

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

**Combined Financial Statements and Combining Information  
as of June 30, 2011 and 2010 and Report Thereon**

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

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**June 30, 2011 and 2010**

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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 statements of financial position of the Central Administrative Office of the Catholic Diocese of Arlington and its affiliate (the Chancery) as of June 30, 2011 and 2010, and the related combined statements of activities and cash flows for the years then ended. These combined financial statements are the responsibility of the Chancery's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our 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, 2011 and 2010, and the changes in its net assets and cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

*LarsonAllen LLP*  
**LarsonAllen LLP**

St. Cloud, Minnesota  
October 11, 2011



**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
 Combined Statements of Financial Position  
 As of June 30, 2011 and 2010**

	<u>2011</u>	<u>2010</u>
<b>Assets</b>		
Cash and cash equivalents	\$ 11,265,968	\$ 19,803,267
Accounts receivable, net	1,365,620	945,523
Accrued interest receivable	117,644	109,117
Bishop's Lenten Appeal pledges receivable	3,249,308	2,678,281
Bequests and major gifts pledges receivable, net	3,230,582	3,002,209
<i>Rooted in Faith - Forward in Hope, Inc.</i>		
pledges receivable, net	1,098,347	1,660,000
Investments	134,642,953	104,587,841
Prepaid expenses and other assets	1,424,730	524,643
Unamortized bond costs	375,265	392,005
Demand notes and loans receivable		
Paul VI High School bond receivable	4,209,917	4,309,917
Pope John Paul the Great High School receivable	6,358,523	3,912,695
Diocesan Investment and Loan (DIAL) program	-	49,653,316
200 North Glebe Road, Inc.	4,834,286	4,884,286
Property, equipment and land, net	112,761,803	109,801,711
Construction in progress and assets not yet placed in service	-	6,502,811
Land restricted for high school	14,500,000	14,500,000
Total assets	<u>\$ 299,434,946</u>	<u>\$ 327,267,622</u>
<b>Liabilities and Net Assets</b>		
<b>Liabilities</b>		
Deposits held in custody for others	\$ 2,253,477	\$ 1,651,558
Accounts payable and accrued expenses	4,007,816	4,276,227
Accrued interest payable	308,405	314,256
Unearned revenue	923,916	194,045
DIAL deposits payable	-	98,694,502
Notes payable, net of discount	-	677,918
Amounts held on behalf of other diocesan entities	59,501,221	10,120,772
Annuity payment liability	209,112	131,588
Arlington Diocese Educational Foundation (ADEF) funds		
held for schools	2,515,401	2,276,713
Accrued pension liability, priests	4,305,868	5,437,213
Postretirement health benefit obligation	6,227,915	6,523,719
Line of credit payable	-	7,000,000
Bonds payable	23,205,000	23,740,000
Total liabilities	<u>103,458,131</u>	<u>161,038,511</u>
<b>Net assets</b>		
<b>Unrestricted</b>		
Current operations	35,597,754	12,000,987
Invested in property, equipment and land	94,100,799	96,826,489
Functioning as endowment	8,341,510	6,576,021
Designated	9,327,458	8,034,303
Total unrestricted	<u>147,367,521</u>	<u>123,437,800</u>
Temporarily restricted	30,161,286	24,436,272
Permanently restricted	18,448,008	18,355,039
Total net assets	<u>195,976,815</u>	<u>166,229,111</u>
Total liabilities and net assets	<u>\$ 299,434,946</u>	<u>\$ 327,267,622</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, 2011**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Operating revenues and support				
Bishop's Lenten Appeal	\$ 13,963,177	\$ -	\$ -	\$ 13,963,177
Operational assessment	6,699,824	-	-	6,699,824
Investment income for operations	1,400,000	-	-	1,400,000
Transmittal fees	144,649	-	-	144,649
Contributions, bequests and major gifts	4,322,288	5,425,100	92,969	9,840,357
Program revenue	1,744,553	-	-	1,744,553
Other revenue and support	10,072	-	-	10,072
Satisfaction of temporary restrictions	4,862,974	(4,862,974)	-	-
Total operating revenues and support	<u>33,147,537</u>	<u>562,126</u>	<u>92,969</u>	<u>33,802,632</u>
Operating expenses				
Program services				
Pastoral	6,479,230	-	-	6,479,230
Religious personnel development	2,792,594	-	-	2,792,594
Education	5,333,465	-	-	5,333,465
Social services	2,349,078	-	-	2,349,078
Supporting services				
Diocesan administration and parochial support	10,862,196	-	-	10,862,196
<i>Rooted in Faith - Forward in Hope, Inc.</i>	73,655	-	-	73,655
Bishop's Lenten Appeal	565,317	-	-	565,317
Total operating expenses	<u>28,455,535</u>	<u>-</u>	<u>-</u>	<u>28,455,535</u>
Change in net assets from operations	<u>4,692,002</u>	<u>562,126</u>	<u>92,969</u>	<u>5,347,097</u>
Other changes in net assets				
Investment income less amount included in operations, net	15,762,396	5,352,852	-	21,115,248
Bond interest expense	(1,004,977)	-	-	(1,004,977)
Insurance programs	2,534,237	-	-	2,534,237
Change in unfunded pension liability, priests	1,131,345	-	-	1,131,345
Change in unfunded postretirement health obligation	295,804	-	-	295,804
Net property gains	3,006,541	-	-	3,006,541
<i>Rooted in Faith - Forward in Hope, Inc.</i> contributions, net of bad debt losses	-	7,176	-	7,176
Related parties contributions	(4,217,316)	-	-	(4,217,316)
DIAL loan interest income	2,156,129	-	-	2,156,129
DIAL deposit interest expense	(2,202,279)	-	-	(2,202,279)
Rental income - diocesan properties	1,578,699	-	-	1,578,699
Satisfaction of temporary restrictions	197,140	(197,140)	-	-
Total other changes in net assets	<u>19,237,719</u>	<u>5,162,888</u>	<u>-</u>	<u>24,400,607</u>
Change in net assets	23,929,721	5,725,014	92,969	29,747,704
Net assets, beginning of year	123,437,800	24,436,272	18,355,039	166,229,111
Net assets, end of year	<u>\$147,367,521</u>	<u>\$ 30,161,286</u>	<u>\$ 18,448,008</u>	<u>\$ 195,976,815</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, 2010**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Operating revenues and support				
Bishop's Lenten Appeal	\$ 12,538,426	\$ -	\$ -	\$ 12,538,426
Operational assessment	6,682,150	-	-	6,682,150
Investment income for operations	1,650,000	-	-	1,650,000
Transmittal fees	140,235	-	-	140,235
Contributions, bequests and major gifts	781,032	4,003,809	334,473	5,119,314
Program revenue	1,832,454	-	-	1,832,454
Refugee assistance	-	543,977	-	543,977
Other revenue and support	52,442	-	-	52,442
Satisfaction of temporary restrictions	4,508,442	(4,508,442)	-	-
Total operating revenues and support	<u>28,185,181</u>	<u>39,344</u>	<u>334,473</u>	<u>28,558,998</u>
Operating expenses				
Program services				
Pastoral	5,361,486	-	-	5,361,486
Religious personnel development	2,552,151	-	-	2,552,151
Education	5,188,200	-	-	5,188,200
Social services	2,277,231	-	-	2,277,231
Refugee assistance	543,977	-	-	543,977
Supporting services				
Diocesan administration and parochial support	10,417,106	-	-	10,417,106
<i>Rooted in Faith - Forward in Hope, Inc.</i>	72,036	-	-	72,036
Bishop's Lenten Appeal	618,561	-	-	618,561
Total operating expenses	<u>27,030,748</u>	<u>-</u>	<u>-</u>	<u>27,030,748</u>
Change in net assets from operations	<u>1,154,433</u>	<u>39,344</u>	<u>334,473</u>	<u>1,528,250</u>
Other changes in net assets				
Investment income less amount included in operations, net	4,513,109	1,997,402	-	6,510,511
Bond interest expense	(1,023,953)	-	-	(1,023,953)
Insurance programs	2,435,793	-	-	2,435,793
Change in unfunded pension liability, priests	(1,835,387)	-	-	(1,835,387)
Change in unfunded postretirement health obligation	(1,939,012)	-	-	(1,939,012)
Net property gains	-	-	-	-
<i>Rooted in Faith - Forward in Hope, Inc.</i> contributions, net of bad debt losses	-	(1,284,259)	-	(1,284,259)
DIAL loan interest income	2,413,302	-	-	2,413,302
DIAL deposit interest expense	(2,678,597)	-	-	(2,678,597)
Rental income - diocesan properties	1,535,671	-	-	1,535,671
Satisfaction of temporary restrictions	6,108,853	(6,108,853)	-	-
Total other changes in net assets	<u>9,529,779</u>	<u>(5,395,710)</u>	<u>-</u>	<u>4,134,069</u>
Change in net assets	10,684,212	(5,356,366)	334,473	5,662,319
Net assets, beginning of year	112,753,588	29,792,638	18,020,566	160,566,792
Net assets, end of year	<u>\$123,437,800</u>	<u>\$ 24,436,272</u>	<u>\$ 18,355,039</u>	<u>\$ 166,229,111</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, 2011 and 2010**

