

**EPISCOPAL DIOCESE OF ROCHESTER**

**Financial Statements  
as of December 31, 2012  
Together with  
Independent Auditor's Report**

**Bonadio & Co., LLP**  
Certified Public Accountants

## **INDEPENDENT AUDITOR'S REPORT**

August 13, 2013

To the Diocesan Trustees of the  
Episcopal Diocese of Rochester:

### **Report on Financial Statements**

We have audited the accompanying financial statements of the Episcopal Diocese of Rochester (the Diocese), which comprise the balance sheet as of December 31, 2012, and the related statements of revenue, expenses and changes 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.

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## INDEPENDENT AUDITOR'S REPORT

(Continued)

### ***Basis for Qualified Opinion***

As more fully described in Note 2 to the financial statements, 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 effect of this departure is not reasonably determinable

### ***Qualified Opinion***

In our opinion, except for the effects of the matters discussed in the Basis for Qualified Opinion paragraph, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Episcopal Diocese of Rochester as of December 31, 2012, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Auditor's Updated Opinion on 2011 Financial Statements***

We have previously audited the 2011 financial statements, and In our report dated April 13, 2012 we expressed an opinion that the 2011 financial statements did not fairly present financial position, and the changes in net assets and cash flows in accordance with accounting principles generally accepted in the United States of America because the Diocese did not depreciate buildings and equipment related to improvement and replacement of property and equipment. Also, only certain expenditures, as authorized by the Diocesan Trustees, have been capitalized. Additionally, the Diocese has not adopted the accounting or disclosure requirements for donor restricted gifts including endowments. As described in Note 2, the Diocese has changed its method of accounting for depreciation and capitalization and has restated its 2011 financial statements to conform with accounting principles generally accepted in the United States of America for that matter. Accordingly, our present opinion on the 2011 financial statements, as presented herein, is different from that expressed in our previous report. Except for this matter, in our opinion, the summarized comparative information presented herein as of December 31, 2011 is consistent, in all material respects, with the audited financial statements from which it has been derived.

### ***Report on Supplementary Information***

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental Comparison of Budget to Actual Operating Revenue and Expenses in Exhibit I, which is the responsibility of management, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information, except for that portion marked "unaudited," was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. That 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 Exhibit of the qualified opinion on the financial statements as described above, such 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.

*Bonadio & Co., LLP*

**EPISCOPAL DIOCESE OF ROCHESTER**

**BALANCE SHEET**

**DECEMBER 31, 2012**

(With Comparative Totals for 2011)

|                                                     | 2012         |                 |              |               |              |              |               |                 |               |               | 2011<br>Total<br>All Funds |  |
|-----------------------------------------------------|--------------|-----------------|--------------|---------------|--------------|--------------|---------------|-----------------|---------------|---------------|----------------------------|--|
|                                                     | Unrestricted |                 |              |               |              | Restricted   |               |                 |               |               |                            |  |
|                                                     | Operating    | Special Purpose | Real Estate  | Total         | Endowment    | By Donors    | Total         | Total All Funds |               |               |                            |  |
| <b>ASSETS</b>                                       |              |                 |              |               |              |              |               |                 |               |               |                            |  |
| CASH                                                | \$ 260,910   | \$ 6,064        | \$ -         | \$ 266,974    | \$ -         | \$ 14,366    | \$ 14,366     | \$ 14,366       | \$ 281,340    | \$ 424,304    |                            |  |
| MORTGAGES AND LOANS RECEIVABLE                      | -            | 431,752         | -            | 431,752       | -            | 821,162      | 821,162       | 821,162         | 1,252,914     | 1,081,749     |                            |  |
| MORTGAGES AND LOANS RECEIVABLE -<br>Related parties | 156,257      | 99,257          | -            | 255,514       | -            | -            | -             | -               | 255,514       | 271,841       |                            |  |
| PREPAIDS AND OTHER ASSETS                           | 48,632       | 256             | -            | 48,888        | -            | -            | -             | -               | 48,888        | 43,745        |                            |  |
| BOOK STORE INVENTORIES                              | -            | 16,322          | -            | 16,322        | -            | -            | -             | -               | 16,322        | 24,171        |                            |  |
| INVESTMENTS                                         | -            | 12,386,022      | -            | 12,386,022    | 3,555,562    | 9,132,484    | 12,688,046    | 25,074,068      | 25,305,993    | 25,305,993    |                            |  |
| DUE (TO) FROM OTHER FUNDS                           | 132,444      | 688,717         | -            | 821,161       | -            | (821,161)    | (821,161)     | -               | -             | -             |                            |  |
| LAND, BUILDINGS AND EQUIPMENT, net (Note 2)         | -            | -               | 1,096,053    | 1,096,053     | -            | -            | -             | -               | 1,096,053     | 1,140,015     |                            |  |
|                                                     | \$ 598,243   | \$ 13,628,390   | \$ 1,096,053 | \$ 15,322,686 | \$ 3,555,562 | \$ 9,146,851 | \$ 12,702,413 | \$ 28,025,099   | \$ 28,291,818 | \$ 28,291,818 |                            |  |
| <b>LIABILITIES AND NET ASSETS</b>                   |              |                 |              |               |              |              |               |                 |               |               |                            |  |
| ACCOUNTS PAYABLE                                    | \$ 51,084    | \$ 6,635        | \$ -         | \$ 57,719     | \$ -         | \$ -         | \$ -          | \$ -            | \$ 57,719     | \$ 25,528     |                            |  |
| ACCRUED LIABILITIES                                 | 67,238       | -               | -            | 67,238        | -            | 17,384       | 17,384        | 17,384          | 84,622        | 107,530       |                            |  |
| FUNDS HELD FOR OTHERS                               | -            | -               | -            | -             | -            | 6,528,073    | 6,528,073     | 6,528,073       | 6,528,073     | 6,393,596     |                            |  |
|                                                     | 118,322      | 6,635           | -            | 124,957       | -            | 6,545,457    | 6,545,457     | 6,545,457       | 6,670,414     | 6,526,654     |                            |  |
| <b>NET ASSETS:</b>                                  |              |                 |              |               |              |              |               |                 |               |               |                            |  |
| Unrestricted                                        | 479,921      | 13,621,755      | 1,096,053    | 15,197,729    | -            | -            | -             | -               | 15,197,729    | 15,629,711    |                            |  |
| Restricted                                          | -            | -               | -            | -             | 3,555,562    | 2,601,394    | 6,156,956     | 6,156,956       | 6,156,956     | 6,135,453     |                            |  |
| Total net assets                                    | 479,921      | 13,621,755      | 1,096,053    | 15,197,729    | 3,555,562    | 2,601,394    | 6,156,956     | 21,354,685      | 21,765,164    |               |                            |  |
|                                                     | \$ 598,243   | \$ 13,628,390   | \$ 1,096,053 | \$ 15,322,686 | \$ 3,555,562 | \$ 9,146,851 | \$ 12,702,413 | \$ 28,025,099   | \$ 28,291,818 | \$ 28,291,818 |                            |  |

