

**EPISCOPAL DIOCESE OF ROCHESTER**

**ROCHESTER, NEW YORK**

**AUDITED FINANCIAL STATEMENTS**

**AND**

**INDEPENDENT AUDITOR'S REPORT**

**DECEMBER 31, 2017**

**(With Comparative Totals for 2016)**



MENGEL METZGER BARR & CO. LLP

Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT

To the Diocesan Trustees of the  
Episcopal Diocese of Rochester

**Report on the Financial Statements**

We have audited the accompanying financial statements of the Episcopal Diocese of Rochester (the "Diocese"), which comprise the statement of financial position as of December 31, 2017, and the related statements of activities and change in net assets and cash flows for the year then ended, and the related notes to the financial statements.

**Management's Responsibility for the Financial Statements**

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

**Auditor's Responsibility**

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

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

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

**Basis for Qualified Opinion**

The Diocese has not adopted the accounting or disclosure requirements for donor restricted gifts including endowments. In our opinion, all donor restricted gifts should be accounted for as temporarily or permanently restricted to conform with accounting principles generally accepted in the United States of America. The effects of these departures from accounting principles generally accepted in the United States of America on the accompanying financial statements could not be determined. In 2017 and 2016, the Diocese has also excluded a liability regarding their retiree health reimbursement account plan (HRA), (Note I, page 20). In our opinion, the total liability related to the plan should be recorded. If this liability was recorded, total liabilities would have increased between \$522,393 to \$786,386 as of December 31, 2017 and 2016. Net assets as of December 31, 2017 and 2016 would have decreased by the same amount.

**Qualified Opinion**

In our opinion, except for the effects on the financial statements relating to the matters discussed in the Basis for Qualified Opinion paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of Episcopal Diocese of Rochester as of December 31, 2017, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

**Other Matter**

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The other financial information (page 22), for the year ended December 31, 2017, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, except for the effects on the other financial information as explained in the Basis for Qualified Opinion paragraph of this report, the information is fairly stated in all material respects in relation to the financial statements as a whole. The information marked “unaudited” has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

**Report on Summarized Comparative Information**

We have previously audited Episcopal Diocese of Rochester’s December 31, 2016 financial statements, and we expressed a qualified opinion on those audited financial statements in our report dated July 25, 2017. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2016 is consistent, in all material respects, with the audited financial statements from which it has been derived.

*Mengel, Metzger, Baw & Co. LLP*

Rochester, New York  
August 6, 2018

EPISCOPAL DIOCESE OF ROCHESTER  
STATEMENT OF FINANCIAL POSITION  
DECEMBER 31, 2017  
(With Comparative Totals for 2016)

	Unrestricted				Restricted			December 31,	
	Operating	Special Purpose	Real Estate	Total	Endowment	By		2017 Total All Funds	2016 Total All Funds
						Donors	Total		
<u>ASSETS</u>									
Cash and cash equivalents	\$ 228,673	\$ 1,006,723	\$ -	\$ 1,235,396	\$ -	\$ 11,630	\$ 11,630	\$ 1,247,026	\$ 379,339
Mortgage and loans receivable, net	-	1,388,506	-	1,388,506	-	582,565	582,565	1,971,071	2,226,660
Prepays and other assets	70,069	-	-	70,069	-	-	-	70,069	64,644
Investments	-	13,843,208	-	13,843,208	3,947,266	2,726,781	6,674,047	20,517,255	17,936,107
Due from (to) other funds	554,090	137,916	-	692,006	-	(692,006)	(692,006)	-	-
Land, buildings and equipment, net	-	-	174,569	174,569	-	-	-	174,569	592,256
TOTAL ASSETS	<u>\$ 852,832</u>	<u>\$ 16,376,353</u>	<u>\$ 174,569</u>	<u>\$ 17,403,754</u>	<u>\$ 3,947,266</u>	<u>\$ 2,628,970</u>	<u>\$ 6,576,236</u>	<u>\$ 23,979,990</u>	<u>\$ 21,199,006</u>
<u>LIABILITIES AND NET ASSETS</u>									
<u>LIABILITIES</u>									
Accounts payable	\$ 7,950	\$ -	\$ -	\$ 7,950	\$ -	\$ -	\$ -	\$ 7,950	\$ 17,504
Accrued liabilities and other	48,222	-	-	48,222	-	834	834	49,056	28,231
TOTAL LIABILITIES	<u>56,172</u>	<u>-</u>	<u>-</u>	<u>56,172</u>	<u>-</u>	<u>834</u>	<u>834</u>	<u>57,006</u>	<u>45,735</u>
<u>NET ASSETS</u>									
Unrestricted	796,660	16,376,353	174,569	17,347,582	-	-	-	17,347,582	15,365,918
Restricted	-	-	-	-	3,947,266	2,628,136	6,575,402	6,575,402	5,787,353
TOTAL NET ASSETS	<u>796,660</u>	<u>16,376,353</u>	<u>174,569</u>	<u>17,347,582</u>	<u>3,947,266</u>	<u>2,628,136</u>	<u>6,575,402</u>	<u>23,922,984</u>	<u>21,153,271</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 852,832</u>	<u>\$ 16,376,353</u>	<u>\$ 174,569</u>	<u>\$ 17,403,754</u>	<u>\$ 3,947,266</u>	<u>\$ 2,628,970</u>	<u>\$ 6,576,236</u>	<u>\$ 23,979,990</u>	<u>\$ 21,199,006</u>