	<b>2011</b>	<b>2010</b>
Cash flows from operating activities		
Change in net assets	29,747,704	\$ 5,662,319
Adjustments to reconcile change in net assets to net cash and cash equivalents provided by operating activities		
Depreciation of property	2,629,684	2,226,686
Gain on sale of assets	(3,018,542)	-
Contributed investment, real property	(2,936,000)	-
(Decrease) in allowance for uncollectible accounts receivable	(700)	(4,975)
(Decrease) in discount on major gifts pledges receivable	(51,170)	(120,592)
Bad debt losses in <i>Rooted in Faith~Forward in Hope, Inc.</i> pledges receivable	-	1,298,140
Decrease in discount on notes payable	27,082	11,776
Unrealized and realized (gain) on investments	(21,242,044)	(6,543,320)
(Decrease) in amounts held on behalf of other diocesan entities	(3,024,518)	(2,195,749)
(Increase) decrease in accounts receivable	(419,397)	498,597
(Increase) decrease in accrued interest receivable, net of amounts transferred	(8,729)	5,793
(Increase) in BLA pledges receivable	(571,027)	(146,514)
(Increase) decrease in bequests and major gift pledges receivable	(177,203)	1,206,127
Decrease in <i>Rooted in Faith~Forward in Hope, Inc.</i> pledges receivable	561,653	2,484,253
(Increase) in prepaid expenses and other assets	(900,087)	(101,066)
Decrease in unamortized bond costs	16,740	16,741
Increase in deposits held in custody for others	599,762	1,167,105
Increase (decrease) in accounts payable and accrued expenses	171,544	(188,606)
(Decrease) in ADEF funds held for schools	(10,587)	(759)
(Decrease) in accrued interest payable	(5,851)	(5,578)
Increase in unearned revenue	729,871	166,725
(Decrease) increase in accrued pension liability, priests	(1,131,345)	1,835,387
(Decrease) increase in postretirement health benefit obligation	(295,804)	1,939,012
Increase (decrease) in annuity payment liability	77,524	(8,128)
Net cash and cash equivalents provided by operating activities	768,560	9,203,374
Cash flows from investing activities		
Purchases of buildings and land	-	(1,307,700)
Purchases of equipment	(626,225)	(513,484)
Payments made for construction in progress and improvements	(82,153)	(7,350,773)
Proceeds from sale of property	4,200,000	-
Decrease in 200 North Glebe Road loan receivable	50,000	600,000
Loans to Pope John Paul the Great High School	(2,445,828)	(2,444,531)
DIAL demand loans made	(5,307,368)	(6,171,251)
Repayments on DIAL demand loans	12,200,112	5,264,833
Purchases of investments	(161,681,334)	(146,384,367)
Sales of investments	156,571,938	157,836,019
Net cash and cash equivalents provided by (used in) investing activities	2,879,142	(471,254)
Cash flows from financing activities		
Deposits into DIAL deposits payable	25,672,740	27,070,772
Withdrawals of DIAL deposits	(17,187,314)	(35,364,559)
Cash transferred to DIAL Corp	(12,530,427)	-
Decrease in Paul VI High School loan receivable	100,000	95,000
(Repayment) proceeds from line of credit	(7,000,000)	7,000,000
Repayments of notes payable	(705,000)	-
Repayments of bonds payable	(535,000)	(510,000)
Net cash and cash equivalents (used in) financing activities	(12,185,001)	(1,708,787)
Net increase (decrease) in cash and cash equivalents	(8,537,299)	7,023,333
Cash and cash equivalents, at beginning of year	19,803,267	12,779,934
Cash and cash equivalents, at end of year	\$ 11,265,968	\$ 19,803,267

*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, 2011 and 2010**

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	<u>2011</u>	<u>2010</u>
Supplemental cash flow information		
Interest paid on debt	\$ 1,260,272	\$ 1,276,703
Supplemental schedule of non-cash investing and financing activities		
Equipment and construction in progress purchases in accounts payable	\$ 41,186	\$ 439,955
Contributed investment, real property	\$ 2,936,000	\$ -
<p>On May 1, 2011, the assets and liabilities of the DIAL Fund as administered by the Central Administrative Office of the Catholic Diocese of Arlington were transferred to DIAL Corp. Assets and (liabilities) transferred were as follows:</p>		
Cash	\$ 12,530,427	
Accrued interest receivable	202	
Investments (held in master investment pool)	51,888,727	
Loans receivable	42,760,572	
Deposits payable	(107,179,928)	
	<u>\$ -</u>	

*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, 2011 and 2010**

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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 ministering 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 fund raising drive.

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, 2011 and 2010**

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The Campaign's goal was to raise a minimum of \$75 million for the following specific needs:

- \$15 million for parish needs
- \$25 million for Catholic education projects
- \$15 million for establishment of tuition assistance, faculty development, catechetics and youth ministry endowment funds
- \$5 million for creation of a priests' retirement home
- \$5 million for creation of a diocesan spirituality center
- \$5 million for establishment of a Catholic Charities endowment fund
- \$5 million for the creation of Catholic Charities' emergency shelter projects

Funds raised in excess of the goal of \$60 million for non-parish needs have been placed in a separate temporarily restricted fund (allocation fund) to be allocated at the discretion of the Bishop to those Campaign needs, except Catholic Charities, requiring additional funding beyond the original goal.

**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. or Arlington Diocesan Investment and Loan Corporation (DIAL Corp), over which the Diocesan Bishop exercises control, and are reported separately. Significant 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

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Notes to Combined Financial Statements  
For the years ended June 30, 2011 and 2010**

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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.

*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.

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Notes to Combined Financial Statements**  
**For the years ended June 30, 2011 and 2010**

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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 receivable**

Accounts 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 receivable.

**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 consist of money market funds, mutual funds, government and government-sponsored enterprises' securities, corporate, foreign and municipal bonds and equities. Fair value for investments is determined by reference to quoted prices in an active market and other relevant information generated by market transactions. Also included in investments is an interest in a limited liability partnership which is considered an alternative investment. The Chancery carries its investment at fair value based on the respective net asset value and other financial information reported by external investment managers. In this case, the underlying investments of the investment fund are accounted for at fair value as described in the investment fund's financial statements, all of which are subject to a third party annual audit. Due to the inherent uncertainty of valuation, the fair value of the investments may differ significantly from the values that would have been used had a ready market for the investments existed, and the differences could be material.

**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 is recorded on the accrual basis.

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Notes to Combined Financial Statements**  
**For the years ended June 30, 2011 and 2010**

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**Investment pools**

The Chancery maintains master investment accounts for long-term assets, including certain DIAL reserves and endowments, including those amounts held on behalf of Catholic Charities and DIAL Corp. 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.

**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.

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 reclassified to unrestricted net assets.

Contributions solicited and 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. As of June 30, 2011 all non-interest bearing demand deposits were federally insured. Other deposits exceeded 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 \$3,027 as of June 30, 2011. The Chancery also invests excess funds (\$6,182,649 as of June 30, 2011) 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. Pledges

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receivable, which have been adjusted for doubtful accounts, are due from individuals, corporations, and foundations. The amount due from two contributors comprises 97% of the total bequest and major gifts pledges receivable balance at June 30, 2011. The amount due from another contributor comprises 68% of the *Rooted in Faith~Forward in Hope, Inc.* pledges receivable at June 30, 2011. 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.

**Reclassifications**

Certain prior year amounts have been reclassified to conform to the current year financial statement presentation.

**Subsequent events**

In preparing these financial statements, the Chancery has evaluated events and transactions for potential recognition or disclosure through October 11, 2011, the date the financial statements were available to be issued.