The accompanying notes are an integral part of these statements.

**EPISCOPAL DIOCESE OF ROCHESTER**

**STATEMENT OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS  
FOR THE YEAR ENDED DECEMBER 31, 2012**

(With Comparative Totals for 2011)

|                                                             | 2012               |                      |                     |                      |                     |                     |                     |                      |                      |  | 2011<br>Total<br>All Funds |
|-------------------------------------------------------------|--------------------|----------------------|---------------------|----------------------|---------------------|---------------------|---------------------|----------------------|----------------------|--|----------------------------|
|                                                             | Unrestricted       |                      |                     |                      |                     | Restricted          |                     |                      |                      |  |                            |
|                                                             | Operating          | Special Purpose      | Real Estate         | Total                | Endowment           | By Donors           | Total               | Total All Funds      |                      |  |                            |
| <b>REVENUE:</b>                                             |                    |                      |                     |                      |                     |                     |                     |                      |                      |  |                            |
| Parish support                                              | \$ 1,014,977       | \$ -                 | \$ -                | \$ 1,014,977         | \$ -                | \$ -                | \$ 41,921           | \$ 1,014,977         | \$ 1,016,685         |  |                            |
| Contributions                                               | -                  | -                    | -                   | -                    | -                   | 41,921              | -                   | 41,921               | 21,457               |  |                            |
| Book store                                                  | -                  | 88,424               | -                   | 88,424               | -                   | -                   | -                   | 88,424               | 92,791               |  |                            |
| Interest on mortgages and loans                             | 83,944             | -                    | -                   | 83,944               | -                   | -                   | -                   | 83,944               | 92,372               |  |                            |
| Other                                                       | 3,000              | -                    | -                   | 3,000                | -                   | -                   | -                   | 3,000                | 3,392                |  |                            |
|                                                             | <u>1,101,921</u>   | <u>88,424</u>        | <u>-</u>            | <u>1,190,345</u>     | <u>-</u>            | <u>41,921</u>       | <u>41,921</u>       | <u>1,232,266</u>     | <u>1,226,697</u>     |  |                            |
| <b>EXPENSES:</b>                                            |                    |                      |                     |                      |                     |                     |                     |                      |                      |  |                            |
| Mission outside the Diocese                                 | 231,592            | -                    | -                   | 231,592              | -                   | -                   | -                   | 231,592              | 229,643              |  |                            |
| Mission within the Diocese                                  | 227,209            | -                    | -                   | 227,209              | -                   | -                   | -                   | 227,209              | 183,686              |  |                            |
| Congregational Development                                  | 416,519            | -                    | -                   | 416,519              | -                   | -                   | -                   | 416,519              | 447,503              |  |                            |
| Communications                                              | 22,335             | -                    | -                   | 22,335               | -                   | -                   | -                   | 22,335               | 69,813               |  |                            |
| Leadership Development                                      | 47,895             | -                    | -                   | 47,895               | -                   | -                   | -                   | 47,895               | 54,282               |  |                            |
| Governance, Committees and Missioners                       | 116,134            | 2,124                | -                   | 118,258              | -                   | -                   | -                   | 118,258              | 122,829              |  |                            |