The accompanying notes are an integral part of the financial statements

EPISCOPAL DIOCESE OF ROCHESTER

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

FOR THE YEAR ENDED DECEMBER 31, 2017

(With Comparative Totals for 2016)

	Unrestricted				Restricted			December 31,	
	Operating	Special Purpose	Real Estate	Total	Endowment	By Donors	Total	2017	2016
								Total All Funds	Total All Funds
<b>REVENUE</b>									
Parish Support	\$ 972,304	\$ -	\$ -	\$ 972,304	\$ -	\$ -	\$ -	\$ 972,304	\$ 973,288
Interest on mortgages and loans	58,094	-	-	58,094	-	-	-	58,094	62,901
Other	125	-	-	125	-	-	-	125	3,000
<b>TOTAL REVENUE</b>	<b>1,030,523</b>	<b>-</b>	<b>-</b>	<b>1,030,523</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>1,030,523</b>	<b>1,039,189</b>
<b>EXPENSES</b>									
Mission outside the Diocese	238,000	-	-	238,000	-	-	-	238,000	227,750
Mission within the Diocese	215,531	-	-	215,531	-	-	-	215,531	216,925
Congregational development	289,098	-	-	289,098	-	-	-	289,098	288,976
Leadership development	116,050	-	-	116,050	-	-	-	116,050	80,584
Governance, committees and missionaries	77,125	-	-	77,125	-	-	-	77,125	100,796
Executive staff	497,737	-	-	497,737	-	-	-	497,737	414,682
Support staff	391,344	-	-	391,344	-	-	-	391,344	401,038
Office Expense	127,820	-	-	127,820	-	-	-	127,820	108,178
Clergy and lay benefits	63,969	-	-	63,969	-	-	-	63,969	76,040
Distributions to beneficiaries	-	-	-	-	-	21,290	21,290	21,290	54,637
Depreciation	-	-	3,486	3,486	-	-	-	3,486	22,879
	<u>2,016,674</u>	<u>-</u>	<u>3,486</u>	<u>2,020,160</u>	<u>-</u>	<u>21,290</u>	<u>21,290</u>	<u>2,041,450</u>	<u>1,992,485</u>
<b>EXPENSES IN EXCESS OF REVENUE</b>	<b>(986,151)</b>	<b>-</b>	<b>(3,486)</b>	<b>(989,637)</b>	<b>-</b>	<b>(21,290)</b>	<b>(21,290)</b>	<b>(1,010,927)</b>	<b>(953,296)</b>
Gain on disposal of assets	-	-	768,817	768,817	-	-	-	768,817	-
Transfer of property	-	-	-	-	-	-	-	-	44,608
Non-operating income	3,449	-	-	3,449	-	-	-	3,449	20,078
Investment income, net	-	1,991,085	-	1,991,085	569,993	447,296	1,017,289	3,008,374	1,274,325
<b>CHANGE IN NET ASSETS</b>	<b>(982,702)</b>	<b>1,991,085</b>	<b>765,331</b>	<b>1,773,714</b>	<b>569,993</b>	<b>426,006</b>	<b>995,999</b>	<b>2,769,713</b>	<b>385,715</b>
Net assets at beginning of year	941,394	13,832,268	592,256	15,365,918	3,550,573	2,236,780	5,787,353	21,153,271	20,767,556
Spending policy transfer	904,800	(695,000)	-	209,800	(173,300)	(36,500)	(209,800)	-	-
Inter-fund transfers	(66,832)	1,248,000	(1,183,018)	(1,850)	-	1,850	1,850	-	-
<b>NET ASSETS AT END OF YEAR</b>	<b>\$ 796,660</b>	<b>\$ 16,376,353</b>	<b>\$ 174,569</b>	<b>\$ 17,347,582</b>	<b>\$ 3,947,266</b>	<b>\$ 2,628,136</b>	<b>\$ 6,575,402</b>	<b>\$ 23,922,984</b>	<b>\$ 21,153,271</b>