**3. Accounts receivable**

The Chancery bills the parishes, schools and miscellaneous 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.

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As of June 30, 2011 and 2010, respectively, the Chancery had the following accounts receivable:

	<u>2011</u>	<u>2010</u>
Parishes	\$ 647,019	\$ 441,548
Schools	630,018	514,077
Employee advances	6,433	5,052
Federal and state grants receivable	-	1,824
Due from brokers	48,596	13,378
Miscellaneous	156,908	93,698
Total accounts receivable	<u>1,488,974</u>	<u>1,069,577</u>
Less: allowance for doubtful accounts	<u>(123,354)</u>	<u>(124,054)</u>
Total accounts receivable, net	<u>\$ 1,365,620</u>	<u>\$ 945,523</u>

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

As of June 30, 2011 and 2010, contributors to the Bishop's Lenten Appeal (BLA) have unconditionally promised to give \$3,249,308 and \$2,678,281. As the Bishop's Lenten Appeal is an annual campaign, the pledges are due within one year.

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

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

	<u>2011</u>	<u>2010</u>
Receivables due in one year or less	\$ -	\$ 11,351
Receivables due in one to five years	<u>3,343,202</u>	<u>3,154,648</u>
Total unconditional promises to give	3,343,202	3,165,999
Less: discount to present value	<u>(112,620)</u>	<u>(163,790)</u>
Pledges receivable, net	<u>\$ 3,230,582</u>	<u>\$ 3,002,209</u>

Unconditional promises to give due in more than one year are discounted at rates ranging from 1.24% to 3.57%.

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**6. Rooted in Faith ~ Forward in Hope, Inc. pledges receivable**

Campaign pledges receivable at June 30 are:

	<u>2011</u>	<u>2010</u>
Receivables due in one year or less	\$ 4,167,377	\$ 7,284,277
Less: allowance for doubtful accounts	<u>(3,069,030)</u>	<u>(5,624,277)</u>
Pledges receivable, net	<u>\$ 1,098,347</u>	<u>\$ 1,660,000</u>

Bad debt losses for the years ended June 30, 2011 and 2010 were \$0 and \$1,298,140, respectively. The collectability of outstanding pledges was re-evaluated during the years ended June 30, 2011 and 2010. The allowance for doubtful accounts was adjusted based on a detailed analysis of specific parishes, pledges and trends. It is at least reasonably possible that the estimated pledges to be collected may change within the next year.

**7. Investments**

Investments are stated at fair value. The cost of investments and related fair values at June 30, 2011 and 2010 consist of the following:

	<u>2011</u>		<u>2010</u>	
	<u>Cost</u>	<u>Fair Value</u>	<u>Cost</u>	<u>Fair Value</u>
Short-term investments	\$ 9,547,985	\$ 9,547,985	\$ 15,400,343	\$ 15,400,343
U.S. Government and sponsored enterprises securities	4,166,310	4,324,441	3,181,397	3,404,245
Corporate, municipal and foreign bonds and other fixed instruments	24,591,476	27,449,150	20,343,963	23,166,748
Equities, including publicly traded REITs	73,918,622	88,997,467	59,277,834	61,283,864
Real property held for investment	2,936,000	2,936,000	-	-
Limited partnerships	1,004,399	1,387,910	1,045,891	1,332,641
	<u>\$ 116,164,792</u>	<u>\$ 134,642,953</u>	<u>\$ 99,249,428</u>	<u>\$ 104,587,841</u>

Also included in investments at June 30, 2011 and 2010 is \$255,307 and \$131,981, 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 four to seventeen 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>2011</u>	<u>2010</u>
Current operations and programs	\$ 33,326,782	\$ 8,135,029
Long-term purposes, including endowments	36,373,608	25,370,837
Assets held on behalf of other diocesan entities, including DIAL	59,092,032	65,644,332
Reserve fund, bonds payable	1,784,881	1,802,277
Arlington Diocese Educational Fund (ADEF)	4,065,650	3,635,048
<i>Rooted in Faith~Forward in Hope</i>	-	318
Total	<u>\$ 134,642,953</u>	<u>\$ 104,587,841</u>

Investments in the amount of \$108,865,474 and \$85,123,059 as of June 30, 2011 and 2010, respectively, are held in a pool under a trust agreement with a bank in which participants share in allocated investment income.

Investment income is reported on the Statement of Activities as follows:

	<u>2011</u>	<u>2010</u>
For Operations	\$ 1,400,000	\$ 1,650,000
In Other changes in net assets	21,115,248	6,510,511
Net investment gains (losses) - Chancery	<u>\$ 22,515,248</u>	<u>\$ 8,160,511</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, 2011 and 2010, respectively, consists of the following:

	<u>2011</u>	<u>2010</u>
<b>Chancery</b>		
Interest, dividends and other investment income	\$ 1,933,090	\$ 2,220,280
Realized gains and (losses), net	7,337,402	5,472,235
Unrealized gains and (losses), net	13,904,642	1,071,085
Less - investment management expenses	<u>(659,886)</u>	<u>(603,089)</u>
Net investment gains (losses) - Chancery	<u>\$ 22,515,248</u>	<u>\$ 8,160,511</u>
<b>Funds held for Diocesan entities</b>		
Investment income allocated to Diocesan entities	\$ 1,277,124	\$ 872,314
Total net investment gains (losses) - Chancery and funds held for Diocesan entities	<u>\$ 23,792,372</u>	<u>\$ 9,032,825</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.

**8. 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>2011</u>		<u>2010</u>	
	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Cash and cash equivalents	\$ 11,265,968	\$ 11,265,968	\$ 19,803,267	\$ 19,803,267
Investments	\$ 134,642,953	\$ 134,642,953	\$ 104,587,841	\$ 104,587,841
Demand notes and loans receivable	\$ 15,402,726	\$ 13,804,081	\$ 62,760,214	\$ 61,803,237
DIAL deposits payable	\$ -	\$ -	\$ 98,694,502	\$ 98,694,502
Notes payable	\$ -	\$ -	\$ 677,918	\$ 692,115
Bonds payable	\$ 23,205,000	\$ 23,836,920	\$ 23,740,000	\$ 24,662,073

The carrying amount approximates fair value of cash and DIAL deposits. The fair value of long-term debt is based on current rates at which the Chancery could borrow funds with similar remaining maturities.

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**9. 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, 2011 are as follows:

	<u>Fair Value</u>	<u>Quote Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Short-term investments	\$ 9,547,985	\$ 9,547,985	\$ -	\$ -
U.S. Government and sponsored enterprises securities	4,324,441	1,331,838	2,992,603	-
Corporate, municipal and foreign bonds and other fixed instruments	27,449,150	-	27,449,150	-
Equities, including publicly traded REITs	88,997,467	88,997,467	-	-
Real property held for investment	2,936,000	-	2,936,000	-
Limited partnerships	1,387,910	-	-	1,387,910
Total	<u>\$ 134,642,953</u>	<u>\$ 99,877,290</u>	<u>\$ 33,377,753</u>	<u>\$ 1,387,910</u>

Fair values of assets measured on a recurring basis by level at June 30, 2010 are as follows:

	<u>Fair Value</u>	<u>Quote Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Short-term investments	\$ 15,400,343	\$ 15,400,343	\$ -	\$ -
U.S. Government and sponsored enterprises securities	3,404,245	1,087,550	2,316,695	-
Corporate and municipal bonds and other fixed instruments	23,166,748	-	23,166,748	-
Equities, including publicly traded REITs	61,283,864	60,680,180	603,684	-
Limited partnerships	1,332,641	-	-	1,332,641
Total	<u>\$ 104,587,841</u>	<u>\$ 77,168,073</u>	<u>\$ 26,087,127</u>	<u>\$ 1,332,641</u>

Included in investments is an interest in a limited liability partnership comprised of timber, energy and real estate portfolios which is considered an alternative investment. This investment is classified within Level 3 as the value of this interest is primarily based on the net asset value reported by external fund managers. Additionally, the Chancery's rights of transfer or redemption are subject to terms of the partnership agreement. It is anticipated that the investment will be liquidated over the life of the fund.

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

	<u>2011</u>	<u>2010</u>
Balance, beginning of year	\$1,332,641	\$1,438,578
Contributions/(distributions), net	(41,492)	2,309
Change in value - unrealized (loss)	96,761	(108,246)
Balance, end of year	<u>\$1,387,910</u>	<u>\$1,332,641</u>

Unrealized gains (losses) recorded for Level 3 investments are reported as investment income under other changes in net assets on the Statement of Activities.

