

**AUDITED FINANCIAL STATEMENTS**

**AND OTHER FINANCIAL INFORMATION**

**THE EPISCOPAL DIOCESE OF NORTHWESTERN PENNSYLVANIA**

**Erie, Pennsylvania**

**December 31, 2008 and 2007**

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Erie, Pennsylvania

### INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying statement of assets, liabilities and net assets arising from cash transactions of The Episcopal Diocese of Northwestern Pennsylvania (Diocese) as of December 31, 2008 and the related statement of activities and cash flows for the year then ended. These financial statements are the responsibility of the Diocesan management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of The Episcopal Diocese of Northwestern Pennsylvania as of December 31, 2007 were audited by other auditors whose report dated October 31, 2008, expressed an unqualified opinion on those statements.

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 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 audit provides a reasonable basis for our opinion.

It is the policy of the Diocese not to capitalize or depreciate long lived assets over their estimated useful lives; rather, it expenses all long-lived assets when acquired. Additionally, the Diocese has not recorded the funded status of its defined benefit pension plans on the statements of financial position and not recorded the related cost elements of these plans in the statements of activities as required by Financial Accounting Standards (FAS) Nos. 87, 106, 132 and 158. It has also omitted disclosures related to these defined benefit plans required by FAS Nos. 132 and 158. Finally, as discussed in Note 9, these financial statements do not include any activity from "discretionary" checking accounts owned by the Diocese and "controlled" by the Bishop. In our opinion, accounting principles generally accepted in the United States of America require not-for-profit organizations to (1) capitalize long-lived tangible assets and recognize the depreciation of those assets, (2) record the funded status of defined benefit pension plans in the statements of financial position and record the related cost elements in the statements of activities as required by FAS Nos. 87, 106, 132 and 158,

(3) make disclosures relative to defined benefit pension plans as required by FAS Nos. 132 and 158, and (4) include all material assets owned in general purpose external financial statements. It was not practical to determine the effects of not capitalizing or depreciating any long-lived assets or recording defined benefit plan expense on a cash rather than GAAP basis; however, the aggregate total of the checking accounts excluded at both December 31, 2008 and 2007, was approximately \$167,450 and \$157,000, respectively.

In our opinion, except for the effects on the financial statements of the four matters discussed in the preceding paragraph, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Diocese at December 31, 2008, and 2007, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink that reads "De Marco Wachtel & Co". The signature is written in a cursive, flowing style.

Certified Public Accountants

Erie, Pennsylvania  
December 30, 2009

**BALANCE SHEET**  
**THE EPISCOPAL DIOCESE OF NORTHWESTERN PENNSYLVANIA**  
**December 31, 2008 and 2007**

<b><u>ASSETS</u></b>		
	<u>2008</u>	<u>2007</u>
<b>Current Assets:</b>		
Cash	\$ 159,391	\$ 189,973
Cash (sweep account interest)	18,834	13,800
Prepaid expenses	9,382	7,518
Accounts receivable - churches	10,850	10,060
Miscellaneous receivable	<u>4,727</u>	<u>2,844</u>
Total Current Assets	<u>203,184</u>	<u>224,195</u>
<b>Investments</b>	<u>8,625,912</u>	<u>11,432,626</u>
<b>Other Assets:</b>		
Loans receivable - clergy	98,367	98,367
Accounts receivable - church	<u>15,505</u>	<u>19,169</u>
	<u>113,872</u>	<u>117,536</u>
<b>TOTAL ASSETS</b>	<u><b>\$ 8,942,968</b></u>	<u><b>\$ 11,774,357</b></u>
 <b><u>LIABILITIES AND NET ASSETS</u></b>		
<b>Current Liabilities:</b>		
Current maturities of long-term debt	\$ 3,681	\$ 3,460
Accounts payable	8,138	7,699
Accrued payroll and related liabilities	<u>4,714</u>	<u>10,022</u>
Total Current Liabilities	<u>16,533</u>	<u>21,181</u>
<b>Long-Term Debt</b>	<u>15,505</u>	<u>19,169</u>
Total Liabilities	<u>32,038</u>	<u>40,350</u>
<b>Net Assets:</b>		
Unrestricted	7,347,090	9,818,773
Temporarily restricted	402,922	267,825
Permanently restricted	<u>1,160,918</u>	<u>1,647,409</u>
Total Net Assets	<u>8,910,930</u>	<u>11,734,007</u>
<b>Total Liabilities and Net Assets</b>	<u><b>\$ 8,942,968</b></u>	<u><b>\$ 11,774,357</b></u>