The accompanying notes are an integral part of the financial statements

EPISCOPAL DIOCESE OF ROCHESTER

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED DECEMBER 31, 2017

(With Comparative Totals for 2016)

	Unrestricted				Restricted			December 31,	
	Operating	Special Purpose	Real Estate	Total	Endowment	By Donors	Total	2017	2016
								Total All Funds	Total All Funds
<b><u>CASH FLOWS - OPERATING ACTIVITIES</u></b>									
Change in net assets	\$ (982,702)	\$ 1,991,085	\$ 765,331	\$ 1,773,714	\$ 569,993	\$ 426,006	\$ 995,999	\$ 2,769,713	\$ 385,715
Adjustments to reconcile change in net assets to net cash (used for) provided from operating activities:									
Depreciation	-	-	3,486	3,486	-	-	-	3,486	22,879
Realized and unrealized gain on investments, net	-	(1,991,085)	-	(1,991,085)	(569,993)	(447,296)	(1,017,289)	(3,008,374)	(1,274,325)
Gain on disposal of assets	-	-	(768,817)	(768,817)	-	-	-	(768,817)	-
Transfer of property	-	-	-	-	-	-	-	-	(44,608)
Changes in certain assets and liabilities affecting operations:									
Due to (from) other funds	-	54,030	-	54,030	-	(54,030)	(54,030)	-	-
Prepays and other assets	(5,425)	-	-	(5,425)	-	-	-	(5,425)	(11,316)
Accounts payable	(9,554)	-	-	(9,554)	-	-	-	(9,554)	51
Accrued liabilities	20,825	-	-	20,825	-	-	-	20,825	27,397
NET CASH (USED FOR) PROVIDED FROM OPERATING ACTIVITIES	(976,856)	54,030	-	(922,826)	-	(75,320)	(75,320)	(998,146)	(894,207)
<b><u>CASH FLOWS - INVESTING ACTIVITIES</u></b>									
Changes in mortgages and loans receivable, net	-	201,558	-	201,558	-	54,031	54,031	255,589	195,037
Sales of investments	-	721,946	-	721,946	173,300	159,419	332,719	1,054,665	1,039,712
Purchase of investments	-	(523,811)	-	(523,811)	-	(103,628)	(103,628)	(627,439)	(222,245)
Purchases of buildings and equipment	-	-	-	-	-	-	-	-	(5,056)
Proceeds from the sale of buildings and equipment	-	-	1,183,018	1,183,018	-	-	-	1,183,018	-
Spending policy transfer	904,800	(695,000)	-	209,800	(173,300)	(36,500)	(209,800)	-	-
Inter-fund transfer	(66,832)	1,248,000	(1,183,018)	(1,850)	-	1,850	1,850	-	-
NET CASH PROVIDED FROM INVESTING ACTIVITIES	837,968	952,693	-	1,790,661	-	75,172	75,172	1,865,833	1,007,448
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(138,888)	1,006,723	-	867,835	-	(148)	(148)	867,687	113,241
Cash and cash equivalents at beginning of year	367,561	-	-	367,561	-	11,778	11,778	379,339	266,098
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ 228,673	\$ 1,006,723	\$ -	\$ 1,235,396	\$ -	\$ 11,630	\$ 11,630	\$ 1,247,026	\$ 379,339

The accompanying notes are an integral part of the financial statements

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE A: THE DIOCESE AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Diocese

The Episcopal Diocese of Rochester (the “Diocese”) was formed in December 1931. It stretches from Lake Ontario south to Pennsylvania, its east and west borders are formed by the Diocese of Central New York and the Diocese of Western New York. The Diocese comprises Episcopal congregations throughout eight counties in the State of New York. These are Steuben, Allegany, Schuyler, Yates, Livingston, Ontario, Wayne and Monroe Counties. It includes 45 active congregations and several summer and institutional chapels.

The vision and mission of the Diocese are described as follows:

- Vision – “Joy in Christ, as a way of life”
- Mission – “Grow and develop congregations spiritually, numerically and in missional leadership”

The Diocese is rich in material and spiritual resources and in people able and willing to use them.