**10. 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>2011</u>	<u>2010</u>
Assets:		
Accounts receivable, parishes, schools and other related entities	\$ 1,314,113	\$ 862,283
Paul VI High School bond receivable, for \$4,839,917 in bond proceeds used for renovations and additions, terms equivalent to those for bonds payable (Note 14)	4,209,917	4,309,917
Pope John Paul the Great High School loan receivable, to supplement tuition in covering operating costs, interest waived for 2011 and 2010, no fixed repayment, repayments accepted as cash is available	6,358,523	3,912,695
DIAL Program loans receivable, parishes and high schools	-	49,653,316
200 North Glebe Road, Inc., interest waived for 2011 and 2010, due on demand, repayments accepted as cash is available	4,834,286	4,884,286
	<u>\$16,716,839</u>	<u>\$63,622,497</u>

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	<u>2011</u>	<u>2010</u>
Liabilities:		
Accounts payable, parishes, schools, other related entities	\$ 16,663	\$ 41,771
DIAL deposits payable	-	98,694,502
Due to parishes, split interest annuities	107,264	104,231
Amounts held on behalf of other diocesan entities:		
DIAL Corp, funds held in investment pool	51,061,802	-
Catholic Charities, housing program	-	2,890,507
Catholic Charities, endowment funds held in investment pool	8,030,231	6,420,569
Catholic Charities, major gift pledges	96,513	142,250
Due to parish, major gift pledge, net of discount	4,703	7,153
<i>Rooted-In-Faith~Forward in Hope</i> Campaign pledges:		
Due to parishes, net of allocated bad debt losses	303,844	602,165
Due to Catholic Charities, housing program and endowment	4,128	58,128
ADEF funds held for schools	2,515,401	2,276,713
	<u>\$ 62,140,549</u>	<u>\$ 111,237,989</u>

	<u>2011</u>	<u>2010</u>
Revenues and Support:		
Operational assessment, parishes	\$ 6,699,824	\$ 6,682,150
Contributions, diocesan tuition assistance program	1,837,499	1,750,001
Program fees	1,018,281	1,099,674
Accounting and computer service fees	98,400	31,200
Rental income, Catholic Charities	179,105	96,597
Rental income, Arlington Catholic Herald	107,953	102,664
Rental income, Pope John Paul the Great High School	1,445,828	1,444,531
Insurance and risk management premiums billed	15,945,842	15,991,628
DIAL Program interest income from member loans	2,156,129	2,413,302
	<u>\$29,488,861</u>	<u>\$29,611,747</u>

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	<u>2011</u>	<u>2010</u>
Expenses:		
Rent paid to 200 N. Glebe Road, Inc.	\$ 1,713,209	\$ 1,555,468
Contributions, tuition assistance program	1,830,047	1,745,000
Contribution, subsidy to Catholic Charities	1,197,750	1,180,092
Contribution, other program service subsidies	413,651	250,000
Contributions made to Lay Retirement Plan	682,366	622,543
Contributions made to Priest Retirement Plan	119,250	108,000
Advertising expense to Arlington Catholic Herald	99,927	99,400
DIAL program contributions	4,217,316	-
DIAL fund interest expense on member deposits	2,299,229	2,678,597
	<u>\$12,572,745</u>	<u>\$ 8,239,100</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.

The Chancery administered a Diocesan Investment and Loan (DIAL) program for parishes and related entities (Note 11). The assets and liabilities of the DIAL program were transferred to Arlington Diocesan Investment and Loan Corporation (DIAL Corp) effective May 1, 2011. At its request, investment funds held for long-term purposes are held on their behalf by the Chancery in a master investment pool.

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.

Under the terms of the *Rooted In Faith~Forward In Hope* Campaign, parishes and Catholic Charities will receive a percentage of contributions for their programs. At its request, Catholic Charities endowment funds are held by the Chancery in a master investment pool.

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.

**11. Diocesan Investment and Loan (DIAL) Program**

DIAL was a collaborative effort where diocesan parishes, schools and other entities deposited excess funds and diocesan parishes and high schools could obtain loans for appropriate construction needs. Deposits earned 2.5% annual interest and were considered demand deposits. Loans given

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for construction purposes carried interest at 6.5% annually with maturity dates ranging from 2012 to 2032. Loans were not collateralized.

Effective May 1, 2011, assets and liabilities of DIAL Fund were transferred to Arlington Diocesan Investment and Loan Corporation (DIAL Corp), a Virginia non-stock corporation. DIAL Corp is a participant in the investment pool (see Note 7).

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

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

	<u>2011</u>	<u>2010</u>
Operating properties-buildings	\$ 84,448,642	\$ 79,117,413
Operating properties-land and land development	25,436,288	24,287,609
Operating properties-improvements	7,163,954	7,051,071
Operating properties-furniture and equipment	3,864,615	3,440,536
Land held for future projects and parishes	10,895,532	12,891,038
Office furniture and equipment	699,003	790,297
Computer hardware	165,968	269,668
Computer software	743,754	707,299
Vehicles	547,568	528,875
Leasehold improvements	691,329	691,329
Total property, equipment and land	<u>134,656,653</u>	<u>129,775,135</u>
Less: accumulated depreciation	<u>(21,894,850)</u>	<u>(19,973,424)</u>
Property, equipment and land, net	<u>\$ 112,761,803</u>	<u>\$ 109,801,711</u>

Depreciation expense was \$2,629,684 and \$2,226,686 during the years ended June 30, 2011 and 2010, respectively. Of the total assets listed above, \$12,468,173 and \$12,634,397 were fully depreciated at June 30, 2011 and 2010, respectively.

On October 31, 2003, land known as Oakland Farm was purchased for \$1,409,388 to be potentially used for construction of the diocesan spirituality center, one of the identified projects of the Campaign. Subsequent to purchase, it was decided that this property will be used for other purposes. The sellers took back two demand promissory notes for a total of \$705,000 (see Note 13). The notes were paid in full June, 2011.

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.



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As of June 30, 2010, included in construction in progress and assets not yet placed in service is building and furniture and equipment for a new diocesan priests' retirement residence. Assets necessary for initial use in the approximate amount of \$6,500,000 were placed in service October 2010.

Construction of Pope John Paul the Great High School was funded, in part, from tax-exempt bonds (see Note 14). 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.

Capitalized interest previously included in construction in progress is included in operating property. Amortization of capitalized interest is included in depreciation expense. Capitalized interest at June 30 was:

	<u>2011</u>	<u>2010</u>
Net amount capitalized, beginning of year	\$ 944,802	\$ 964,434
Less: amortization expense	19,632	19,632
Net amount capitalized, end of year	<u>\$ 925,170</u>	<u>\$ 944,802</u>

Upon completion of the high school, bond interest cost was charged to expense (see Note 14).

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

In January 2011, the Chancery completed a land exchange involving two properties located in Loudoun County, Virginia. Gain was recognized only in proportion to the ratio of cash received to total consideration received. The property received in the exchange was measured based on the recorded amount of the property surrendered plus the gain recognized of \$399,115.

**13. Notes payable**

The Chancery has two demand promissory notes to outside parties in the face amount of \$705,000 at June 30, 2010 (stated value of \$677,918; fair value of \$692,115). The fair value is based on an imputed interest rate of 3.25%. The notes are not collateralized. Interest on the outstanding balance of the notes is due monthly at the rate of 2% per annum. The total unamortized discount of \$27,082 at June 30, 2010 is based on an imputed interest rate of 4.01%. The notes were paid in full June, 2011.

**14. 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 12). The fair value of these bonds is \$23,836,920 and \$24,662,073 at June 30, 2011 and 2010, respectively. These bonds have varying maturity terms ranging through October 1, 2033 with interest payments due ranging from \$46,613 to

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\$666,247 and interest rates ranging from 4.375% to 5.500%. Interest is due and payable on April 1 and October 1 of each year. Principal, ranging from \$80,000 to \$1,695,000, is due and payable on October 1 each year. There is no expectation that any bonds will be redeemed prior to maturity. An amount equal to the maximum annual debt service on the bonds (\$1,784,881 at June 30, 2011) has been deposited in a reserve fund with Wells Fargo Bank Minnesota, N. A., the Trustee. The Chancery is subject to an acceleration clause under the default provisions of the Indenture of Trust and is subject to 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 \$1,004,977 and \$1,023,953, net of amount received from Paul VI Catholic High School, for the year ended June 30, 2011 and 2010, respectively.

