). Accordingly, the fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The Chancery may use valuation techniques consistent with the market, income and cost approaches to measure fair value.

The inputs used to measure fair value are categorized into the following three categories:

- Level 1 Inputs – Unadjusted quoted prices in active markets for identical assets or liabilities such as stocks and government bonds.
- Level 2 Inputs – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, or other inputs that can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 Inputs – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or other valuation techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

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Fair values of assets measured on a recurring basis by level at June 30, 2014 are as follows:

	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
<b>Assets</b>				
Investments				
Short-term investments	\$ 10,994,157	\$ 10,994,157	\$ -	\$ -
U.S. Government and sponsored enterprises securities	3,600,885	2,578,095	1,022,790	-
Corporate,municipal and foreign bonds and other fixed instruments	40,567,661	-	40,567,661	-
Equities, including publicly traded REITs	137,603,974	137,603,974	-	-
Real property held for investment	2,908,599	-	2,908,599	-
Alternative investments	5,275,400	-	-	5,275,400
Total	<u>\$ 200,950,676</u>	<u>\$ 151,176,226</u>	<u>\$ 44,499,050</u>	<u>\$ 5,275,400</u>
Interest rate swap agreement	<u>\$ 338,502</u>	<u>\$ -</u>	<u>\$ 338,502</u>	<u>\$ -</u>

Fair values of assets measured on a recurring basis by level at June 30, 2013 are as follows:

	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
<b>Assets</b>				
Investments				
Short-term investments	\$ 9,579,340	\$ 9,579,340	\$ -	\$ -
U.S. Government and sponsored enterprises securities	3,894,299	2,563,006	1,331,293	-
Corporate,municipal and foreign bonds and other fixed instruments	33,258,571	-	33,258,571	-
Equities, including publicly traded REITs	111,637,190	111,637,190	-	-
Real property held for investment	2,366,000	-	2,366,000	-
Alternative investments	3,351,937	-	-	3,351,937
Total	<u>\$ 164,087,337</u>	<u>\$ 123,779,536</u>	<u>\$ 36,955,864</u>	<u>\$ 3,351,937</u>
Interest rate swap agreement	<u>\$ 553,399</u>	<u>\$ -</u>	<u>\$ 553,399</u>	<u>\$ -</u>

The following is a description of what is included in the categories of investments, along with the valuation methodologies used for measuring assets at fair value.

Short-term investments – These include money market and money market mutual funds, investing primarily in cash, U.S. Treasury obligations, or short-term, high quality fixed income securities. These are considered cash and cash equivalents and are valued at their cash value.

U.S. Government and sponsored enterprises securities – U.S. Treasury notes and bonds are valued by independent pricing services based on active market data and are

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categorized as Level 1. Government sponsored enterprises securities and mortgage-backed securities, categorized as Level 2, are valued by independent pricing services based on inputs that may include issuer type, coupon, cash flows, benchmark yields, reported trades, and bids and offers.

Corporate, municipal and foreign bonds and other fixed instruments – These primarily include holdings in three diverse bond funds, two fixed bond funds and one high yield bond fund. The bond funds invest primarily in U.S. Government, agency, corporate and mortgage-backed securities. The fair value of the bond fund investments are estimated using the net asset value per share of investments provided by the fund manager. Holdings also include fixed rate corporate and foreign bonds that are valued based on yields currently available for comparable securities. All investments are categorized as Level 2.

Equity securities, including publicly traded REITs – These investments are individual securities and are valued based on their published closing price in an active market.

Real property held for investment – Real estate investment properties, categorized as Level 2, are valued using a market approach based primarily on current appraised values and other information for similar property.

Alternative investments – comprised of separate private equity interests focusing on venture and/or buy-out strategies, investments in real assets leased to the U.S. government, and a diversified portfolio with concentrations in timber, energy and real estate. These investments are classified within Level 3 as the value of these interests is primarily based on the net asset value reported by external fund managers. The underlying investments of the investment funds are accounted for at fair value as described in the investment funds' financial statements, all of which are subject to a third party annual audit. The Chancery's rights of transfer or redemption are restricted, subject to terms of the agreements. It is anticipated that these investments will be redeemed over the life of the funds, all greater than one year.

The Chancery has entered into an interest rate swap agreement in association with a new financing arrangement of bonds payable (Note 11). The fair value of the interest rate swap agreement is determined by comparing the difference between the present value of the fixed monthly payments and the estimated present value of the floating monthly payments based on estimated forward rates derived from yield curves. The Chancery has recognized in the statement of activities a decrease in fair value of the interest rate swap agreement of \$214,897 for the year ended June 30, 2014 and an increase of \$553,399 for the year ended June 30, 2013.

Due to the inherent uncertainty involving assumptions and estimation methods, the fair value of the investments and interest rate swap agreements may differ materially from actual results.