Basis of accounting

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"), except for the items noted below:

	<u>Generally Accepted Accounting Principles</u>	<u>Diocese Accounting Principles</u>
Donor restricted contributions	Donor restricted contributions are to be recorded as temporarily or permanently restricted at the time of donation. Net assets are released from restriction when the donor restriction is satisfied.	Use of Fund Accounting
Endowments	The composition of, and activity related to, endowment funds are required to be disclosed, as well as the related spending policy, investment return objectives and other information related to managing the endowment.	Disclosure is omitted
Health Reimbursement Accounts	See Note I	



EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE A: THE DIOCESE AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Cont'd

The Diocese has not adopted financial reporting practices to reflect the classification of its net assets and activities as unrestricted, temporarily restricted or permanently restricted in conformity with GAAP. Rather, it uses the principles of fund accounting consistent with its historical practice. In addition, the financial statements do not include a disclosure providing the composition of, and activity related to endowment funds, as well as the related spending policy, investment return objectives and other information related to managing the endowment which are required by GAAP. The effects of these departures from GAAP in the accompanying financial statements could not be determined.

Financial statement presentation

The assets, liabilities, and net assets of the Diocese are classified as follows:

Unrestricted: Represents net assets available for use without any donor-imposed restrictions. The following unrestricted funds are maintained by the Diocese:

Operating: This fund is used to account for all resources which are intended for current operating activities. In addition, a significant portion of the income from investments held in other funds is transferred to the operating fund to support operations.

Special Purpose: This fund includes the General Endowment investments and Housing Loan Fund.

Real Estate: This fund includes the Diocese's net investment in land, buildings and equipment.

Restricted: Represents net assets that have donor-imposed restrictions that require the Diocese to treat the donated asset as specified. The following restricted funds are maintained by the Diocese:

Endowment: This fund consists of permanent endowments contributed to the Diocese, the earnings from which are available to support operating activities.

By Donors: This fund consists of amounts that are restricted by the donor for a specified purpose, as well as amounts belonging to parishes in the Diocese deposited with the Diocese for investment management purposes

Cash and cash equivalents

Cash balances are maintained at various financial institutions located in Upstate New York and are insured by the FDIC up to \$250,000 at each institution. In the normal course of business, the cash account balances at any given time may exceed insured limits. However, the Diocese has not experienced any losses in such accounts and does not believe it is exposed to significant risk in cash. Cash equivalents include money market accounts and certificates of deposit which have maturity dates of 12 months or less.

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE A: THE DIOCESE AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Cont'd

Mortgages and loans receivable

Mortgages and loans receivable represent amounts due to the Diocese under loan agreements with parishes, clergy and buyers of closed church properties. Loans are stated at unpaid principal balances, less an allowance for loan losses. The Diocese periodically evaluates the loan for collectability based on inherent collection risks and adverse situations that may affect the borrower's ability to repay. Loans for which no contractual payments have been received for a period of time are considered delinquent. After all collection efforts are exhausted, any amounts deemed uncollectible based upon an assessment of the debtor's financial condition are written off. The Diocese believes that no allowance for loan loss is necessary at December 31, 2017 and 2016.

Loans are placed on nonaccrual status when management believes collection of interest is doubtful. As of December 31, 2017 and 2016, the Diocese did not have any loans on nonaccrual status.

Investments

Investments are stated at fair value. The fair value of all debt and equity securities with readily determinable fair values are based on quotations obtained from national security agencies. The alternative investments, which are not readily marketable, are carried at estimated fair values as provided by the investment managers. The Diocese reviews and evaluates the values provided by the investment managers and agrees with the valuation methods and assumptions used in determining the fair value of the alternative investments. Those estimated fair values may differ significantly from the values that would have been used had a market for these securities existed. Due to the risk associated with certain investment securities, it is at least reasonably possible that changes in the fair value of investment securities will occur in the near-term and that such changes could materially affect the amounts reported in the accompanying financial statements.

Land, buildings and equipment

Land, buildings and equipment of the Diocese are stated at cost. However, missions (parish churches, which are not self-supporting) and other properties which were reverted back to the Diocese are recorded at the appraised value or estimated fair value at the time the Diocese obtained possession of the property. Effective January 2017, the Diocese changed their policy from capitalizing property and equipment in excess of \$1,000, which have a useful life of greater than three years, to capitalizing property and equipment in excess of \$2,500, which have a useful life of greater than three years. Depreciation expense is computed using the straight-line method over the estimated useful lives of the related assets, which are as follows:

Buildings and building improvements	40 Years
Equipment	3-10 Years

Tax exempt status

The Diocese is a not-for-profit corporation and is exempt from income taxes as a religious organization. The Diocese has also been classified by the Internal Revenue Service as an entity that is not a private foundation.

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE A: THE ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Cont'd

Revenue

The Diocese recognizes revenue when it is realized or realizable and has been earned. Investment gain (loss) includes interest and dividends earned during the period as well as realized and unrealized gains and losses on investment, net of investment expense.