| Executive staff                                             | 494,935            | -                    | -                   | 494,935              | -                   | -                   | -                   | 494,935              | 521,953              |  |                            |
| Support staff                                               | 424,284            | -                    | -                   | 424,284              | -                   | -                   | -                   | 424,284              | 560,796              |  |                            |
| Office expense                                              | 144,915            | -                    | -                   | 144,915              | -                   | -                   | -                   | 144,915              | 179,972              |  |                            |
| Clergy and Lay benefits                                     | 162,707            | -                    | -                   | 162,707              | -                   | -                   | -                   | 162,707              | 155,410              |  |                            |
| Nonoperating expense                                        | 179,865            | -                    | -                   | 179,865              | -                   | -                   | -                   | 179,865              | -                    |  |                            |
| Distributions to parishes                                   | -                  | -                    | -                   | -                    | -                   | 54,865              | 54,865              | 54,865               | 234,730              |  |                            |
| Depreciation                                                | -                  | -                    | 52,211              | 52,211               | -                   | 63,944              | 63,944              | 63,944               | 75,230               |  |                            |
| Book store                                                  | -                  | 91,268               | -                   | 91,268               | -                   | -                   | -                   | 91,268               | 40,314               |  |                            |
|                                                             | <u>2,468,390</u>   | <u>93,392</u>        | <u>52,211</u>       | <u>2,613,993</u>     | <u>-</u>            | <u>118,809</u>      | <u>118,809</u>      | <u>2,732,802</u>     | <u>2,736,272</u>     |  |                            |
| <b>EXCESS OF REVENUE OVER EXPENSES</b>                      | <b>(1,366,469)</b> | <b>(4,968)</b>       | <b>(52,211)</b>     | <b>(1,423,648)</b>   | <b>-</b>            | <b>(76,888)</b>     | <b>(76,888)</b>     | <b>(1,500,536)</b>   | <b>(1,509,575)</b>   |  |                            |
| <b>LOSS ON LOAN WRITE-OFF</b>                               | <b>-</b>           | <b>(262,116)</b>     | <b>-</b>            | <b>(262,116)</b>     | <b>-</b>            | <b>-</b>            | <b>-</b>            | <b>(262,116)</b>     | <b>-</b>             |  |                            |
| <b>INVESTMENT INCOME, net</b>                               | <b>-</b>           | <b>689,974</b>       | <b>-</b>            | <b>689,974</b>       | <b>419,913</b>      | <b>242,286</b>      | <b>662,199</b>      | <b>1,352,173</b>     | <b>(403,890)</b>     |  |                            |
| <b>CHANGE IN NET ASSETS</b>                                 | <b>(1,366,469)</b> | <b>422,890</b>       | <b>(52,211)</b>     | <b>(995,790)</b>     | <b>419,913</b>      | <b>165,398</b>      | <b>585,311</b>      | <b>(410,479)</b>     | <b>(1,913,465)</b>   |  |                            |
| <b>NET ASSETS - beginning of year, as previously stated</b> | <b>621,838</b>     | <b>13,867,858</b>    | <b>1,140,015</b>    | <b>15,629,711</b>    | <b>3,368,923</b>    | <b>2,766,530</b>    | <b>6,135,453</b>    | <b>21,765,164</b>    | <b>25,300,410</b>    |  |                            |
| <b>CHANGE IN ACCOUNTING FOR FIXED ASSETS (Note 2)</b>       | <b>-</b>           | <b>-</b>             | <b>-</b>            | <b>-</b>             | <b>-</b>            | <b>-</b>            | <b>-</b>            | <b>-</b>             | <b>(1,621,781)</b>   |  |                            |
| <b>NET ASSETS - beginning of year, as restated</b>          | <b>621,838</b>     | <b>13,867,858</b>    | <b>1,140,015</b>    | <b>15,629,711</b>    | <b>3,368,923</b>    | <b>2,766,530</b>    | <b>6,135,453</b>    | <b>21,765,164</b>    | <b>23,678,629</b>    |  |                            |
| <b>INTER-FUND TRANSFERS</b>                                 | <b>(8,247)</b>     | <b>326,021</b>       | <b>8,249</b>        | <b>326,023</b>       | <b>-</b>            | <b>(326,023)</b>    | <b>(326,023)</b>    | <b>-</b>             | <b>-</b>             |  |                            |
| <b>SPENDING POLICY TRANSFER</b>                             | <b>1,232,799</b>   | <b>(995,014)</b>     | <b>-</b>            | <b>237,785</b>       | <b>(233,274)</b>    | <b>(4,511)</b>      | <b>(237,785)</b>    | <b>-</b>             | <b>-</b>             |  |                            |
| <b>NET ASSETS - end of year</b>                             | <b>\$ 479,921</b>  | <b>\$ 13,621,755</b> | <b>\$ 1,096,053</b> | <b>\$ 15,197,729</b> | <b>\$ 3,555,562</b> | <b>\$ 2,601,394</b> | <b>\$ 6,156,956</b> | <b>\$ 21,354,685</b> | <b>\$ 21,765,164</b> |  |                            |

The accompanying notes are an integral part of these statements.