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

**STATEMENTS OF ACTIVITIES**  
**THE EPISCOPAL DIOCESE OF NORTHWESTERN PENNSYLVANIA**  
December 31, 2008

	Unrestricted Net Assets	Temporarily Restricted Net Assets	Permanently Restricted Net Assets	Totals 2008	Memo 2007
Revenue					
Assessment income	\$ 601,606	-	-	\$ 601,606	\$ 622,290
Other income	6,176			6,176	550
Contributions	105,683	22,804	14,774	143,261	247,004
Investment income (net)	233,737	10,967	38,159	282,863	298,870
Gain on investment transactions	(2,303,781)	(78,678)	(381,264)	(2,763,723)	730,958
Total Revenue	<u>(1,356,579)</u>	<u>(44,907)</u>	<u>(328,331)</u>	<u>(1,729,817)</u>	<u>1,899,672</u>
Net Assets released from Restrictions	-	(5,687)	-	(5,687)	-
Expenditures					
Diocesan house	442,801			442,801	578,586
Miscellaneous diocesan expenditures	101,588			101,588	72,204
Program expenditures	186,449			186,449	176,251
Other non-operating expenditures	182,162	3,424		185,586	346,077
Total Expenditures	<u>913,000</u>	<u>3,424</u>	<u>-</u>	<u>916,424</u>	<u>1,173,118</u>
Increase in Net Assets	(2,269,579)	(54,018)	(328,331)	(2,651,928)	726,554
Transfers and other changes in net assets	(202,104)	189,115	(158,160)	(171,149)	67,604
Net Assets at Beginning of Year	<u>9,818,773</u>	<u>267,825</u>	<u>1,647,409</u>	<u>11,734,007</u>	<u>10,939,849</u>
Net Assets at End of Year	<u>\$ 7,347,090</u>	<u>\$ 402,922</u>	<u>\$ 1,160,918</u>	<u>\$ 8,910,930</u>	<u>\$ 11,734,007</u>

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

**STATEMENTS OF CASH FLOWS**  
**THE EPISCOPAL DIOCESE OF NORTHWESTERN PENNSYLVANIA**  
**For the Years Ended December 31, 2008 and 2007**

	<u>2008</u>	<u>2007</u>
Cash Flows from Operating Activities		
Increase (decrease) in net assets	\$ (2,651,928)	\$ 726,554
Adjustments to reconcile change in net assets to cash from operating activities:		
Net realized and unrealized losses (gains) on investments	2,763,723	(730,958)
Contributions restricted for long-term purposes	-	(2,640)
Transfers, reclassifications and other changes in net assets	(170,103)	67,604
Increase (decrease) in:		
Receivables	(2,673)	(104,901)
Prepaid expense	(1,864)	(729)
Accounts payable	561	5,237
Other current liabilities	(5,087)	
Other assets	3,664	(19,968)
Net Cash Flows from Operating Activities	<u>(63,707)</u>	<u>(59,801)</u>
Cash Flows from Investing Activities		
Net investment purchasing activities	-	37,346
Cash Flows from Financing Activities		
Proceeds from contributions restricted for investing in permanent endowment	<u>38,159</u>	<u>2,640</u>
Net decrease in cash	(25,548)	(19,815)
Balance at December 31, 2007	<u>203,773</u>	<u>223,588</u>
Balance at December 31, 2008	<u>\$ 178,225</u>	<u>\$ 203,773</u>
Supplemental Cash Flow Information		
Non-cash financing activities		
Net (payments) of long-term debt of member churches	\$ (3,443)	\$ (3,208)