Use of estimates

The preparation of financial statements 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 revenue and expenses during the reporting period. Accordingly, actual results could differ from these estimates.

Comparative totals as of December 31, 2016

The accompanying financial statements include certain prior year summarized comparative information in total, but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with The Diocese's financial statements that the year ended December 31, 2016, from which the summarized information was derived.

Reclassifications

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

Subsequent events

The Diocese has conducted an evaluation of potential subsequent events occurring after the statement of financial position date through August 6, 2018, which is the date the financial statements are available to be issued. No subsequent events requiring disclosure, other than those in Notes B, C and G, were noted.

NOTE B: MORTGAGES AND LOANS RECEIVABLE

Mortgages and loans receivable consisted of the following:

	<u>December 31,</u>	
	<u>2017</u>	<u>2016</u>
<u>Unrestricted</u>		
Clergy housing loan fund	\$ 167,943	\$ 264,916
Community development loans	<u>1,220,563</u>	<u>1,325,148</u>
	1,388,506	1,590,064
<u>Restricted</u>		
Sibley revolving loan fund	<u>582,565</u>	<u>636,596</u>
	<u>\$ 1,971,071</u>	<u>\$ 2,226,660</u>

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE B: MORTGAGES AND LOANS RECEIVABLE, Cont'd

Mortgages and loans receivable bear interest at rates ranging from 2.5% to 5.0% and mature at various dates through January 2042. Approximately \$636,000 and \$788,000 of the balance of the receivables outstanding at December 31, 2017 and 2016, respectively, are secured by first and second mortgages. All remaining amounts outstanding are unsecured.

Effective February 2018, The Trustees of the Diocese authorized an early payment discount on the Community Development Loans (CDL) of up to 35% (to be calculated with a discount rate of 9% over the remaining term of the loan). This early payment discount is offered to the nine parishes with CDL loans if they wish to partially or fully pay-off these low interest loans by December 31, 2018. Since authorization, eight of the parishes have paid their discounted loan in full or made partial payments, totaling approximately \$290,000 with a related discount of approximately \$145,000.

Interest on mortgages and loans is recognized over the term of the mortgage or loan and is calculated using the simple-interest method on principal amounts outstanding.

Principal payments due to be received on mortgages and loans receivable are as follows, before discount program:

<u>For the year ended December 31,</u>	<u>Amount</u>
2018	\$ 154,771
2019	147,124
2020	149,970
2021	152,639
2022	155,249
Thereafter	<u>1,211,318</u>
	<u>\$ 1,971,071</u>

NOTE C: INVESTMENTS

Prior to January 2014, the Diocese served as the intermediary custodian of funds held for the benefit of certain congregations and other organizations. As intermediary custodian, the Diocese served as a fiscal intermediary for the parishes to administratively transact their funds. These funds are invested with Canandaigua National Bank (CNB), the custodian of the Diocesan Combined Endowment, with investment income allocated to the benefit of each congregation or organization. Prior to January 2014, the Diocesan balance sheet included the entire asset value of the CNB Combined Endowment. Effective January 2014, CNB moved to direct administration of investment deposits, withdrawals and other transactions with the congregations in the Diocesan Combined Endowment, and as such, the Diocese did not serve as intermediary custodian of the funds subsequent to this change. In 2014, the Diocese removed the investments of these parishes and congregations, and the related Funds Held for Others liability, from their financial statements and there was no effect on net assets. However, these funds continue to be invested together at CNB. The following investment and fair value disclosures pertain to the total fund at CNB.

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE C: INVESTMENTS, Cont'd

The composition of the Combined Endowment Fund at CNB is as follows:

	<u>December 31,</u>	
	<u>2017</u>	<u>2016</u>
Diocesan funds	\$ 18,426,818	\$ 16,169,035
Parishes and other organizations for which the Diocese is Trustee	<u>2,090,437</u>	<u>1,767,072</u>
Total Diocesan Trusteed Combined Endowment at CNB	20,517,255	17,936,107
Non-Trusteed funds belonging to other parishes in the Diocese	<u>7,944,533</u>	<u>7,155,983</u>
Total Combined Endowment at CNB	<u>\$ 28,461,788</u>	<u>\$ 25,092,090</u>

The fair value of investments in the Combined Endowment Fund held by the CNB on behalf of the Diocese and Individual parishes in the Diocese consisted of the following:

	<u>December 31,</u>	
	<u>2017</u>	<u>2016</u>
Investments, stated at fair value:		
Money market funds	\$ 497,867	\$ 504,539
U.S. government obligations	1,393,910	1,332,662
Common trust funds	5,356,913	4,228,295
Corporate bonds	1,920,525	1,657,250
Fixed income mutual funds	1,692,467	1,614,845
Mid cap mutual funds	1,324,750	1,140,130
Equity mutual funds	608,725	536,144
Common stock	12,798,643	11,229,020
REITS	108,385	120,429
Alternative institutional fund	951,704	921,606
Alternative investments	<u>1,807,899</u>	<u>1,807,170</u>
Total CNB Combined Endowment	<u>\$ 28,461,788</u>	<u>\$ 25,092,090</u>

The Diocese owns approximately a 72% and 71% pro-rata share of each individual investment class above as of December 31, 2017 and 2016, respectively.