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The changes in investment measured at fair value using Level 3 inputs are reflected below:

	<u>2014</u>	<u>2013</u>
Balance, beginning of year	\$3,351,937	\$1,336,747
Contributions	1,766,103	2,112,981
Distributions	(332,883)	(102,130)
Change in value - unrealized gain	490,243	4,339
Balance, end of year	<u>\$5,275,400</u>	<u>\$3,351,937</u>

Unrealized gains recorded for Level 3 investments are reported as investment income under other changes in net assets on the statement of activities. Certain distributions from alternative investments are recorded as dividend income when identified by the fund manager as a distribution from earnings and profits from the underlying investments. Distributions from Level 3 investments recorded as dividend income amounts to \$190,149 and \$105,247 for the years ended June 30, 2014 and 2013.

The Chancery recognizes transfers into and out of levels at the end of the reporting period. There were no transfers between levels in the years ended June 30, 2014 and 2013.

**9. Related-party transactions**

The Chancery has transactions with diocesan parishes, schools, and other related entities. Below is a summary of the impact of significant transactions with these related parties on the combined statements of financial position and statements of activities:

	<u>2014</u>	<u>2013</u>
Assets:		
Accounts receivable, parishes, schools and other related entities, net	\$ 1,620,579	\$ 1,185,999
Due from Catholic Charities, split interest annuity	78,962	76,124
Paul VI Catholic High School loan receivable, for \$4,839,917 in bond proceeds used for renovations and additions	3,798,634	4,028,557
Saint John Paul the Great High School loan receivable, interest waived for 2014 and 2013, no fixed repayment, repayments accepted as cash is available, net of allowance	-	-
200 North Glebe Road, Inc., interest waived for 2014 and 2013, due on demand, repayments accepted as cash is available	4,034,286	4,334,286
	<u>\$ 9,532,461</u>	<u>\$ 9,624,966</u>

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	<u>2014</u>	<u>2013</u>
Liabilities:		
Accounts payable, parishes, schools, other related entities	\$ 18,785	\$ 32,908
Due to parishes, split interest annuities	6,555	7,146
Amounts held on behalf of other diocesan entities:		
DIAL Corp, funds held in investment pool	75,123,510	58,924,207
Catholic Charities, endowment funds held in investment pool	12,028,549	10,042,103
The Foundation, endowment funds held in investment pool	1,403,833	1,170,131
Catholic Charities, capital campaign pledges	6,128	6,128
Parishes, capital campaign pledges	569,440	26,540
ADEF funds held for schools	2,651,903	2,484,996
	<u>\$ 91,808,703</u>	<u>\$ 72,694,159</u>

	<u>2014</u>	<u>2013</u>
Revenues and Support:		
Operational assessment, parishes	\$ 7,428,795	\$ 7,108,859
Contributions, diocesan tuition assistance program	2,321,499	2,221,518
Program fees	1,312,229	1,574,629
Information technology, accounting and administrative support	280,398	182,208
Rental income, Catholic Charities	277,753	275,204
Rental income, Arlington Catholic Herald	118,802	117,573
Rental income, Saint John Paul the Great High School	1,314,918	1,442,957
Insurance and risk management premiums billed	16,534,965	15,713,232
	<u>\$29,589,359</u>	<u>\$28,636,180</u>

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	<u>2014</u>	<u>2013</u>
Expenses:		
Rent paid to 200 N. Glebe Road, Inc.	\$ 1,994,019	\$ 1,964,274
Contributions, tuition assistance program	2,285,528	2,208,529
Contributions, tuition assistance endowment grants	627,000	560,000
Contribution, subsidy to Catholic Charities	1,653,399	1,504,490
Contribution, Catholic Charities endowment fund (LGI)	75,313	1,253,500
Contribution, restricted for Catholic Charities programs (LGI)	1,000,000	1,000,000
Contribution, restricted, diocesan high schools capital needs (LGI)	4,000,000	-
Contribution, other program service subsidies	434,000	232,927
Contribuiton, Cathedral of St. Thomas More renovations	510,623	-
Contributions made to Lay Retirement Plan	985,746	941,941
Contributions made to Priest Retirement Plan, including LGI	1,375,000	232,000
Advertising expense to Arlington Catholic Herald	153,470	103,195
Loan reserve, Saint John Paul the Great High School	1,314,918	1,542,957
	<u>\$ 16,409,016</u>	<u>\$ 10,983,813</u>

Affiliates participating in the diocesan sponsored insurance plans are charged premiums to cover estimated claims and program expenses. The net revenue or expense of these programs is reflected under other changes in net assets.

Certain parishes have chosen to participate in the Arlington Diocese Educational Foundation (ADEF) program. This program was established to support the cause of Catholic education through endowments or quasi-endowment investment accounts. The assets of ADEF are held in trust with the Chancery being steward and guardian of such endowments.

The Chancery administers a master investment pool (Notes 1 and 6). Endowment funds and long term investments of certain affiliates are held in the master pool at their request. Investment income is allocated based on the proportionate market value of investments held by participants.

The Chancery has entered into services agreements with certain affiliates to provide information technology, accounting and administrative support.

Property and equipment includes the original buildings and grounds of four diocesan high schools acquired by the Chancery. The Chancery does not charge Bishop O'Connell, Paul VI and Bishop Ireton High Schools for use of the facilities. Improvements and repairs necessary to maintain the property are financed by the high schools and carried on their financial statements. The Chancery has joined with Catholic Charities in providing transitional housing and counseling services by providing use of a family housing facility at no charge.