**EPISCOPAL DIOCESE OF ROCHESTER**

**STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED DECEMBER 31, 2012**  
(With Comparative Totals for 2011)

|                                                                                           | 2012           |                    |                |              |            |            |            |                    |                |  | 2011<br>Total<br>All Funds |  |
|-------------------------------------------------------------------------------------------|----------------|--------------------|----------------|--------------|------------|------------|------------|--------------------|----------------|--|----------------------------|--|
|                                                                                           | Unrestricted   |                    |                |              |            | Restricted |            |                    |                |  |                            |  |
|                                                                                           | Operating      | Special<br>Purpose | Real<br>Estate | Total        | Endowment  | By Donors  | Total      | Total<br>All Funds |                |  |                            |  |
| <b>CASH FLOW FROM OPERATING ACTIVITIES:</b>                                               |                |                    |                |              |            |            |            |                    |                |  |                            |  |
| Change in net assets                                                                      | \$ (1,366,469) | \$ 422,890         | \$ (52,211)    | \$ (995,790) | \$ 419,913 | \$ 165,398 | \$ 585,311 | \$ (410,479)       | \$ (1,913,465) |  |                            |  |
| Adjustments to reconcile change in net assets to net cash flow from operating activities: |                |                    |                |              |            |            |            |                    |                |  |                            |  |
| Depreciation                                                                              | -              | -                  | 52,211         | 52,211       | -          | -          | -          | 52,211             | 40,314         |  |                            |  |
| Loss (gain) on investments, net                                                           | -              | (689,974)          | -              | (689,974)    | (419,913)  | (242,286)  | (662,199)  | (1,352,173)        | 561,569        |  |                            |  |
| Changes in:                                                                               |                |                    |                |              |            |            |            |                    |                |  |                            |  |
| Book store inventories                                                                    | -              | 7,849              | -              | 7,849        | -          | -          | -          | 7,849              | (6,560)        |  |                            |  |
| Due to (from) other funds                                                                 | (11,180)       | (534,452)          | -              | (545,632)    | -          | 545,632    | 545,632    | -                  | -              |  |                            |  |
| Prepays and other assets                                                                  | (5,459)        | 316                | -              | (5,143)      | -          | -          | -          | (5,143)            | (10,364)       |  |                            |  |
| Accounts payable                                                                          | 31,497         | 693                | -              | 32,190       | -          | 2,337      | 2,337      | 34,527             | (18,557)       |  |                            |  |
| Accrued liabilities                                                                       | (24,800)       | -                  | -              | (24,800)     | -          | -          | -          | (24,800)           | 32,740         |  |                            |  |
| Net cash flow from operating activities                                                   | (1,376,411)    | (792,678)          | -              | (2,169,089)  | -          | 471,081    | 471,081    | (1,698,008)        | (1,314,323)    |  |                            |  |
| <b>CASH FLOW FROM INVESTING ACTIVITIES:</b>                                               |                |                    |                |              |            |            |            |                    |                |  |                            |  |
| Change in mortgages and loans receivable, net                                             | -              | (558)              | -              | (558)        | -          | (170,607)  | (170,607)  | (171,165)          | (42,538)       |  |                            |  |
| Change in mortgages and loans receivable-Related parties, net                             | 7,327          | 2,300              | -              | 9,627        | -          | -          | -          | 9,627              | 7,200          |  |                            |  |
| (Purchases) sales of investments, net                                                     | -              | 2,117,985          | -              | 2,117,985    | 233,274    | (760,909)  | (527,635)  | 1,590,350          | 2,488,232      |  |                            |  |
| Purchases of land, buildings, and equipment                                               | -              | -                  | (8,245)        | (8,245)      | -          | -          | -          | (8,245)            | -              |  |                            |  |
| Spending policy transfer                                                                  | 1,232,799      | (995,014)          | -              | 237,785      | (233,274)  | (4,511)    | (237,785)  | -                  | -              |  |                            |  |
| Inter-fund transfers                                                                      | (8,247)        | (326,021)          | 8,245          | (326,023)    | -          | 326,023    | 326,023    | -                  | -              |  |                            |  |
| Change in funds held for others, net                                                      | -              | -                  | -              | -            | -          | 134,477    | 134,477    | 134,477            | (834,858)      |  |                            |  |
| Net cash flow from investing activities                                                   | 1,231,879      | 798,692            | -              | 2,030,571    | -          | (475,527)  | (475,527)  | 1,555,044          | 1,618,036      |  |                            |  |
| <b>CHANGE IN CASH</b>                                                                     | (144,532)      | 6,014              | -              | (138,518)    | -          | (4,446)    | (4,446)    | (142,964)          | 303,713        |  |                            |  |
| <b>CASH - beginning of year</b>                                                           | 405,442        | 50                 | -              | 405,492      | -          | 18,812     | 18,812     | 424,304            | 120,591        |  |                            |  |
| <b>CASH - end of year</b>                                                                 | \$ 260,910     | \$ 6,064           | \$ -           | \$ 266,974   | \$ -       | \$ 14,366  | \$ 14,366  | \$ 281,340         | \$ 424,304     |  |                            |  |