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE C: INVESTMENTS, Cont'd

Investment income

The Diocese recorded the following investment income on the Diocesan Trusteed CNB Combined Endowment for the years ended:

	<u>December 31, 2017</u>		
	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>
Interest and dividend income	\$ 263,592	\$ 123,665	\$ 387,257
Gain on investments	1,843,543	949,576	2,793,119
Investment related expenses	<u>(116,050)</u>	<u>(55,952)</u>	<u>(172,002)</u>
	<u>\$ 1,991,085</u>	<u>\$ 1,017,289</u>	<u>\$ 3,008,374</u>

  

	<u>December 31, 2016</u>		
	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>
Interest and dividend income	\$ 202,877	\$ 100,000	\$ 302,877
Gain on investments	743,696	390,217	1,133,913
Investment related expenses	<u>(103,217)</u>	<u>(59,248)</u>	<u>(162,465)</u>
	<u>\$ 843,356</u>	<u>\$ 430,969</u>	<u>\$ 1,274,325</u>

Effective February 2018, the Trustees of the Diocese intend to target a spending rate of 5% of the trailing, 5-year average of the audited, year-end, market value of endowment assets; while maintaining the purchasing power of these investments. That is, net of spending, the objective is to grow the value of the portfolio at the rate of inflation over the investment horizon. The market value of these assets is inclusive of the year-end balance of the Diocesan loan and mortgage assets.

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE D: FAIR VALUE MEASUREMENTS

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets and liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are as follows:

- Level 1* Financial assets valued using level 1 inputs are based on unadjusted quoted market prices within active markets. Investments included in level 1 may include equity securities, mutual funds, and exchange traded funds.
- Level 2* Inputs to the valuation methodology include:
- Quoted prices for similar assets or liabilities in active markets;
  - Quoted prices for identical or similar assets or liabilities in inactive markets;
  - Inputs other than quoted prices that are observable for the asset or liability;
  - Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.

- Level 3* Inputs to the valuation methodology that are unobservable and significant to the fair value measurement. The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value. There have been no changes in the methodologies used at December 31, 2017 and 2016:

*Money market funds, U.S. government obligations, fixed income mutual funds, mid cap mutual funds, equity mutual funds, common stock and real estate investment trusts (REITS):* Valued at the closing price reported on the active market on which the individual funds are traded.

*Corporate bonds:* Valued by third party brokers based on terms and conditions using trades, bid price or spread, two sided markets, quotes, benchmark curves, discount rates, financial statements and trustee reports.

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE D: FAIR VALUE MEASUREMENTS, Cont'd

*Common trust funds* (Level two): Valued at net asset value provided by the underlying fund managers. The following is a description of the fund:

Silchester International Investors International Value Equity Trust - The Trust is a Delaware Statutory Trust investing in a diversified portfolio of equity securities of companies ordinarily incorporated in any country other than the United States for an opportunity to obtain long-term capital gains and income. Redemptions are permitted on a monthly basis as of the first business day of each month. As of December 31, 2017 and 2016, the Diocese had no unfunded commitments related to this investment.

*Alternative institutional fund* (Level two): Valued at the Diocese's share of the net asset value of funds the Diocese is invested in. Management has determined to use the net asset value as a practical expedient to determining fair value. The following is a description of the alternative institutional fund:

Pine Grove Alternative Institutional Fund – The Fund is a Delaware statutory trust registered as a non-diversified, closed end management investment company offering shares of beneficial interest at net asset value per share. The investment objective of the Fund is to seek long-term capital appreciation. Redemptions are permitted on a monthly basis based on a restriction period of up to ten months. As of December 31, 2017 and 2016, the Diocese had no unfunded commitments related to this investment.