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The Chancery has advanced funds to Saint John Paul the Great High School periodically since its opening in August 2008, to supplement tuition in covering operating costs. The collectability of the loan was reviewed in 2014 and 2013 and based on current enrollment and operating financial position a reserve was established on the loan balance, \$11,282,757 and \$9,967,839 at June 30, 2014 and 2013, respectively. It is at least reasonably possible that the estimated loan to be collected may change as school enrollment and fundraising activities increase.

The Chancery obtained financing through issuance of tax-exempt revenue bonds with the Prince William County Industrial Authority, a portion of which was used for building renovations and improvements to Paul VI Catholic High School (PVI) (Note 11). The Chancery established a loan with PVI in the amount of \$4,960,000, the amount of bond proceeds used to cover these costs. Through December 2012, the terms of this loan were equivalent to those contained in the Diocese's bond agreement. In December 2012, the Chancery refinanced the bonds outstanding. The Chancery has re-amortized the principal outstanding with PVI based on the effective fixed rate of 2.482% which was secured by the refinancing and related interest rate swap. Monthly principal and interest payments of \$27,563 are expected to be paid by PVI to the Chancery through maturity, December 1, 2027.

Loans have been made to 200 N. Glebe Road, Inc., a related entity and lessor of office space to the Chancery. The loan to 200 N. Glebe Road, Inc. is due on demand, with repayments accepted as cash is available. Amounts repaid by 200 N. Glebe Road, Inc. were \$300,000 and \$400,000 for the years ended June 30, 2014 and 2013, respectively.

Annually, management assesses the adequacy of the allowance for credit losses evaluating required and expected repayment on loans. Changes in the allowance for related party loans receivable as of June 30 are as follows:

	<b>2014</b>	<b>2013</b>
Balance, beginning of year	\$ 9,967,839	\$ 8,424,882
Provision for credit losses	1,314,918	1,542,957
Balance, end of year	<u>\$ 11,282,757</u>	<u>\$ 9,967,839</u>

The Chancery granted three diocesan high schools \$4,000,000, raised through the Leadership Gift Initiative campaign, restricted for the capital needs of the schools. The grants may only be used for capital improvements approved by the Chancery.

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**10. Property, equipment and land, net**

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

	<u>2014</u>	<u>2013</u>
Operating properties-buildings	\$ 84,378,316	\$ 84,424,477
Operating properties-land and land development	25,414,566	25,368,404
Operating properties-improvements	7,811,278	7,419,719
Operating properties-furniture and equipment	3,900,839	3,882,115
Land held for future projects and parishes	10,935,532	11,003,416
Office furniture and equipment	777,094	755,160
Computer hardware	273,041	204,389
Computer software	992,343	864,692
Vehicles	669,006	664,507
Leasehold improvements	1,030,509	722,456
Total property, equipment and land	<u>136,182,524</u>	<u>135,309,335</u>
Less: accumulated depreciation	<u>(29,472,369)</u>	<u>(26,921,304)</u>
Property, equipment and land, net	<u>\$ 106,710,155</u>	<u>\$ 108,388,031</u>

Depreciation expense was \$2,622,656 and \$2,617,602 during the years ended June 30, 2014 and 2013, respectively. Of the total assets listed above, \$13,440,993 and \$13,174,038 were fully depreciated at June 30, 2014 and 2013, respectively.

Included in construction in progress and assets not yet placed in service is land and buildings purchased for a new location of an existing diocesan regional elementary school in Culpeper, Virginia. Assets approximating \$1,600,000 and representing the originally purchased 20 acre campus plus improvements were placed in service in August 2014.

In 1998, a conditional gift of approximately forty acres of land in Prince William County was donated to the Chancery. In August 2006, the conditions of this gift were satisfied and the donation was recorded at the appraised value of \$14,500,000. The land must be used for educational purposes for a period of thirty years and therefore the donation will remain in temporarily restricted net assets until such time this restriction expires.

Construction of Saint John Paul the Great High School was funded, in part, from tax-exempt bonds (Note 11). Once it was reasonably assured that the high school would be constructed, interest costs, net of interest earned from the temporary investment of the bonds were capitalized. Upon completion of the high school, bond interest cost was charged to expense.

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Capitalized interest is included in operating properties. Amortization of capitalized interest is included in depreciation expense. Capitalized interest at June 30 was:

	<u>2014</u>	<u>2013</u>
Net amount capitalized, beginning of year	\$ 885,906	\$ 905,538
Less: amortization expense	<u>19,632</u>	<u>19,632</u>
Net amount capitalized, end of year	<u>\$ 866,274</u>	<u>\$ 885,906</u>

Cumulative investment earnings do not exceed cumulative investment expenses, and therefore the Diocese does not have an arbitrage recapture obligation.

**11. Bonds payable**

On November 1, 2003, tax-exempt bonds with a face value of \$25,465,000 were issued by the Prince William County Industrial Development Authority on behalf of the Diocese of Arlington with proceeds to be used for construction of a new high school in Prince William County and renovations and additions to Paul VI Catholic High School (Note 10).