The accompanying notes are an integral part of these statements.

# EPISCOPAL DIOCESE OF ROCHESTER

## NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2012

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### 1. ORGANIZATION

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 47 active congregations and 8 summer and institutional chapels. The Diocesan House, on East Avenue in Rochester, New York is the administrative center of the Diocese and houses the office of the Bishop.

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.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### Basis of Accounting

Prior to 2012, the Diocese followed the accounting principles generally accepted in the United States, except for the items described below.

|                                     | <u>Generally Accepted Accounting Principles</u>                                                                                                                                                                          | <u>Diocese Accounting Principles</u>                       |
|-------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------|
| Recording of furniture and fixtures | Capitalized and depreciated                                                                                                                                                                                              | Expensed (or charged to special funds) at time of purchase |
| Other fixed assets                  | Capitalized and depreciated                                                                                                                                                                                              | Capitalized, but not depreciated                           |
| 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                                      |

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### **Basis of Accounting (Continued)**

The Diocese has not yet modified its financial reporting practices to reflect the classification of its net assets and activities as unrestricted, temporarily restricted or permanently restricted. Rather, it uses the principles of fund accounting consistent with its historical practice. Accounting principles generally accepted in the United States requires that the classification of net assets and activities be based on donor wishes and include unrestricted, temporarily and permanently restricted classifications. The effect of this departure from generally accepted accounting principles is not reasonably determinable.

### **Change in Accounting Principle**

The Diocese changed its accounting policy for fixed assets in 2012 and began recording depreciation on fixed assets. Prior to 2012, the Diocese did not depreciate its fixed assets. The reason the Diocese changed the accounting policy was to be in compliance with generally accepted accounting principles. The change in accounting policy was retrospectively adopted and the effect was a reduction in unrestricted net assets of \$1.6 million as of January 1, 2011.

### **Financial Reporting**

The Diocese's assets, liabilities and net assets are classified as follows:

- **Unrestricted**

Unrestricted net assets are 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, Housing Loan Fund and book store operations.

- **Real Estate**

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

- **Restricted**

Restricted net assets 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.

### **Comparative Information**

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



## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### **Cash**

Cash consists of bank demand deposit and money market accounts which, at times, may exceed federally insured limits. The Diocese has not experienced any losses related to cash and believes it is not exposed to any significant credit risk with respect to these balances.

### **Mortgages and Loans Receivable**

Mortgages and loans receivable represent amounts due to the Diocese under loan agreements. 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. As of December 31, 2012 and 2011, the Diocese determined that an allowance is not necessary.

Loans are placed on nonaccrual status when management believes collection of interest is doubtful. As of December 31, 2012 and 2011, the Diocese did not have any loans on nonaccrual status.

### **Book Store Inventories**

Inventory is stated at the lower of cost, as determined on the first-in, first-out basis, or market.

### **Investments**

Investments consist of various items stated at fair value as well as certain money market funds that are stated at cost, which approximate fair value. The Diocese's investment in Community Development mortgages and loans receivable are carried at historical cost.

Investment securities are exposed to various risks, such as interest rate, market economic conditions, world affairs and credit risks. Due to the level of risk associated with certain investment securities, it is possible that changes in their values could occur in the near term and such changes could materially affect the net assets of the Diocese.

### **Fair Value Measurement - Definition and Hierarchy**

The Diocese uses various valuation techniques in determining fair value. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the Diocese. Unobservable inputs are inputs that reflect the Diocese's assumptions about the estimates market participants would use in pricing the asset or liability, developed based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

- Level 1 - Valuations based on quoted prices in active markets for identical assets or liabilities that the Diocese has the ability to access. Valuation adjustments are not applied to Level 1 instruments. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation does not entail a significant degree of judgment.
- Level 2 - Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly.
- Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### **Fair Value Measurement - Definition and Hierarchy (Continued)**

The availability of observable inputs can vary and is affected by a wide variety of factors. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised in determining fair value is greatest for instruments categorized in Level 3. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, for disclosure purposes the level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

### **Land, Buildings, and Equipment**

In addition to the Diocesan House, the Diocese owns certain missions (parish churches, which are not self-supporting) and other properties. These properties were brought under general ledger control of the Diocese on January 1, 1973, and were recorded on its balance sheet at their appraised replacement value. The appraisal included only buildings and equipment. Land has been recorded at cost.