*Alternative investments* (Level three): Valued at fair value utilizing valuations provided by the underlying fund managers. The market value of the underlying investments in the funds are valued based on unobservable inputs. The following is a description of the alternative investment:

Broadstone Net Lease, LLC – The Company is a real estate investment trust focused on investing in income-producing, net leased commercial properties. The Company owns commercial properties in the United States and leases the properties to businesses under the terms of long-term lease arrangements. As of December 31, 2017 and 2016, the Diocese had no unfunded commitments to this LLC. The Diocese can redeem shares quarterly; however, the investment is subject to redemption restrictions. If the investment has been held for more than 5 years, then the investor can redeem shares at 100% of the determined share value. If the investment has been held for less than 5 years, but greater than 1 year, there is a 5% penalty, (i.e. the investor receives 95% of the determined share value). Investments held for less than 1 year cannot be redeemed (i.e. 1 year lock up). The maximum redemption per quarter is 1% of shares outstanding at the start of the year plus 50% of reinvested dividends in the previous quarter. Broadstone can decide to redeem up to 5% of shareholder's allocation at any time within each calendar year.



EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
 (With Comparative Totals for 2016)

NOTE D: FAIR VALUE MEASUREMENTS, Cont'd

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Diocese believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain instruments could result in a different fair value measurement at the reporting date.

The following table sets forth by level within the fair value hierarchy, the assets held in the CNB Combined Endowment Fund at fair value at December 31, 2017 and 2016:

	December 31, 2017			
	Level 1	Level 2	Level 3	Total
Money market funds	\$ 497,867	\$ -	\$ -	\$ 497,867
U.S. government obligations	1,393,910	-	-	1,393,910
Common trust funds	-	5,356,913	-	5,356,913
Corporate bonds	-	1,920,525	-	1,920,525
Fixed income mutual funds	1,692,467	-	-	1,692,467
Mid cap mutual funds	1,324,750	-	-	1,324,750
Equity mutual funds	608,725	-	-	608,725
Common stock	12,798,643	-	-	12,798,643
REITS	108,385	-	-	108,385
Alternative institutional fund	-	951,704	-	951,704
Alternative investments	-	-	1,807,899	1,807,899
	<u>\$ 18,424,747</u>	<u>\$ 8,229,142</u>	<u>\$ 1,807,899</u>	<u>\$ 28,461,788</u>
	December 31, 2016			
	Level 1	Level 2	Level 3	Total
Money market funds	\$ 504,539	\$ -	\$ -	\$ 504,539
U.S. government obligations	1,332,662	-	-	1,332,662
Common trust funds	-	4,228,295	-	4,228,295
Corporate bonds	-	1,657,250	-	1,657,250
Fixed income mutual funds	1,614,845	-	-	1,614,845
Mid cap mutual funds	1,140,130	-	-	1,140,130
Equity mutual funds	536,144	-	-	536,144
Common stock	11,229,020	-	-	11,229,020
REITS	120,429	-	-	120,429
Alternative institutional fund	-	921,606	-	921,606
Alternative investments	-	-	1,807,170	1,807,170
	<u>\$ 16,477,769</u>	<u>\$ 6,807,151</u>	<u>\$ 1,807,170</u>	<u>\$ 25,092,090</u>

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE D: FAIR VALUE MEASUREMENTS, Cont'd

The following is a reconciliation of the beginning and ending balances for the Diocese's investments which are measured at fair value using significant unobservable inputs (Level 3):

Alternative Investments

	Balance at January 1, 2016	\$ 1,760,173
Purchases		56,828
Loss on investment		<u>(9,831)</u>
	Balance at December 31, 2016	1,807,170
Sales		(93,150)
Gain on investment		<u>93,879</u>
	Balance at December 31, 2017	<u>\$ 1,807,899</u>

NOTE E: LAND, BUILDINGS AND EQUIPMENT

Land, buildings and equipment consists of the following:

	<u>December 31,</u>	
	<u>2017</u>	<u>2016</u>
Land	\$ 68,278	\$ 166,978
Buildings and improvements	530,880	1,797,542
Equipment	<u>40,003</u>	<u>185,417</u>
	639,161	2,149,937
Less accumulated depreciation	<u>464,592</u>	<u>1,557,681</u>
	<u>\$ 174,569</u>	<u>\$ 592,256</u>

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE F: RETIREMENT AND BENEFIT PLANS

Retirement Plans

Diocesan clergy participate in the Church Pension Fund of the National Episcopal Church. Under the terms of this plan, the Diocese contributes 18% of each employee's salary to the plan. Employer contributions were approximately \$59,600 and \$42,700 for the years ended December 31, 2017 and 2016, respectively.

The Diocese sponsors a defined contribution plan for full-time lay employees. Under the terms of this plan, the Diocese contributes up to 12% of each employee's salary to the plan. In addition, employees are allowed to make elective tax-deferred contributions. Employer contributions were approximately \$44,400 and \$45,300 for the years ended December 31, 2017 and 2016, respectively.