In December 2012, the Chancery entered into a new financing arrangement obtaining \$21,808,515 in bank qualified tax-exempt financing for the purpose of defeasing the current bonds outstanding. The loan proceeds, together with the reserve fund related to the 2003 bonds, were placed in escrow to purchase U.S. Treasury obligations – state and local government series. The escrow fund was used to pay the scheduled debt service requirement of the 2003 bonds on each scheduled payment date through October 1, 2013, at which time the 2003 bonds payable were redeemed in full at a price equal to 101% of par.

The outstanding balance on the 2012 bonds is \$20,479,836 and \$21,335,573 at June 30, 2014 and 2013, respectively. The 2012 bonds payable bear interest at a floating rate, 78% of the 30-day London Interbank Offered Rate (LIBOR) plus 1.002%. The average interest rate for the fiscal year ended June 30, 2014 and 2013 is 1.13% and 1.16%, respectively. The Chancery entered into an interest rate swap agreement in May 2013 related to the 2012 bonds payable securing an effective fixed rate of 2.482% in exchange for the floating LIBOR rate. The original notional amount under the agreement was \$21,405,966, decreasing based on a 15 year amortization, terminating December 1, 2027. The notional amount at June 30, 2014 and 2013 is \$20,068,648 and \$21,303,296, respectively.

The 2012 bonds contain no pre-payment penalties but require compliance with certain covenants such as operating liquidity, additional indebtedness, maintenance of insurance on the project, use of the bond proceeds, maintenance of tax-exempt status of the Diocese and financial reporting.

Bond interest expense is \$721,650 and \$1,108,103, reflective of the swap agreement and net of amount received from Paul VI Catholic High School, for the years ended June 30, 2014 and 2013, respectively. Bond related costs for the year ended June 30, 2014, include the premium paid and write off of unamortized bond costs in connection with the redemption of 2003 bond payable.

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Principal and interest are payable monthly based on a 20 year amortization with a balloon payment due in 15 years. Maturities on the bonds payable annually for the years through 2019 and thereafter are as follows:

2015	878,052
2016	900,264
2017	923,740
2018	948,515
2019	973,249
Thereafter	15,856,016
	<u>\$ 20,479,836</u>

**12. Pension expense**

**Pension plan - employees**

The Diocese has a noncontributory defined benefit pension plan which covers substantially all lay employees within the Diocese. The plan provides benefits based on a formula which takes into account the lay employees' annual compensation, period of service, and age.

The lay employees' plan is administered by the Chancery, but is a multi-employer plan. The plan covers employees from other diocesan organizations, such as parishes and schools, the Arlington Catholic Herald, and diocesan high schools, which, as noted in Note 2, are not combined with the Chancery for financial reporting purposes. Premiums are calculated based on 10% of eligible participant salaries, and are used toward the quarterly funding of the plan. The cost of the plan for the Chancery and charged to expense was \$985,746 and \$941,941 for the years ended June 30, 2014 and 2013, respectively. The plan is not subject to ERISA funding requirements.

**Pension plan - priests**

The Diocese also has a noncontributory defined benefit plan which covers diocesan priests incardinated in the Diocese and provides benefits based on age and compensation at retirement. As required by generally accepted accounting standards, the full funding status of the defined benefit pension plans, as of the balance sheet date, has been recognized as an asset (overfunded plan) or as a liability (underfunded plan). The pension benefit obligation for retired priests has been actuarially determined.

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The following amounts relate to the diocesan priests' defined benefit pension plan:

	<u>2014</u>	<u>2013</u>
Change in benefit obligation:		
Benefit obligation at beginning of year	\$16,471,472	\$16,804,242
Service cost	616,261	622,775
Interest cost	823,451	677,703
Plan amendments	-	335,571
Actuarial loss/(gain)	2,396,825	(1,288,704)
Benefits paid	<u>(822,561)</u>	<u>(680,115)</u>
Benefit obligation at end of year	<u>19,485,448</u>	<u>16,471,472</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	9,422,197	8,390,634
Return on plan assets	1,178,525	534,678
Employer contributions	3,000,000	1,177,000
Benefits paid	<u>(822,561)</u>	<u>(680,115)</u>
Fair value of plan assets at end of year	<u>12,778,161</u>	<u>9,422,197</u>
Accrued pension liability, priests	<u>\$ 6,707,287</u>	<u>\$ 7,049,275</u>

In January 2013, the pension plan was amended to increase housing benefits for certain retirees. In addition, the personal benefits were enhanced for the priests who retired prior to 2002 to remove disparity for all participants with regard to retirement date.