The Diocese capitalizes additional land, buildings, and equipment purchases greater than \$1,000 with an estimated useful life exceeding three (3) years. Beginning in 2012, depreciation expense is recognized over the assets estimated useful lives which range from 3-40 years.

### **Income Taxes**

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.

For tax-exempt entities, their tax-exempt status itself is deemed to be an uncertainty, since events could potentially occur to jeopardize their tax-exempt status. As of December 31, 2012 and 2011, the Diocese does not have a liability for unrecognized tax benefits.

### **Estimates**

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

### **Reclassifications**

Certain 2011 amounts have been reclassified to conform to the 2012 presentation.

### 3. MORTGAGES AND LOANS RECEIVABLE

Mortgages and loans receivable consisted of the following at December 31:

|                                       | <u>2012</u>         | <u>2011</u>         |
|---------------------------------------|---------------------|---------------------|
| Unrestricted:                         |                     |                     |
| Mortgages and loans - related parties | \$ 255,514          | \$ 271,841          |
| Housing loan fund                     | <u>431,752</u>      | <u>431,194</u>      |
| Total unrestricted funds              | <u>687,266</u>      | <u>703,035</u>      |
| Restricted:                           |                     |                     |
| Sibley revolving loan fund            | 821,162             | 650,027             |
| Bishop's revolving loan fund          | <u>-</u>            | <u>528</u>          |
| Total restricted funds                | <u>821,162</u>      | <u>650,555</u>      |
|                                       | <u>\$ 1,508,428</u> | <u>\$ 1,353,590</u> |

Mortgages and loans receivable bear interest at rates ranging from 2.5% to 5.0% and mature at various dates through October 2031. Approximately \$687,000 and \$703,000 of the balance of the receivables outstanding at December 31, 2012 and 2011, respectively, are secured by first and second mortgages. All remaining amounts outstanding are unsecured. Included in unrestricted mortgages and loans receivable are amounts due from the Bishop, priests and canons which totaled \$255,514 and \$271,841 at December 31, 2012 and 2011, respectively.

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.

During 2012 certain loans were deemed uncollectible and a loss on loan write-off of \$262,116 is reflected in the statement of revenue, expenses, and changes in net assets. There were no such write-offs in 2011. As of December 31, 2012 and 2011, there were no other receivables that were past due or on non-accrual status.

Principal payments due to be received on mortgages and loans receivable are as follows for the years ending December 31:

|            |                     |
|------------|---------------------|
| 2013       | \$ 94,691           |
| 2014       | 88,305              |
| 2015       | 90,532              |
| 2016       | 91,566              |
| 2017       | 93,032              |
| Thereafter | <u>1,050,302</u>    |
|            | <u>\$ 1,508,428</u> |

#### 4. INVESTMENTS

Investments consisted of the following at December 31:

|                                    | <u>2012</u>          | <u>2011</u>          |
|------------------------------------|----------------------|----------------------|
| Investments, stated at fair value: |                      |                      |
| Money market funds                 | \$ 729,390           | \$ 1,313,449         |
| U.S. government obligations        | 1,392,957            | 1,300,221            |
| Common trust funds                 | 4,305,156            | 3,875,401            |
| Commodities                        | 233,686              | 95,767               |
| Corporate bonds                    | 1,171,176            | 838,585              |
| Fixed income mutual funds          | 948,834              | 1,107,680            |
| Equity mutual funds                | 2,518,030            | 2,619,021            |
| Common stock                       | 11,544,979           | 11,790,972           |
| REITS                              | 251,575              | 194,067              |
| Alternative investments            | <u>393,454</u>       | <u>218,410</u>       |
|                                    | 23,489,237           | 23,353,573           |
| Other:                             |                      |                      |
| Community development loans        | <u>1,584,831</u>     | <u>1,952,420</u>     |
|                                    | <u>\$ 25,074,068</u> | <u>\$ 25,305,993</u> |

Other investments are carried at cost and represent the Diocese's investment in community development initiatives in the form of interest-bearing loans that have been approved by the Diocesan trustees. The Diocese is authorized by the Trustees to loan up to 10% of its unrestricted endowment fund in fixed rate loans for community development purposes. These loans are considered investments for purposes of the Diocese's investment spending policy and bear interest at 2.5%.