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

**NOTES TO FINANCIAL STATEMENTS**  
**THE EPISCOPAL DIOCESE OF NORTHWESTERN PENNSYLVANIA**  
**December 31, 2008 and 2007**

**Note 1 - Summary of Significant Accounting Policies**

This summary of significant accounting policies of the Episcopal Diocese of Northwestern Pennsylvania ("Diocese") is presented to assist in understanding the Diocese's financial statements. The financial statements and notes are representations of the Diocese's management, who is responsible for their integrity and objectivity. These accounting policies conform to generally accepted accounting principles, consistently applied in the preparation of the financial statements.

**A. Nature of Activities**

The Episcopal Diocese of Northwestern Pennsylvania was incorporated in 1911 under the Non-profit Corporation Law of Pennsylvania and embraces the Episcopal Church in all or parts of thirteen counties in Northwestern Pennsylvania. The Church in the Diocese of Northwestern Pennsylvania, being a constituent part of the Episcopal Church accedes to, recognizes, and adopts the Constitution and Canons of that church, and acknowledges its authority accordingly.

The Diocese collects, receives, and holds all assets conveyed, devised, bequeathed, or transferred to it, absolutely or in trust for any religious, charitable or educational use or purpose connected with the Church in said Diocese, or any portion thereof, for the aid, benefit or advancement of the said Diocese, or any parish or congregation, or of any religious, charitable or educational association of Churchmen in said Diocese.

The Rt. Rev. Sean Rowe was ordained Bishop of the Diocese in May, 2007 and began his duties in September of that year. Revenues of the Diocese consist primarily of assessments charge to member churches and investment activity.

**B. Basis of Accounting**

Assets, liabilities, revenues and expenses are recognized on the accrual basis of accounting for financial statements presentation purposes, with the exception of parish assessments, which are generally recorded as revenue when received. Diocesan management does not believe there would be a material difference in assessment revenue had the accrual basis been utilized. For 2008, 32 of the Diocese's 34 congregations paid its assessment in full.

**C. Cash and Cash Equivalents**

The Diocese considers time deposits, certificates of deposit and all other highly liquid debt instruments with original maturities of three months or less as cash and cash equivalents in determining the net change in cash on the statement of cash flows.

## Note 1 - Summary of Significant Accounting Policies (Continued...)

### D. Investments

The Diocese accounts for its investments in accordance with SFAS No. 124, Accounting for Certain Investments held by Not-for-Profit Organizations. SFAS No. 124 requires investments in equity securities with readily determinable fair values and all debt securities to be measured at fair value. Fair value is obtained from quoted market prices. SFAS No. 124 also requires dividends, interest and realized and unrealized gains and losses to be reported in the Statement of Activity as increases or decreases in unrestricted net assets unless their use is temporarily or permanently limited by externally imposed restrictions.

### E. Concentration of Credit Risk

The Diocese maintains cash accounts which, at times, exceed the federally insured limit. This limit was increase to \$250,000 from \$100,000 as a result of the Emergency Economic Stabilization Act of 2008. The Organization has not experienced any losses from maintaining cash accounts in excess of this limit and does not believe that it is exposed to any significant credit risk.

### F. Donated Services

No amounts have been reflected in the financial statements donated services, since no objectives basis is available to measure the value of such services. However, a number of volunteers have donated significant amounts of their time to operations at the Diocese.

### G. Net Assets

The Diocese's financial statements presentation is in accordance with Statement of Financial Accounting Standards (SFAS) No. 117, Financial Statements of Not-for-Profit Organizations. SFAS No. 117 establishes standards for external financial reporting by not-for-profit organizations. SFAS No. 117 requires that resources be classified into three net asset categories according to externally imposed restrictions. The three categories are as follows:

**Unrestricted Net Assets** – Net assets that are not subject to external restriction. The unrestricted net assets in these financial statements are sub-categorized into “general” and “Council designated” unrestricted net assets.