The outstanding balance on the bonds at June 30, 2011 is \$23,205,000. Maturities on the bonds payable annually for the years through 2016 and thereafter are as follows:

2012	\$	555,000
2013		580,000
2014		605,000
2015		635,000
2016		665,000
Thereafter		20,165,000
	\$	<u>23,205,000</u>

**15. 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. Annual premiums are calculated based on 10% of eligible participant salaries, and are used toward the annual funding of the plan. The cost of the plan for the Chancery and charged to expense was \$682,366 and \$622,543 for the years ended June 30, 2011 and 2010, respectively. The plan is not subject to ERISA funding requirements.

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Notes to Combined Financial Statements**  
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**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.

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

	<u>2011</u>	<u>2010</u>
Change in benefit obligation:		
Benefit obligation at beginning of year	\$12,535,189	\$10,088,673
Service cost	505,639	386,208
Interest cost	677,695	665,773
Actuarial loss (gain)	(807,832)	1,812,379
Benefits paid	<u>(498,216)</u>	<u>(417,844)</u>
Benefit obligation at end of year	<u>12,412,475</u>	<u>12,535,189</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	7,097,976	6,486,847
Return on plan assets	840,847	442,973
Employer contributions	666,000	586,000
Benefits paid	<u>(498,216)</u>	<u>(417,844)</u>
Fair value of plan assets at end of year	<u>8,106,607</u>	<u>7,097,976</u>
Accrued pension liability, priests	<u>\$ 4,305,868</u>	<u>\$ 5,437,213</u>

The accumulated benefit obligation at June 30, 2011 and 2010 was \$11,465,928 and \$11,455,874, respectively. The net periodic pension cost for the years ended June 30, 2011 and 2010 were \$746,569 and \$593,518, respectively. Net loss previously recognized in unrestricted net assets not yet recognized as periodic pension cost at June 30, 2011 and 2010 were \$1,591,234 and \$2,803,148, respectively. The estimated net loss that will be amortized from changes in unrestricted net assets into net periodic benefit cost in 2012 is \$17,031.

Assumptions used to determine the year-end benefit obligation:

	<u>2011</u>	<u>2010</u>
Discount rate on the benefit obligation	5.50%	5.50%
Rate of expected return on plan assets	7.00%	7.00%
Rate of priests' compensation increase	2.00%	2.00%

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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 (see Note 9).

Fair values of the plan's assets measured on a recurring basis by level at June 30, 2011 are as follows:

	<u>Fair Value</u>	<u>Quote Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Short-term investments	\$ 341,595	\$ 341,595	\$ -	\$ -
U.S. Government and sponsored enterprises securities	3,724,279	1,297,512	2,426,767	-
Corporate and foreign bonds	808,518	-	808,518	-
Equities	3,232,215	3,232,215	-	-
Total	<u>\$ 8,106,607</u>	<u>\$ 4,871,322</u>	<u>\$ 3,235,285</u>	<u>\$ -</u>

Fair values of the plan's assets measured on a recurring basis by level at June 30, 2010 are as follows:

	<u>Fair Value</u>	<u>Quote Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Short-term investments	\$ 362,862	\$ 362,862	\$ -	\$ -
U.S. Government and sponsored enterprises securities	3,165,674	1,182,978	1,982,696	-
Corporate bonds	807,486	-	807,486	-
Equities	2,761,954	2,761,954	-	-
Total	<u>\$ 7,097,976</u>	<u>\$ 4,307,794</u>	<u>\$ 2,790,182</u>	<u>\$ -</u>

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
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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	7% - 50%
Fixed income securities	45% - 55%
Short term cash/money market	5% - 20%

The Diocese expects to contribute approximately \$740,000 to the plan in 2012. Benefits expected to be paid by the plan during the ensuing five years and thereafter are approximately as follows:

2012	\$ 481,165
2013	492,156
2014	551,290
2015	605,665
2016	676,146
Thereafter	\$ 3,910,493

**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.

**16. 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.

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Notes to Combined Financial Statements**  
**For the years ended June 30, 2011 and 2010**

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The following amounts relate to the postretirement health obligation:

	<u>2011</u>	<u>2010</u>
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 6,523,719	\$ 4,584,707
Service cost	229,197	171,284
Interest cost	355,178	304,984
Employee contributions	183,648	156,290
Actuarial (gain) loss	(891,690)	1,484,529
Benefits paid	<u>(172,137)</u>	<u>(178,075)</u>
Benefit obligation at end of year	6,227,915	6,523,719
Change in plan assets:		
Fair value of plan assets at beginning of year	-	-
Employer contributions	(11,511)	21,785
Employee contributions	183,648	156,290
Benefits paid	<u>(172,137)</u>	<u>(178,075)</u>
Fair value of plan assets at end of year	-	-
Post retirement health benefit obligation	<u>\$ 6,227,915</u>	<u>\$ 6,523,719</u>

The net periodic benefit cost (credit) for the years ended June 30, 2011 and 2010 were \$326,452 and \$178,523, respectively. Amounts previously recognized in unrestricted net assets not yet recognized as periodic benefit cost at June 30:

	<u>2011</u>	<u>2010</u>
Net gain	\$ 1,638,038	\$ 887,895
Net prior service credit	<u>232,751</u>	<u>349,127</u>
Amounts previously recognized in unrestricted net assets, not yet recognized as periodic benefit cost	<u>\$ 1,870,789</u>	<u>\$ 1,237,022</u>

The estimated net gain that will be amortized from changes in unrestricted net assets into net periodic benefit cost in 2012 is \$256,783.

Assumptions used to determine the year-end benefit obligation:

	<u>2011</u>	<u>2010</u>
Discount rate on the benefit obligation	5.50%	5.50%

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For measurement purposes, an 8.3% increase in the cost of health care benefits was assumed for 2011. This rate was assumed to decrease over a 16 year period to an ultimate rate of 4.5% by 2027. In 2010, a 10% increase was assumed with a decrease to 5% over 5 years, and then to remain level.

The Diocese expects to contribute approximately \$138,000 to the plan in 2012. Benefits expected to be paid by the plan during the ensuing five years and thereafter are approximately as follows:

2012	\$	138,000
2013		160,000
2014		186,000
2015		219,000
2016		248,000
Thereafter		1,496,000

**17. Temporarily restricted net assets**

Costs incurred in association with construction of Pope John Paul the Great High School, the priests' retirement home and the spirituality center resulted in a release of restricted net assets which is included in other changes in net assets. Expenses incurred for program activities such as seminarian education, educational programs, youth ministry, outreach, and communications resulted in a release of restricted net assets which is included in operations.

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

	<u>2011</u>	<u>2010</u>
Donated land restricted for high school	\$ 14,500,000	\$ 14,500,000
Catholic education	6,653,358	2,270,702
Retired priests' needs	3,560,601	3,175,489
Major gifts pledges receivable for future period use	2,076,000	1,300,004
ADEF education scholarships	1,207,446	1,022,576
Allocation funds	920,352	921,908
Youth ministry	239,853	104,280
Continuing formation fund	229,416	231,966
Project Rachel and Gabriel	218,969	189,809
Diocesan work camp	157,842	152,787
Pope John Paul the Great high school	74,298	97,490
Permanent diaconate	59,307	64,017
Black and Indian mission	52,379	52,379
Campaign for human development	32,421	63,979
Priest retirement home	31,797	85,894
Others	147,247	202,992
Total	<u>\$ 30,161,286</u>	<u>\$ 24,436,272</u>

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**18. 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.

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

	<u>2011</u>	<u>2010</u>
Catholic education	\$ 14,551,573	\$ 14,043,885
Catechetics	2,045,653	2,045,653
Youth ministry	510,988	510,988
ADEF education scholarships	310,500	310,500
Diocesan operations	50,000	-
Original endowment corpus	17,468,714	16,911,026
Endowment major gifts receivable	979,294	1,444,013
Total	<u>\$ 18,448,008</u>	<u>\$ 18,355,039</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



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**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, 2011 and 2010.