Postretirement Health Insurance Benefits

On an annual basis, the Diocese determines what amount, if any, it will make available to pay health insurance benefits on behalf of its retired clergy, partners and Diocesan staff. The Diocese records an expense for these plans as insurance premiums are paid. Expense related to these plans totaled \$3,878 and \$5,423 for the years ended December 31, 2017 and 2016, respectively.

NOTE G: COMMITMENTS

The Diocese leases office equipment under a lease agreement expiring in August 2018. The lease requires monthly payments of \$154 through August 2018. The Diocese recognized approximately \$1,800 in lease expense, related to this lease, for the years ended December 31, 2017 and 2016. During 2018, the Diocese renewed this lease through August 2023. The lease requires monthly payments of \$178 through August 2023. In January 2017, the Diocese entered into an agreement to lease a new office space. The lease requires monthly payments of \$2,045 through January 2018. During 2018, the Diocese extended this lease agreement through January 2019.

The future minimum payments on these agreements are as follows:

<u>For the year ended December 31,</u>	<u>Amount</u>
2018	\$ 26,582
2019	4,185
2020	2,140
2021	2,140
2022	2,140
Thereafter	1,249
	<u>\$ 38,436</u>

EPISCOPAL DIOCESE OF ROCHESTER

NOTES TO FINANCIAL STATEMENTS, Cont'd

DECEMBER 31, 2017  
(With Comparative Totals for 2016)

NOTE H: SALE OF DIOCESAN HOUSE

In January 2017, the Diocese closed on the sale of their administrative center, located on East Avenue in Rochester, New York to 935 East, LLC. The administrative center was sold for approximately \$1,200,000. The Diocese received approximately \$1,000,000 at closing after \$200,000 was deposited with the escrow agent. 935 East, LLC also agreed to purchase select furnishings of the administrative center for an additional \$25,000. The Diocese also incurred approximately \$38,800 in moving expenses and improvements to its new office space, related to the sale of its administrative center.

NOTE I: HEALTH REIMBURSEMENT ACCOUNTS

During 2016, the Diocese began operating a health reimbursement account for its retired clergy that meet certain requirements such as age and employment history with the Diocese. The contribution amount is determined on an annual basis at the annual Diocesan convention. The amount expensed related to these accounts was \$60,091 and \$59,224 for the years ended December 31, 2017 and 2016, respectively. The Diocese has not recorded an obligation related to the account, which is required by generally accepted accounting principles as they consider potential alternatives for future funding of retiree benefits. The Diocese estimates that the current obligation could range from approximately \$522,000 to \$786,000.

Effective December 31, 2019, the Diocese will no longer accept new participants into its Health Reimbursement Account (HRA) plan. As of December 31, 2017, the Diocese believes that the actuarial estimate of the HRA liability, calculated as of December 31, 2016, is still accurate. The Diocese will reevaluate the estimated liability at December 31, 2019.

**EPISCOPAL DIOCESE OF ROCHESTER**

**OTHER FINANCIAL INFORMATION**

EPISCOPAL DIOCESE OF ROCHESTER

COMPARISON OF BUDGET TO ACTUAL OPERATING REVENUE AND EXPENSES

FOR THE YEAR ENDED DECEMBER 31, 2017

	Budget Approved by Diocesan Convention as Revised (Unaudited)	Actual	Actual Over/Under Budget
<u>REVENUE</u>			
Parish Support	\$ 973,151	\$ 972,304	\$ (847)
Investment spending policy	975,000	904,800	(70,200)
Interest on mortgages and loans	70,000	58,094	(11,906)
Other	<u>3,000</u>	<u>125</u>	<u>(2,875)</u>
	<u>2,021,151</u>	<u>1,935,323</u>	<u>(85,828)</u>
<u>EXPENSES</u>			
D & F MS Asking	238,000	238,000	-
Mission Partnerships	232,000	215,531	(16,469)
Congregational development	270,000	289,098	19,098
Leadership development	132,950	116,050	(16,900)
Governance	76,127	77,125	998
Diocesan Staff - Salaries	615,244	616,941	1,697
Diocesan Staff - Benefits	244,100	230,577	(13,523)
Diocesan Staff - Expenses	31,000	41,563	10,563
Office Expense	137,730	127,820	(9,910)
Health benefits	<u>63,200</u>	<u>63,969</u>	<u>769</u>
Total operating expenses	2,040,351	2,016,674	(23,677)
Non-operating (expense) income	<u>(32,500)</u>	<u>3,449</u>	<u>35,949</u>
Loss from operating fund	<u>\$ (51,700)</u>	<u>\$ (77,902)</u>	<u>\$ (26,202)</u>