#### Investment Income (Loss)

Investment income (loss) consisted of the following for the years ended December 31:

|                              | <u>2012</u>         |                   |                     | <u>2011</u>         |                     |                     |
|------------------------------|---------------------|-------------------|---------------------|---------------------|---------------------|---------------------|
|                              | <u>Unrestricted</u> | <u>Restricted</u> | <u>Total</u>        | <u>Unrestricted</u> | <u>Restricted</u>   | <u>Total</u>        |
| Interest and dividend income | \$ 214,333          | \$ 123,151        | \$ 337,484          | \$ 184,850          | \$ 139,474          | \$ 324,324          |
| Gain (loss) on investments   | 610,413             | 598,824           | 1,209,237           | (197,115)           | (294,759)           | (491,874)           |
| Investment related expenses  | <u>(134,772)</u>    | <u>(59,776)</u>   | <u>(194,548)</u>    | <u>(182,482)</u>    | <u>(53,858)</u>     | <u>(236,340)</u>    |
|                              | <u>\$ 689,974</u>   | <u>\$ 662,199</u> | <u>\$ 1,352,173</u> | <u>\$ (194,747)</u> | <u>\$ (209,143)</u> | <u>\$ (403,890)</u> |

In addition to the investment expenses stated above, the Operating Fund incurred investment consulting fees of approximately \$32,000 in 2012 and the Diocese Trustees Funds incurred investment related expenses of approximately \$83,000 in 2012.

The Diocese has adopted an investment spending policy under which 5% of the average market value of unrestricted investment balances over the previous 13 calendar quarters is allocated to fund operating activities. Investment earnings on restricted balances are allocated for expenditures based on donor restrictions or added to the restricted net assets.

In 2012 and 2011, the Diocese drew more than standard spending policy due to additional approved expenditures by the Diocesan Trustees, as well as, an error which had been identified in the formula for computing the spending policy calculation in prior years. The additional amount drawn in 2012 and 2011 was approximately \$300,000 and \$250,000, respectively.

## 5. FAIR VALUE MEASUREMENTS

Fair value of the Diocese's U.S. government obligations, fixed income mutual funds, equity mutual funds, common stocks and REITS is determined based on quoted market prices.

Fair value of the Diocese's commodities and corporate bonds is determined by entering standard inputs into a pricing model. These inputs include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, and industry and economic events. Fair value of the Diocese's common trust funds is determined using the closing price reported by the primary market in which they are traded and translated at each valuation date from the local currency into U.S. dollars using the mean between the bid and ask market exchange rates from WM/Reuters for such currencies, when applicable.

Alternative investments consist of funds that are stated at fair market value utilizing the net asset valuations provided by the underlying fund managers.

The following are measured at fair value at December 31, 2012:

|                             | <u>Level 1 Inputs</u> | <u>Level 2 Inputs</u> | <u>Level 3 Inputs</u> |
|-----------------------------|-----------------------|-----------------------|-----------------------|
| U.S. government obligations | \$ 1,392,957          | \$ -                  | \$ -                  |
| Common trust funds          | -                     | 4,305,156             | -                     |
| Commodities                 | -                     | 233,686               | -                     |
| Corporate bonds             | -                     | 1,171,176             | -                     |
| Fixed income mutual funds   | 948,834               | -                     | -                     |
| Equity mutual funds         | 2,518,030             | -                     | -                     |
| Common stocks               | 11,544,979            | -                     | -                     |
| REITS                       | 251,575               | -                     | -                     |
| Alternative investments     | -                     | 393,454               | -                     |
|                             | <u>\$ 16,656,375</u>  | <u>\$ 6,103,472</u>   | <u>\$ -</u>           |

The following are measured at fair value at December 31, 2011:

|                             | <u>Level 1 Inputs</u> | <u>Level 2 Inputs</u> | <u>Level 3 Inputs</u> |
|-----------------------------|-----------------------|-----------------------|-----------------------|
| U.S. government obligations | \$ 1,300,221          | \$ -                  | \$ -                  |
| Common trust funds          | -                     | 3,875,401             | -                     |
| Commodities                 | -                     | 95,767                | -                     |
| Corporate bonds             | -                     | 838,585               | -                     |
| Fixed income mutual funds   | 1,107,680             | -                     | -                     |
| Equity mutual funds         | 2,619,021             | -                     | -                     |
| Common stocks               | 11,790,972            | -                     | -                     |
| REITS                       | 194,067               | -                     | -                     |
| Alternative investments     | -                     | 218,410               | -                     |
|                             | <u>\$ 17,011,961</u>  | <u>\$ 5,028,163</u>   | <u>\$ -</u>           |

Investments in common trust funds include an investment of \$4,305,155 and \$3,875,401 as of December 31, 2012 and 2011, respectively, in Silchester International Investors International Value Equity Trust, which is a privately offered trust investing in a diversified portfolio of equity securities incorporated in any country other than the United States. The investment objective of this fund is long-term capital gains and income. Redemptions are permitted on a monthly basis, with notification of 6 business days. As of December 31, 2012 and 2011, the Diocese had no unfunded commitments related to this investment.