**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 8% 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. 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, 2011 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Donor-restricted endowment funds	\$ -	\$7,439,253	\$17,468,714	\$24,907,967
Endowment major gifts receivable	-	-	979,294	979,294
Board-designated endowment funds	8,341,510	-	-	8,341,510
Total funds	<u>\$ 8,341,510</u>	<u>\$7,439,253</u>	<u>\$18,448,008</u>	<u>\$34,228,771</u>

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Endowment net asset composition by type of fund as of June 30, 2010 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Donor-restricted endowment funds	\$ -	\$ 2,755,732	\$ 16,911,026	\$ 19,666,758
Endowment major gifts receivable	-	-	1,444,013	1,444,013
Board-designated endowment funds	6,576,021	-	-	6,576,021
Total funds	<u>\$ 6,576,021</u>	<u>\$ 2,755,732</u>	<u>\$ 18,355,039</u>	<u>\$ 27,686,792</u>

**Donor-restricted endowment**

Changes in donor-restricted endowment net assets as of June 30, 2011 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Endowment net assets, beginning of year	\$ -	\$ 2,755,732	\$ 16,911,026	\$ 19,666,758
Contributions	-	-	557,688	557,688
Investment income	-	341,841	-	341,841
Net appreciation	-	4,826,412	-	4,826,412
Amounts appropriated for expenditure and satisfying purpose restrictions	-	(484,732)	-	(484,732)
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 7,439,253</u>	<u>\$ 17,468,714</u>	<u>\$ 24,907,967</u>

Changes in donor-restricted endowment net assets as of June 30, 2010 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Endowment net assets, beginning of year	\$ -	\$ 1,430,828	\$ 16,156,710	\$ 17,587,538
Contributions	-	-	754,316	754,316
Investment income	-	319,713	-	319,713
Net appreciation	-	1,507,252	-	1,507,252
Net loss on perpetual trusts	-	-	-	-
Amounts appropriated for expenditure and satisfying purpose restrictions	-	(502,061)	-	(502,061)
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 2,755,732</u>	<u>\$ 16,911,026</u>	<u>\$ 19,666,758</u>

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

	<u>Unrestricted</u>	
	<u>2011</u>	<u>2010</u>
Board-designated endowment net assets, beginning of year	\$ 6,576,021	\$ 5,890,646
Investment income	111,250	110,331
Net appreciation (depreciation)	1,654,239	575,044
Board-designated endowment net assets, end of year	<u>\$ 8,341,510</u>	<u>\$ 6,576,021</u>

**19. 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 first \$150,000 of each individual loss and aggregate annual losses of up to 125% of expected claims, or about \$10,600,000 in plan year 2010 -2011, are self-insured. Losses exceeding these amounts are covered by stop-loss insurance policies up to an annual limit on aggregate losses of \$3,000,000. Incurred but not reported health claims are estimated to be \$1,008,000 and \$1,061,000 at June 30, 2011 and 2010, 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 \$150,000 per occurrence with an annual aggregate of \$500,000. The retention amount applies cumulatively to property and liability exposures. The Chancery's estimated exposure for future payments of this layer is \$408,698 and \$290,304 at June 30, 2011 and 2010, 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.

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.

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
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This coverage provided \$5,500,000 in excess of the primary layer of \$1,500,000 of insurance coverage. Currently there are 49 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 3% 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>2011</u>	<u>2010</u>
Incurred but not reported estimated health claims	\$ 1,008,000	\$ 1,061,000
Estimated property and general liability claims	\$ 408,698	\$ 290,304

**20. 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 various office equipment under operating leases expiring through September 2016. Total rent expense, net of sublease rentals for years ended June 30, 2011 and 2010, is as follows:

	<u>2011</u>	<u>2010</u>
Office space	\$ 1,713,209	\$ 1,555,468
Office equipment	102,003	88,665
Sublease office rental (related entities)	(287,058)	(199,261)
Net expense	<u>\$ 1,528,154</u>	<u>\$ 1,444,872</u>

At June 30, 2011, future minimum lease payments are as follows:

	<u>Total Lease</u>	<u>Sublease</u>	<u>Net Lease</u>
2012	\$ 1,789,889	\$ 340,519	\$ 1,449,370
2013	1,842,840	350,735	1,492,105
2014	1,864,479	361,257	1,503,222
2015	1,868,489	372,094	1,496,395
2016	1,921,233	383,257	1,537,976
2017 and thereafter	2,123,844	427,731	1,696,113
Total future minimum lease payments	<u>\$ 11,410,774</u>	<u>\$ 2,235,593</u>	<u>\$ 9,175,181</u>

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Notes to Combined Financial Statements  
For the years ended June 30, 2011 and 2010**

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See also Note 10 for current fiscal year lease payments to 200 North Glebe Road, Inc. and sublease rental income from related parties.

**Lines of credit and letters of credit**

The Chancery has obtained lines of credit as follows:

	<u>June 30, 2011</u>		<u>June 30, 2010</u>	
	<u>Total Available</u>	<u>Outstanding</u>	<u>Total Available</u>	<u>Outstanding</u>
Operating needs	\$ 10,000,000	\$ -	\$ 15,000,000	\$ 7,000,000
Building improvement programs	\$ -	\$ 8,823,419	\$ -	\$ 9,908,259
Standby letters of credit for various construction projects	\$ 15,000,000	\$ 4,328,205	\$ 15,000,000	\$ 3,756,419

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 line of credit for operating needs had a stated rate of interest of the monthly London Interbank Offered Rate (LIBOR) plus 195 basis points for the years ended June 30, 2011 and 2010. The building improvement programs have interest rates ranging from 2.67% to 6.78% for the years ended June 30, 2011 and 2010. 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 for the years ended June 30, 2011 and 2010.

These facilities are subject to annual renewals by our financial institutions.

**Investments**

In connection with a limited partnership subscription agreement, the Chancery is required to make future capital contributions in the amount of \$152,286. The commitment period is 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 2011 and 2010.

## INDEPENDENT AUDITORS' REPORT ON SUPPLEMENTARY COMBINING INFORMATION

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

Our report on our audit of the basic combined financial statements of the Chancery for 2011 and 2010 appears on page 1. That audit was made for the purpose of forming an opinion on the basic combined financial statements taken as a whole. The combining information has been subjected to the auditing procedures applied in the audit of the combined financial statements and, in our opinion is fairly stated in all material respects in relation to the combined financial statements taken as a whole.

*LarsonAllen LLP*  
**LarsonAllen LLP**

St. Cloud, Minnesota  
October 11, 2011

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Combining Statement of Financial Position**  
**As of June 30, 2011**

	<u>Chancery</u>	<u>Rooted in Faith~ Forward in Hope</u>	<u>Elimination Entries</u>	<u>Combined</u>
<b>Assets</b>				
Cash and cash equivalents	\$ 11,117,801	\$ 148,167	\$ -	\$ 11,265,968
Accounts receivable, net	1,365,620	-	-	1,365,620
Accrued interest receivable	117,644	-	-	117,644
Bishop's Lenten Appeal pledges receivable	3,249,308	-	-	3,249,308
Bequests and major gifts pledges receivable, net	3,230,582	-	-	3,230,582
<i>Rooted in Faith - Forward in Hope, Inc.</i>				
pledges receivable, net	-	1,098,347	-	1,098,347
Investments	134,642,953	-	-	134,642,953
Prepaid expenses and other assets	1,424,730	-	-	1,424,730
Unamortized bond costs	375,265	-	-	375,265
Demand notes and loans receivable				
Paul VI High School bond receivable	4,209,917	-	-	4,209,917
Pope John Paul the Great High School receivable	6,358,523	-	-	6,358,523
Diocesan Investment and Loan (DIAL) program	-	-	-	-
200 North Glebe Road, Inc.	4,834,286	-	-	4,834,286
Property, equipment and land, net	112,761,803	-	-	112,761,803
Construction in progress and assets not yet placed in service	-	-	-	-
Land restricted for high school	14,500,000	-	-	14,500,000
Total assets	<u>\$ 298,188,432</u>	<u>\$ 1,246,514</u>	<u>\$ -</u>	<u>\$ 299,434,946</u>
<b>Liabilities and Net Assets</b>				
<b>Liabilities</b>				
Deposits held in custody for others	\$ 2,253,477	\$ -	\$ -	\$ 2,253,477
Accounts payable and accrued expenses	4,007,816	-	-	4,007,816
Accrued interest payable	308,405	-	-	308,405
Unearned revenue	923,916	-	-	923,916
DIAL deposits payable	-	-	-	-
Notes payable, net of discount	-	-	-	-
Amounts held on behalf of other diocesan entities	59,193,249	307,972	-	59,501,221
Annuity payment liability	209,112	-	-	209,112
ADEF funds held for schools	2,515,401	-	-	2,515,401
Accrued pension liability, priests	4,305,868	-	-	4,305,868
Postretirement health benefit obligation	6,227,915	-	-	6,227,915
Line of credit payable	-	-	-	-
Bonds payable	23,205,000	-	-	23,205,000
Total liabilities	<u>103,150,159</u>	<u>307,972</u>	<u>-</u>	<u>103,458,131</u>
<b>Net assets</b>				
<b>Unrestricted</b>				
Current operations	35,597,754	-	-	35,597,754
Invested in property, equipment and land	94,100,799	-	-	94,100,799
Functioning as endowment	8,341,510	-	-	8,341,510
Designated	9,327,458	-	-	9,327,458
Total unrestricted	147,367,521	-	-	147,367,521
Temporarily restricted	29,229,071	932,215	-	30,161,286
Permanently restricted	18,441,681	6,327	-	18,448,008
Total net assets	<u>195,038,273</u>	<u>938,542</u>	<u>-</u>	<u>195,976,815</u>
Total liabilities and net assets	<u>\$ 298,188,432</u>	<u>\$ 1,246,514</u>	<u>\$ -</u>	<u>\$ 299,434,946</u>