The accumulated benefit obligation at June 30, 2014 and 2013 was \$18,029,233 and \$15,287,605, respectively. The net periodic pension cost for the years ended June 30, 2014 and 2013 were \$916,650 and \$907,586, respectively. Amounts previously recognized in unrestricted net assets not yet recognized as periodic pension cost at June 30:

	<u>2014</u>	<u>2013</u>
Net (loss)	\$ (6,339,901)	\$ (4,581,662)
Net prior service cost	<u>(318,694)</u>	<u>(335,571)</u>
Amounts previously recognized in unrestricted net assets, not yet recognized as periodic benefit cost	<u>\$ (6,658,595)</u>	<u>\$ (4,917,233)</u>

The estimated net loss that will be amortized from changes in unrestricted net assets into net periodic benefit cost in 2015 is \$238,070.

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Assumptions used to determine the year-end benefit obligation:

	<u>2014</u>	<u>2013</u>
Discount rate on the benefit obligation	4.40%	5.10%
Rate of expected return on plan assets	7.00%	7.00%
Rate of priests' compensation increase	2.00%	2.00%

The expected return assumption was developed as the weighted average of expected returns determined under a forward looking approach and a historical approach using the plan's target asset assumption. The forward looking assumption was developed based on a market analysis applied to the plan's investment mix. The historical return assumption was developed from a proprietary database of prior investment returns.

The Diocese measures fair value of the plan's assets using a three-level hierarchy based upon observable inputs (Note 8).

Fair values of the plan's assets measured on a recurring basis by level at June 30, 2014 are as follows:

	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Short-term investments	\$ 510,142	\$ 510,142	\$ -	\$ -
U.S. Government and sponsored enterprises securities	2,538,650	1,511,750	1,026,900	-
Corporate and foreign bonds	1,635,780	-	1,635,780	-
Equities	8,093,589	8,093,589	-	-
Total	<u>\$ 12,778,161</u>	<u>\$ 10,115,481</u>	<u>\$ 2,662,680</u>	<u>\$ -</u>

Fair values of the plan's assets measured on a recurring basis by level at June 30, 2013 are as follows:

	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Short-term investments	\$ 295,275	\$ 295,275	\$ -	\$ -
U.S. Government and sponsored enterprises securities	3,042,838	1,635,533	1,407,305	-
Corporate and foreign bonds	1,035,681	-	1,035,681	-
Equities	5,048,403	5,048,403	-	-
Total	<u>\$ 9,422,197</u>	<u>\$ 6,979,211</u>	<u>\$ 2,442,986</u>	<u>\$ -</u>

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In connection with the plan amendment, investment assets used to fund personal and housing pension benefits in the plan were combined. The Diocese’s overall strategy is to invest in high-grade securities and other assets with a minimum risk of market value fluctuation. In general, the Diocese’s goal is to maintain the following allocation ranges:

Equity securities	50% - 60%
Fixed income securities	40% - 50%
Short term cash/money market	0% - 10%

The Diocese expects to contribute approximately \$1,490,000 to the plan in 2015. Benefits expected to be paid by the plan during the ensuing five years and thereafter are approximately as follows:

2015	\$ 820,420
2016	866,625
2017	860,073
2018	878,895
2019	897,403
Thereafter	5,262,649

**Tax-deferred retirement savings plan**

The Diocese also sponsors and maintains a tax-deferred 403(b) retirement savings plan for eligible employees and diocesan priests. All contributions are from employee elective salary reduction agreements. Since there is no employer match, there is no expense to the Chancery related to this plan.

**13. Postretirement benefits**

The Chancery sponsors a post-retirement Medicare supplemental plan for retired priests. The plan pays medical and prescription costs not covered by parts A and B of Medicare. The plan is noncontributory for diocesan priests. The Chancery also sponsors a lay-retiree postretirement plan which provides health benefits to retired lay employees meeting service and other participation requirements. The plan provides benefits to employees of the Chancery and other diocesan organizations, such as parishes, schools, the Arlington Catholic Herald, and diocesan high schools. The lay retirees pay 100% of the stated premium which is a blended rate for both active employees and retirees. Because the true medical costs are higher for retirees than for active employees, the plan is providing an “implicit subsidy” to the retirees. The postretirement obligation for both priests and lay retirees has been actuarially determined.

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The following amounts relate to the postretirement health obligation:

	<u>2014</u>	<u>2013</u>
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 7,484,062	\$ 8,855,277
Service cost	253,093	291,175
Interest cost	377,815	359,860
Employee contributions	146,020	110,690
Actuarial loss (gain)	655,310	(1,933,027)
Benefits paid	<u>(238,591)</u>	<u>(199,913)</u>
Benefit obligation at end of year	8,677,709	7,484,062
Change in plan assets:		
Fair value of plan assets at beginning of year	-	-
Employer contributions	92,571	89,223
Employee contributions	146,020	110,690
Benefits paid	<u>(238,591)</u>	<u>(199,913)</u>
Fair value of plan assets at end of year	-	-
Post retirement health benefit obligation	<u>\$ 8,677,709</u>	<u>\$ 7,484,062</u>

The net periodic benefit cost for the years ended June 30, 2014 and 2013 were \$509,448 and \$472,218, respectively. Amounts previously recognized in unrestricted net assets not yet recognized as periodic benefit cost at June 30:

	<u>2014</u>	<u>2013</u>
Net gain	\$ 422,401	\$ 1,199,171
Net prior service credit	<u>-</u>	<u>-</u>
Amounts previously recognized in unrestricted net assets, not yet recognized as periodic benefit cost	<u>\$ 422,401</u>	<u>\$ 1,199,171</u>

The estimated net gain that will be amortized from changes in unrestricted net assets into net periodic benefit cost in 2015 is \$88,516.