## 5. FAIR VALUE MEASUREMENTS (Continued)

Alternative investments include an investment of \$393,454 and \$218,410 as of December 31, 2012 and 2011, respectively, in Excelsior Multi-Strategy Hedge Fund of Funds, which is a non-diversified, closed-ended management investment company incorporated in Delaware. The investment objective of this fund is to seek capital appreciation. The fund pursues its investment objectives primarily through investing substantially all its assets in additional funds of funds. As of December 31, 2012 and 2011 the Diocese had no unfunded commitments relating to this alternative investment. The redemption liquidity is quarterly per tender offer authorized by the board of directors.

## 6. LAND, BUILDINGS AND EQUIPMENT

Land, buildings and equipment consisted of the following at December 31:

|                                     | <u>2012</u>         | <u>2011</u>         |
|-------------------------------------|---------------------|---------------------|
| Land                                | \$ 169,600          | \$ 169,600          |
| Buildings and building improvements | 2,487,873           | 2,482,261           |
| Equipment                           | <u>142,332</u>      | <u>150,249</u>      |
|                                     | 2,799,805           | 2,802,110           |
| Less: Accumulated depreciation      | <u>(1,703,752)</u>  | <u>(1,662,095)</u>  |
|                                     | <u>\$ 1,096,053</u> | <u>\$ 1,140,015</u> |

## 7. FUNDS HELD FOR OTHERS

The Diocese serves as the custodian of funds held for the benefit of certain congregations and other organizations. These funds are invested by the Diocese, with investment income allocated to the benefit of each congregation or organization. The total amount held for others was \$6,528,073 and \$6,393,596 at December 31, 2012 and 2011, respectively.

## 8. PENSION AND POSTRETIREMENT BENEFIT PLANS

### Pension 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. Contributions of \$76,003 and \$71,861 were made by the Diocese under the terms of this plan in 2012 and 2011, respectively.

The Diocese sponsors a defined contribution plan for full-time lay employees. Under the terms of this plan, the Diocese contributes 12% to 18% of each employee's salary to the plan. In addition, employees are allowed to make elective tax-deferred contributions. Contributions of \$59,160 and \$51,297 were made by the Diocese under the terms of this plan in 2012 and 2011, respectively.

**8. PENSION AND POSTRETIREMENT BENEFIT PLANS (Continued)**

**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 recognized under these plans totaled \$132,119 and \$122,884 for the years ended December 31, 2012 and 2011, respectively.

**9. SUBSEQUENT EVENTS**

Subsequent events have been evaluated through August 13, 2013, which is the date the financial statements were available to be issued.

## EPISCOPAL DIOCESE OF ROCHESTER

### COMPARISON OF BUDGET TO ACTUAL OPERATING REVENUE AND EXPENSES FOR THE YEAR ENDED DECEMBER 31, 2012

|                                       | Budget Approved<br>by Diocesan<br>Convention as Revised<br>(Unaudited) | Actual              | Actual<br>Over/Under<br>Budget |
|---------------------------------------|------------------------------------------------------------------------|---------------------|--------------------------------|
| Revenue:                              |                                                                        |                     |                                |
| Parish support                        | \$ 1,021,901                                                           | \$ 1,014,977        | \$ (6,924)                     |
| Investment spending policy            | 1,496,673                                                              | 1,232,799           | (263,874)                      |
| Interest on mortgages and loans       | 84,000                                                                 | 83,944              | (56)                           |
| Other                                 | 3,000                                                                  | 3,000               | -                              |
|                                       | <u>2,605,574</u>                                                       | <u>2,334,720</u>    | <u>(270,854)</u>               |
| Expenses:                             |                                                                        |                     |                                |
| Congregational Development            | 421,390                                                                | 416,519             | (4,871)                        |
| Mission within the Diocese            | 239,000                                                                | 227,209             | (11,791)                       |
| Mission outside the Diocese           | 231,445                                                                | 231,592             | 147                            |
| Clergy and Lay Benefits               | 163,600                                                                | 162,707             | (893)                          |
| Leadership Development                | 54,000                                                                 | 47,895              | (6,105)                        |
| Communications                        | 60,000                                                                 | 22,335              | (37,665)                       |
| Governance, Committees and Missioners | 132,500                                                                | 116,134             | (16,366)                       |
| Support staff                         | 442,774                                                                | 424,284             | (18,490)                       |
| Executive staff                       | 522,989                                                                | 494,935             | (28,054)                       |
| Office expense                        | 177,000                                                                | 144,915             | (32,085)                       |
|                                       | <u>2,444,698</u>                                                       | <u>2,288,525</u>    | <u>(156,173)</u>               |
| Total operating expenses              |                                                                        |                     |                                |
| Non-operating expense                 | <u>160,876</u>                                                         | <u>179,865</u>      | <u>18,989</u>                  |
| Excess of revenue over expenses       | <u>\$ -</u>                                                            | <u>\$ (133,670)</u> | <u>\$ (133,670)</u>            |

The accompanying notes are an integral part of this exhibit.