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate**  
**Combining Statement of Financial Position**  
**As of June 30, 2010**

	<u>Chancery</u>	<u>Rooted in Faith~ Forward in Hope</u>	<u>Elimination Entries</u>	<u>Combined</u>
<b>Assets</b>				
Cash and cash equivalents	\$ 19,617,605	\$ 185,662	\$ -	\$ 19,803,267
Accounts receivable, net	945,354	169	-	945,523
Accrued interest receivable	108,875	242	-	109,117
Bishop's Lenten Appeal pledges receivable	2,678,281	-	-	2,678,281
Bequests and major gifts pledges receivable, net	3,002,209	-	-	3,002,209
<i>Rooted in Faith - Forward in Hope, Inc.</i>				
pledges receivable, net	-	1,660,000	-	1,660,000
Investments	104,587,523	318	-	104,587,841
Prepaid expenses and other assets	524,643	-	-	524,643
Unamortized bond costs	392,005	-	-	392,005
Demand notes and loans receivable				
Paul VI High School bond receivable	4,309,917	-	-	4,309,917
Pope John Paul the Great High School receivable	3,912,695	-	-	3,912,695
Diocesan Investment and Loan (DIAL) program	49,653,316	-	-	49,653,316
200 North Glebe Road, Inc.	4,884,286	-	-	4,884,286
Property, equipment and land, net	109,801,711	-	-	109,801,711
Construction in progress and assets not yet placed in service	6,502,811	-	-	6,502,811
Land restricted for high school	14,500,000	-	-	14,500,000
Total assets	<u>\$ 325,421,231</u>	<u>\$ 1,846,391</u>	<u>\$ -</u>	<u>\$ 327,267,622</u>
<b>Liabilities and Net Assets</b>				
<b>Liabilities</b>				
Deposits held in custody for others	\$ 1,651,558	\$ -	\$ -	\$ 1,651,558
Accounts payable and accrued expenses	4,276,227	-	-	4,276,227
Accrued interest payable	314,256	-	-	314,256
Unearned revenue	194,045	-	-	194,045
DIAL deposits payable	98,694,502	-	-	98,694,502
Notes payable, net of discount	677,918	-	-	677,918
Amounts due parishes and Catholic Charities	9,460,479	660,293	-	10,120,772
Annuity payment liability	131,588	-	-	131,588
ADEF funds held for schools	2,276,713	-	-	2,276,713
Accrued pension liability, priests	5,437,213	-	-	5,437,213
Postretirement health benefit obligation	6,523,719	-	-	6,523,719
Line of credit payable	7,000,000	-	-	7,000,000
Bonds payable	23,740,000	-	-	23,740,000
Total liabilities	<u>160,378,218</u>	<u>660,293</u>	<u>-</u>	<u>161,038,511</u>
<b>Net assets</b>				
<b>Unrestricted</b>				
Current operations	12,000,987	-	-	12,000,987
Invested in property, equipment and land	96,826,489	-	-	96,826,489
Functioning as endowment	6,576,021	-	-	6,576,021
Designated	8,034,303	-	-	8,034,303
Total unrestricted	<u>123,437,800</u>	<u>-</u>	<u>-</u>	<u>123,437,800</u>
Temporarily restricted	23,342,501	1,093,771	-	24,436,272
Permanently restricted	18,262,712	92,327	-	18,355,039
Total net assets	<u>165,043,013</u>	<u>1,186,098</u>	<u>-</u>	<u>166,229,111</u>
Total liabilities and net assets	<u>\$ 325,421,231</u>	<u>\$ 1,846,391</u>	<u>\$ -</u>	<u>\$ 327,267,622</u>



**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Combining Statement of Activities  
For the year ended June 30, 2011**

	<u>Chancery</u>	<u>Rooted in Faith- Forward in Hope</u>	<u>Elimination Entries</u>	<u>Combined</u>
<b>Unrestricted</b>				
Operating revenues and support				
Bishop's Lenten Appeal	\$ 13,963,177	\$ -	\$ -	\$ 13,963,177
Operational assessment	6,699,824	-	-	6,699,824
Investment income for operations	1,400,000	-	-	1,400,000
Transmittal fees	144,649	-	-	144,649
Contributions, bequests and major gifts	4,322,288	-	-	4,322,288
Program revenue	1,744,553	-	-	1,744,553
Diocesan subsidy	-	73,655	(73,655)	-
Other revenue and support	10,072	-	-	10,072
Satisfaction of temporary restrictions	4,862,974	-	-	4,862,974
Total operating revenues and support	<u>33,147,537</u>	<u>73,655</u>	<u>(73,655)</u>	<u>33,147,537</u>
Operating expenses				
Program services				
Pastoral	6,479,230	79,000	(79,000)	6,479,230
Religious personnel development	2,792,594	-	-	2,792,594
Education	5,333,465	81,000	(81,000)	5,333,465
Social services	2,339,779	9,299	-	2,349,078
Supporting services				
Diocesan administration and parochial support	10,862,196	-	-	10,862,196
<i>Rooted in Faith - Forward in Hope, Inc.</i>	73,655	73,655	(73,655)	73,655
Bishop's Lenten Appeal	565,317	-	-	565,317
Total operating expenses	<u>28,446,236</u>	<u>242,954</u>	<u>(233,655)</u>	<u>28,455,535</u>
Change in net assets from operations	<u>4,701,301</u>	<u>(169,299)</u>	<u>160,000</u>	<u>4,692,002</u>
Other changes in net assets				
Investment income, less amount included in operations, net	15,762,396	-	-	15,762,396
Bond interest expense	(1,004,977)	-	-	(1,004,977)
Insurance programs	2,534,237	-	-	2,534,237
Change in unfunded pension liability, priests	1,131,345	-	-	1,131,345
Change in unfunded postretirement health obligation	295,804	-	-	295,804
Net property gains	3,006,541	-	-	3,006,541
Rental income - diocesan properties	1,578,699	-	-	1,578,699
Related parties contributions	(4,217,316)	-	-	(4,217,316)
DIAL loan interest income	2,156,129	-	-	2,156,129
DIAL deposit interest expense	(2,202,279)	-	-	(2,202,279)
Satisfaction of temporary restrictions	187,841	169,299	(160,000)	197,140
Total other changes in net assets	<u>19,228,420</u>	<u>169,299</u>	<u>(160,000)</u>	<u>19,237,719</u>
Change in unrestricted net assets	23,929,721	-	-	23,929,721
Unrestricted net assets, beginning of year	<u>123,437,800</u>	<u>-</u>	<u>-</u>	<u>123,437,800</u>
Unrestricted net assets, end of year	<u>\$ 147,367,521</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 147,367,521</u>

*Continued*

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Combining Statement of Activities  
For the year ended June 30, 2011**