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Assumptions used to determine the year-end benefit obligation:

	<u>2014</u>	<u>2013</u>
Discount rate on the benefit obligation	4.40%	5.10%

For measurement purposes, a 7.1% increase in the cost of health care benefits was assumed for 2014. This rate was assumed to decrease over a 13 year period to an ultimate rate of 4.5% by 2027. For 2013, a 7.4% increase in the cost of health care benefits was assumed. This rate was assumed to decrease over a 15 year period to an ultimate rate of 4.5% by 2027.

The Diocese expects to contribute approximately \$191,000 to the plan in 2015. Benefits expected to be paid by the plan during the ensuing five years and thereafter are approximately as follows:

2015	\$	191,000
2016		231,000
2017		259,000
2018		266,000
2019		292,000
Thereafter		1,910,000

**14. Temporarily restricted net assets**

Expenses incurred for program activities such as seminarian education, educational programs, youth ministry, outreach, communications, and operations of the priests' retirement home resulted in a release of restricted net assets which is included in operations. Net assets were also released from restrictions with grants made to related parties for diocesan high school capital needs and charitable programs (Note 9). Affiliates are required to record these contributions as temporarily restricted and release from restrictions as funds are expended for the donor-specified purposes.

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Temporarily restricted net assets are available for the following purposes at June 30:

	<u>2014</u>	<u>2013</u>
Catholic education, endowment income	\$ 14,692,638	\$ 8,836,588
Donated land restricted for high school	14,500,000	14,500,000
Bishop's targeted initiatives	8,593,450	736,219
Retired priests' needs	4,825,077	4,486,877
Student financial aid	2,027,992	1,002,083
New evangelization	934,904	738,019
Charitable programs	772,703	195,520
ADEF education scholarships, endowment income	709,783	605,894
ADEF seminarian education	538,173	483,376
Youth ministry, endowment income	458,614	303,498
Continuing formation funds	426,063	388,098
Major gifts pledges receivable for future period use	393,851	665,273
Project Rachel and Gabriel	349,246	306,268
High school capital	222,002	4,008,333
Diocesan work camp	197,940	134,140
Charitable annuities	131,289	90,560
Catholic education	129,744	31,130
Respect Life	107,423	3,003
Seminarian support	80,259	62,177
Campaign for human development	67,463	66,204
Black and Indian mission	65,889	61,607
Permanent diaconate	56,742	55,991
Communications	35,116	65,479
Others	51,672	44,811
Total	<u>\$ 50,368,033</u>	<u>\$ 37,871,148</u>

Included in Bishop's targeted initiatives are amounts raised through the LGI campaign, where the donors have expressed support for all the stated campaign goals (Note 1). The actual allocation of these funds among the stated goals will be determined based on need.

**15. Permanently restricted endowments**

As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the Diocesan Bishop to function as endowment funds, are classified and reported based on the existence of donor-imposed restrictions.

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Permanently restricted endowments are for the following purposes at June 30:

	<u>2014</u>	<u>2013</u>
Catholic education	\$ 20,299,841	\$ 18,568,841
Catechetics	2,045,653	2,045,653
Youth ministry	510,988	510,988
ADEF education scholarships	310,500	310,500
Diocesan operations	<u>50,000</u>	<u>50,000</u>
Original endowment corpus	23,216,982	21,485,982
Endowment major gifts receivable	<u>573,781</u>	<u>4,500</u>
Total	<u><u>\$ 23,790,763</u></u>	<u><u>\$ 21,490,482</u></u>

**Interpretation of relevant law**

The Uniform Prudent Management of Institutional Funds Act (UPMIFA), effective July 1, 2008, in the Commonwealth of Virginia, has been interpreted as requiring the preservation of fair value of the original gift as of the date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Chancery 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 Chancery in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Chancery considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the funds
2. The purposes of the Chancery and the donor-restricted endowment funds
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 Chancery
7. The investment policies of the Chancery

**Funds with deficiencies**

From time to time, the fair value of assets associated with individual donor-restricted funds may fall below the level that the donor or UPMIFA requires the Chancery to retain as a fund of perpetual duration. There were no such deficiencies as of June 30, 2014 and 2013.

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**Investment return objectives, risk parameters and strategies**

The Chancery has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment funds while also maintaining the purchasing power of those endowment assets over the long-term. Accordingly, the investment process seeks to achieve an after-cost total real rate of return, including investment income as well as capital appreciation, which exceeds the annual distribution with acceptable levels of risk. Endowment assets are invested in a well-diversified asset mix, which includes equity and debt securities, which is intended to result in a consistent inflation-protected rate of return that has sufficient liquidity to make an annual distribution ranging from 4% to 5%, while growing the funds if possible. Therefore, the Chancery expects its endowment assets, over time, to produce an average rate of return of between 7% and 10% annually. Actual returns in any given year may vary from this amount. Investment risk is measured in terms of the total endowment fund; investment assets and allocation between asset classes and strategies are managed to not expose the fund to unacceptable levels of risk.