#### Unrestricted, General

General Fund – Includes the revenues, support and expenses associated with the principle functions and operation of the Diocese.

#### Unrestricted, Council Designated

- Endowment Funds – Funds to be used for specific purposes as designated by the Diocesan Council.
- Venture in Mission Fund – A Council designated fund to be used for Christian Ministry programs.

## Note 1 - Summary of Significant Accounting Policies

### G. Net Assets Unrestricted, Council Designated (Continued...)

- New Development Fund – A Council designated fund to be used to assist in the establishment of new church work, or revitalize church work, in the Diocese or elsewhere in the United States.
- St. Barnabas Fund – A Council designated fund which award “Outreach grants” to qualifying congregations in the diocese.
- Social Missioner Fund – A Council designated fund used to pay the wages, employee benefits and expenses of the social missioner. This fund was closed into the St. Barnabas Fund in 2008.

### Temporarily Restricted Net Assets

Net assets subject to externally-imposed restrictions that may or will be met either by passage of time or actions by the Diocese.

- Sundries and Endowment Funds – Includes funds received from various sources and the income earned from the permanently restricted funds for the purpose of funding the operations and special projects of the Diocese.
- Ida Wood Boyd Fund – Includes the interest earned on the principle from the will of George Boyd (1926); net assets released resulting from satisfaction of donor restrictions related to financial assistance to needy individuals.
- Ida Wood Boyd Emergency fund – Includes the principle from the will of George Boyd will (1926); for which the income is to be used in emergency relief for individuals or organizations.

### H. Income Tax Status

The Diocese is exempt from federal income tax under Section 501(c)(3) of the United States Internal Revenue code. It is not a private foundation.

### I. Accounting Estimates

The presentation of financial statements requires management to make estimates and assumptions that affect the reported amounts and assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Accordingly, actual results could differ from those estimates.

## Note 2 – Restricted Cash

Pursuant to a donor imposed restriction, monies have been set aside in the Ida Wood Boyd Emergency fund for the purpose of providing aid to families in crisis. In order to facilitate the aid in a timely fashion, income of the fund is maintained separately in cash accounts. This separate cash is restricted to those activities prescribed by the donor and totaled \$57,527 and \$58,845 at December 31, 2008 and 2007, respectively.

### Note 3 – Investments

Investments are presented in the financial statements at fair value. The balances in the various funds, with corresponding cost basis, at December 31, 2008 consist of the following:

	<u>Fair Value</u>	<u>Cost</u>
General Fund	\$ 723,638	\$ 697,396
Diocese	273,873	271,945
Other	582,915	623,407
Sundries	<u>3,088,712</u>	<u>3,317,076</u>
	4,669,138	4,909,824
Ida Wood Boyd Fund	348,802	361,717
Ida Wood Boyd Emergency Fund	401,294	422,537
Venture in Mission Fund	886,074	911,423
New Development Fund	292,947	304,200
St. Barnabas Fund	<u>2,027,657</u>	<u>2,184,871</u>
	<u>\$ 8,625,912</u>	<u>\$9,094,572</u>

The fair value of investments at December 31, 2008 and 2007 consisted of the following:

	<u>2008</u>	<u>2007</u>
Short term investments	\$ 1,212,344	\$ 645,998
Mutual funds	2,712,950	4,446,508
Fixed income securities	6,724,938	8,322,218
Common stocks	<u>7,544,632</u>	<u>11,079,176</u>
	18,194,864	24,493,900
Less assets of other Diocesan Churches commingled at year End (Note 1)	<u>9,568,952</u>	<u>13,061,274</u>
	<u>\$ 8,625,912</u>	<u>\$11,432,626</u>

Statement of activities line items "Investment Income (Net)" and "Gain on investments transactions" were comprised of the following for the year ended December 31, 2008:

Dividends and interest income	\$ 320,003
Investment fees paid	<u>39,247</u>
Investment income (Net)	<u>\$ 280,756</u>
Realized losses	\$ 415,482
Unrealized losses	<u>2,348,241</u>
Loss on investment transactions	<u>\$2,763,723</u>

#### Note 4 – Loans Receivable – Clergy

The Nellie J. Cockerham Fund loaned \$48,367 (\$50,000 less a repayment of \$1,633) to the Diocese's new Bishop, the Rt. Rev. Sean Rowe for the purchase of a residence in August, 2007. Additionally, in October, 2007 that same fund advanced the Diocese's new Canon to the Ordinary, Martha S. Ishman, \$50,000 for the purchase of a residence. Each loan is classified as other (long-term) asset because repayment of each is only required upon (1) the sale of the real estate or (2) the termination of the ecclesiastical relationship between the Diocese and the respective clergy member.

#### Note 5 - Pension Plans

The Diocese makes contributions to the Church Pension Fund, for clergy and Episcopal Church Lay Employees Retirement Plan, now administered by the Church Life Insurance Corporation, for lay employees. Both are defined benefit plans and contributions are actuarially computed based upon the total employee compensation and pooled pension funds. The contribution amount paid, and financial statement pension expense, for the years ended December 31, 2008 and 2007 was \$37,714 and \$39,023, respectively. It is management's understanding that these amounts approximate the expense as if it were determined under generally accepted accounting principles; however, this "cash basis" recording of the expense results in an exception from Financial Accounting Standards Nos. 87, 106, 132 and 158.

The Diocese also began a Section 403(b) Plan for other lay employees effective in 2004. the employer contribution to this defined contribution plan was \$6,099 and \$4,249, respectively for 2008 and 2007. Finally, the Diocese makes monthly pension payments to a retired lay employee under a private agreement. The amount of these "direct pension" payments totaled \$7,575 and \$5,331 for the respective years ended December 31, 2008 and 2007.

#### Note 6 – Functional Classification of Expenditures

Expenditures by functional classification for the years ended December 31, 2008 and 2007 are as follows:

	<u>2008</u>	<u>2007</u>
Program services	\$ 368,611	\$ 522,328
Administration and support	544,389	650,790
	<u>\$ 913,000</u>	<u>\$1,173,118</u>

### Note 7 – Long-Term Debt

The Diocese, in an effort to help its mission churches, signs loan agreements for the debt of these churches, and an agreement is made that the churches will make the loan payments. Since the diocese is an obligor on these notes, the liability is recorded and an offsetting receivable from the churches is recorded because the churches repay the notes and use the proceeds. The following is a summary of long-term debt at December 31, 2008:

Loans payable to PNC Bank with monthly payments of \$398.01 (including interest at 6.25% per annum secured by the general assets of the Diocese, maturing August, 2013.	\$ 19,186
Less current portion	<u>3,681</u>
	<u>\$ 15,505</u>

Long-term debt maturing within each of the five years subsequent to December 31, 2008 is as follows:

2009	\$ 3,681
2010	3,918
2011	4,170
2012	4,438
2013	<u>2,979</u>
	<u>\$ 19,186</u>

### Note 8 – Operating Lease

The Diocese is obligated under three operating leases for office equipment. Their aggregate monthly payment is \$235. The lease expense totaled \$2,820 for 2008 and 2007. Lease payments with no cancellation rights are as follows:

2009	\$ 2,216
2010	1,586
2011	1,586
2012	78

### Note 9 – “Discretionary Funds”

There are five checking accounts, owned by the Diocese but “controlled” by the Bishop, not included in these financial statements. They totaled approximately \$167,450 and \$157,000 at December 31, 2008 and 2007, respectively. While this is not an uncommon practice in the Episcopal Church, the omission of these accounts and the activity within them is a departure from U.S. generally accepted accounting principles. The monies are used for various purposes, as directed by the Bishop, including for people in need, seminarians and non-budgeted Diocesan operating expenditures during the year.