	<u>Chancery</u>	<u>Rooted in Faith- Forward in Hope</u>	<u>Elimination Entries</u>	<u>Combined</u>
<b>Temporarily restricted</b>				
Operating revenues and support				
Contributions, bequests and major gifts	\$ 5,585,100	\$ -	\$ (160,000)	\$ 5,425,100
Satisfaction of temporary restrictions	<u>(4,862,974)</u>	<u>-</u>	<u>-</u>	<u>(4,862,974)</u>
Total operating revenues and support	<u>722,126</u>	<u>-</u>	<u>(160,000)</u>	<u>562,126</u>
Operating expenses				
Total operating expenses	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Change in net assets from operations	<u>722,126</u>	<u>-</u>	<u>(160,000)</u>	<u>562,126</u>
Other changes in net assets				
Investment income, net	5,352,285	567	-	5,352,852
<i>Rooted in Faith - Forward in Hope, Inc.</i>				
contributions, net of bad debt losses	-	7,176	-	7,176
Satisfaction of temporary restrictions	<u>(187,841)</u>	<u>(169,299)</u>	<u>160,000</u>	<u>(197,140)</u>
Total other changes in net assets	<u>5,164,444</u>	<u>(161,556)</u>	<u>160,000</u>	<u>5,162,888</u>
Change in temporarily restricted net assets	5,886,570	(161,556)	-	5,725,014
Temporarily restricted net assets, beginning of year	23,342,501	1,093,771	-	24,436,272
Temporarily restricted net assets, end of year	<u>\$ 29,229,071</u>	<u>\$ 932,215</u>	<u>\$ -</u>	<u>\$ 30,161,286</u>
<b>Permanently restricted</b>				
Contributions, bequests and major gifts	\$ 92,969	\$ -	\$ -	\$ 92,969
Transfers of endowment	<u>86,000</u>	<u>(86,000)</u>	<u>-</u>	<u>-</u>
Total operating revenues and support	<u>178,969</u>	<u>(86,000)</u>	<u>-</u>	<u>92,969</u>
Change in permanently restricted net assets	178,969	(86,000)	-	92,969
Permanently restricted net assets, beginning of year	18,262,712	92,327	-	18,355,039
Permanently restricted net assets, end of year	<u>\$ 18,441,681</u>	<u>\$ 6,327</u>	<u>\$ -</u>	<u>\$ 18,448,008</u>
Total change in net assets	29,995,260	(247,556)	-	29,747,704
Net assets, beginning of year	165,043,013	1,186,098	-	166,229,111
Net assets, end of year	<u>\$ 195,038,273</u>	<u>\$ 938,542</u>	<u>\$ -</u>	<u>\$ 195,976,815</u>

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Combining Statement of Activities  
For the year ended June 30, 2010**

	<u>Chancery</u>	<u>Rooted in Faith- Forward in Hope</u>	<u>Elimination Entries</u>	<u>Combined</u>
<b>Unrestricted</b>				
Operating revenues and support				
Bishop's Lenten Appeal	\$ 12,538,426	\$ -	\$ -	\$ 12,538,426
Operational assessment	6,682,150	-	-	6,682,150
Investment income for operations	1,650,000	-	-	1,650,000
Transmittal fees	140,235	-	-	140,235
Contributions, bequests and major gifts	781,032	-	-	781,032
Program revenue	1,832,454	-	-	1,832,454
Diocesan subsidy	-	72,036	(72,036)	-
Other revenue and support	52,442	-	-	52,442
Satisfaction of temporary restrictions	4,508,442	2,094,600	(2,094,600)	4,508,442
Total operating revenues and support	<u>28,185,181</u>	<u>2,166,636</u>	<u>(2,166,636)</u>	<u>28,185,181</u>
Operating expenses				
Program services				
Pastoral	5,361,486	571,700	(571,700)	5,361,486
Religious personnel development	2,552,151	440,400	(440,400)	2,552,151
Education	5,188,200	1,082,500	(1,082,500)	5,188,200
Social services	2,277,231	-	-	2,277,231
Refugee assistance	543,977	-	-	543,977
Supporting services				
Diocesan administration and parochial support	10,417,106	-	-	10,417,106
<i>Rooted in Faith - Forward in Hope, Inc.</i>	72,036	72,036	(72,036)	72,036
Bishop's Lenten Appeal	618,561	-	-	618,561
Total operating expenses	<u>27,030,748</u>	<u>2,166,636</u>	<u>(2,166,636)</u>	<u>27,030,748</u>
Change in net assets from operations	<u>1,154,433</u>	<u>-</u>	<u>-</u>	<u>1,154,433</u>
Other changes in net assets				
Investment income, less amount included in operations, net	4,513,109	-	-	4,513,109
Bond interest expense	(1,023,953)	-	-	(1,023,953)
Insurance programs	2,435,793	-	-	2,435,793
Change in unfunded pension liability, priests	(1,835,387)	-	-	(1,835,387)
Change in unfunded postretirement health obligation	(1,939,012)	-	-	(1,939,012)
Net property gains	-	-	-	-
Rental income - diocesan properties	1,535,671	-	-	1,535,671
DIAL loan interest income	2,413,302	-	-	2,413,302
DIAL deposit interest expense	(2,678,597)	-	-	(2,678,597)
Satisfaction of temporary restrictions	6,108,853	-	-	6,108,853
Total other changes in net assets	<u>9,529,779</u>	<u>-</u>	<u>-</u>	<u>9,529,779</u>
Change in unrestricted net assets	10,684,212	-	-	10,684,212
Unrestricted net assets, beginning of year	112,753,588	-	-	112,753,588
Unrestricted net assets, end of year	<u>\$ 123,437,800</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 123,437,800</u>

*Continued*

**Central Administrative Office of the Catholic Diocese of Arlington and Affiliate  
Combining Statement of Activities  
For the year ended June 30, 2010**

	<u>Chancery</u>	<u>Rooted in Faith- Forward in Hope</u>	<u>Elimination Entries</u>	<u>Combined</u>
<b>Temporarily restricted</b>				
Operating revenues and support				
Contributions, bequests and major gifts	\$ 6,098,409	\$ -	\$ (2,094,600)	\$ 4,003,809
Refugee assistance	543,977	-	-	543,977
Satisfaction of temporary restrictions	<u>(4,508,442)</u>	<u>-</u>	<u>-</u>	<u>(4,508,442)</u>
Total operating revenues and support	<u>2,133,944</u>	<u>-</u>	<u>(2,094,600)</u>	<u>39,344</u>
Operating expenses				
Total operating expenses	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Change in net assets from operations	<u>2,133,944</u>	<u>-</u>	<u>(2,094,600)</u>	<u>39,344</u>
Other changes in net assets				
Investment income, net	1,990,897	6,505	-	1,997,402
<i>Rooted in Faith - Forward in Hope, Inc.</i> contributions, net of bad debt losses	-	(1,284,259)	-	(1,284,259)
Satisfaction of temporary restrictions	<u>(6,108,853)</u>	<u>(2,094,600)</u>	<u>2,094,600</u>	<u>(6,108,853)</u>
Total other changes in net assets	<u>(4,117,956)</u>	<u>(3,372,354)</u>	<u>2,094,600</u>	<u>(5,395,710)</u>
Change in temporarily restricted net assets	(1,984,012)	(3,372,354)	-	(5,356,366)
Temporarily restricted net assets, beginning of year	<u>25,326,513</u>	<u>4,466,125</u>	<u>-</u>	<u>29,792,638</u>
Temporarily restricted net assets, end of year	<u>\$ 23,342,501</u>	<u>\$ 1,093,771</u>	<u>\$ -</u>	<u>\$ 24,436,272</u>
<b>Permanently restricted</b>				
Contributions, bequests and major gifts	\$ 334,473	\$ -	\$ -	\$ 334,473
Transfers of endowment	<u>1,194,700</u>	<u>(1,194,700)</u>	<u>-</u>	<u>-</u>
Total operating revenues and support	<u>1,529,173</u>	<u>(1,194,700)</u>	<u>-</u>	<u>334,473</u>
Change in permanently restricted net assets	1,529,173	(1,194,700)	-	334,473
Permanently restricted net assets, beginning of year	<u>16,733,539</u>	<u>1,287,027</u>	<u>-</u>	<u>18,020,566</u>
Permanently restricted net assets, end of year	<u>\$ 18,262,712</u>	<u>\$ 92,327</u>	<u>\$ -</u>	<u>\$ 18,355,039</u>
Total change in net assets	10,229,373	(4,567,054)	-	5,662,319
Net assets, beginning of year	<u>154,813,640</u>	<u>5,753,152</u>	<u>-</u>	<u>160,566,792</u>
Net assets, end of year	<u>\$ 165,043,013</u>	<u>\$ 1,186,098</u>	<u>\$ -</u>	<u>\$ 166,229,111</u>