**Spending policy**

The Chancery has a policy of appropriating for distribution each year 4% of its endowment fund average fair value of the prior 12 quarters through the calendar year-end preceding the fiscal year in which the distribution is planned except for ADEF education scholarships which is 5% of the average fair value of the three previous calendar years. In establishing these policies, the Chancery considered the long-term expected return on its investment assets. The Chancery expects the current spending policy to allow its endowment funds to grow at a nominal average rate of between 3% and 4% annually over the spending rate. This is consistent with the Chancery's objective to maintain the purchasing power of the endowment assets as well as to provide additional real growth through new gifts and investment return.

Endowment net asset composition by type of fund as of June 30, 2014 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Donor-restricted endowment funds	\$ -	\$ 15,880,098	\$ 23,216,982	\$ 39,097,080
Endowment major gifts receivable	-	-	573,781	573,781
Board-designated endowment funds	11,761,241	-	-	11,761,241
Total funds	<u>\$ 11,761,241</u>	<u>\$ 15,880,098</u>	<u>\$ 23,790,763</u>	<u>\$ 51,432,102</u>

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Endowment net asset composition by type of fund as of June 30, 2013 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Donor-restricted endowment funds	\$ -	\$ 9,750,716	\$21,485,982	\$31,236,698
Endowment major gifts receivable	-	-	4,500	4,500
Board-designated endowment funds	9,625,921	-	-	9,625,921
Total funds	<u>\$ 9,625,921</u>	<u>\$ 9,750,716</u>	<u>\$21,490,482</u>	<u>\$40,867,119</u>

**Donor-restricted endowments**

Changes in donor-restricted endowment net assets as of June 30, 2014 are as follows:

	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Endowment net assets, beginning of year	\$ 9,750,716	\$ 21,485,982	\$ 31,236,698
Contributions	-	1,731,000	1,731,000
Investment income	383,692	-	383,692
Net appreciation	6,504,184	-	6,504,184
Amounts appropriated for expenditure and satisfying purpose restrictions	(758,491)	-	(758,491)
Endowment net assets, end of year	<u>\$ 15,880,101</u>	<u>\$ 23,216,982</u>	<u>\$ 39,097,083</u>

Changes in donor-restricted endowment net assets as of June 30, 2013 are as follows:

	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Endowment net assets, beginning of year	\$ 7,020,060	\$ 17,976,859	\$ 24,996,919
Contributions	-	3,509,123	3,509,123
Investment income	397,587	-	397,587
Net appreciation	3,012,036	-	3,012,036
Amounts appropriated for expenditure and satisfying purpose restrictions	(678,967)	-	(678,967)
Endowment net assets, end of year	<u>\$ 9,750,716</u>	<u>\$ 21,485,982</u>	<u>\$ 31,236,698</u>

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**Board-designated endowment (functioning as endowment)**

Certain amounts of unrestricted net assets, which include the original patrimony of the Diocese, have been designated by the Diocesan Bishop as functioning as endowment. Since these amounts resulted from an internal designation and are not donor-restricted, they are classified and reported as unrestricted net assets (functioning as endowment). This endowment's investment policy, strategy and objectives are similar to the donor-invested policies, except as it relates to investment spending. All investment returns are added to the endowment.

Composition of and changes in board-designated endowment net assets for the year ended June 30, are as follows:

	<b>Unrestricted</b>	
	<b>2014</b>	<b>2013</b>
Board-designated endowment net assets, beginning of year	\$ 9,625,921	\$ 8,441,012
Investment income	113,412	130,266
Net appreciation	2,021,908	1,054,643
Board-designated endowment net assets, end of year	<u>\$ 11,761,241</u>	<u>\$ 9,625,921</u>

**16. Insurance programs**

The Diocese maintains health, property, general liability and workers compensation insurance plans for the Chancery and participating affiliates. Each entity participating in the plans is charged premiums to cover estimated losses, administrative costs, and excess insurance policy premiums.

Under the medical plan, the self-insured retention layer includes an individual loss limit, \$200,000 in plan years 2014 and 2013, as well as an aggregate loss limit of up to 125% of expected claims, or about \$11,249,000, in plan year March 2014-February 2015. Losses exceeding these amounts are covered by the stop-loss insurance policy with no annual limit on aggregate losses. Incurred but not reported health claims are estimated to be \$1,477,000 and \$1,104,000 at June 30, 2014 and 2013, respectively.

The Diocese continues to maintain a multi-tiered approach to its risk financing program which includes both risk retention and risk transferring strategies. With regard to workers' compensation, coverage is 100% insured and the Diocese does not retain any exposure for this coverage.

The Diocese retains the first layer of coverage for all other property and casualty exposures with the exception of workers' compensation which is fully insured. The self-insured retention layer is \$200,000 per occurrence with an annual aggregate of \$600,000. The retention amount applies cumulatively to property and liability exposures. The Chancery's estimated exposure for future payments of this layer is \$618,000 and \$862,000 at June 30, 2014 and 2013, respectively. Several layers of excess coverage from various carriers beyond the self-insured retention layer and primary insurance layer exist. The amount of excess coverage differs based on the given line of coverage, and at a minimum provides \$1,000,000 of additional insurance.

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Prior to July 2007, the second layer of coverage was retained by the Catholic Umbrella Pool II (CUP II) which is a risk retention pool consisting of member Dioceses of which Arlington is included. This coverage provided \$5,500,000 in excess of the primary layer of \$1,500,000 of insurance coverage. Currently there are 59 participants each with equal voting rights. Participation percentages vary annually based on the exposures of the Diocese and the number of participating entities. The Diocese participation interest has averaged 1.87% of the total contributions to the Pool.

The Diocese does retain an exposure equal to its participation level in any year should the claims in that year exceed contributions collected. The Chancery estimates no material loss with regard to this participation.

Included in accounts payable and accrued expenses are the following:

	<u>2014</u>	<u>2013</u>
Incurred but not reported estimated health claims	\$ 1,477,000	\$ 1,104,000
Estimated property and general liability claims	\$ 618,000	\$ 862,000

**17. Commitments and contingencies**

**Leases**

The Chancery leases office space under a non-cancelable lease agreement with 200 North Glebe Road, Inc., a related entity, which expires July 31, 2017. The lease provides for an automatic adjustment of 3% annually. The financial statements reflect rent expense on a straight-line basis with the excess expense over cash paid reflected in accrued expenses. In addition to lease payments, the office lease generally requires the Chancery to pay any incremental increases in taxes, insurance and utilities. The Chancery also leases office equipment under operating leases expiring through August 2018. Total rent expense, net of sublease rentals for years ended June 30, 2014 and 2013, is as follows:

	<u>2014</u>	<u>2013</u>
Office space	\$ 1,994,020	\$ 1,964,274
Office equipment	111,689	106,293
Sublease office rental (related entities)	(361,257)	(392,777)
Net expense	<u>\$ 1,744,452</u>	<u>\$ 1,677,790</u>

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At June 30, 2014, future minimum lease payments are as follows:

	<u>Total Lease</u>	<u>Sublease</u>	<u>Net Lease</u>
2015	\$ 1,913,561	\$ 372,094	\$ 1,541,467
2016	1,966,305	383,257	1,583,048
2017	2,005,454	394,755	1,610,699
2018	206,510	32,976	173,534
2019	7,062	-	7,062
Total future minimum lease payments	<u>\$ 6,098,892</u>	<u>\$ 1,183,082</u>	<u>\$ 4,915,810</u>

**Lines of credit and letters of credit**

The Chancery has obtained lines of credit as follows:

	<u>June 30, 2014</u>		<u>June 30, 2013</u>	
	<u>Total Available</u>	<u>Outstanding</u>	<u>Total Available</u>	<u>Outstanding</u>
Operating needs	\$ 5,000,000	\$ -	\$ 5,000,000	\$ -
Building and improvement programs	\$ -	\$ 5,633,503	\$ -	\$ 6,543,005
Standby letters of credit for various construction projects	\$ 15,000,000	\$ 2,121,498	\$ 15,000,000	\$ 2,610,177

The outstanding building and improvement loans were obtained for the benefit of two parishes. The parishes are currently paying on and directly liable for these loans with the Chancery acting as guarantor. Under the loan agreements, the Chancery is subject to certain financial covenants such as operating liquidity, minimum net assets, additional indebtedness and financial reporting. The building improvement programs have interest rates ranging from 2.67% to 5.25% for the years ended June 30, 2014 and 2013.

In connection with the bond refinancing and issuance of bank qualified debt, the Chancery renewed its line of credit and letter of credit facility (Note 11). Under the new agreements, the Chancery is subject to certain covenants such as operating liquidity, additional indebtedness, and financial reporting. The line of credit for operating needs had a stated rate of interest based on the 30-day LIBOR plus 195 basis points for the years ended June 30, 2014 and 2013. The issuance fee for standby letters of credit for various parish and Chancery construction projects was 1.5% per annum with a minimum of \$200 per letter for the years ended June 30, 2014 and 2013. These facilities are subject to annual renewals by our financial institutions.

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Notes to Combined Financial Statements  
For the years ended June 30, 2014 and 2013**

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**Investments**

In connection with alternative investments, the Chancery has entered into several subscription agreements where there are requirements to make future capital contributions in the amount of \$2,496,918. The commitment periods under these agreements are determined by the Fund managers.

**Litigation**

The Diocese has been named as a defendant in various lawsuits. Coverage for each of the lawsuits is provided by either a self-insurance fund or excess insurance coverage. When applicable, reserves have been established for those cases where the potential liability is estimable and probable. In instances where a loss is reasonably possible, but the amount is not estimable no reserve is established. There was no reserve for 2014 and 2013.

**Purchase and construction agreements**

In connection with various construction projects, the Chancery is committed under contracts with remaining amounts of \$196,280.