

Financial Statements and Report of  
Independent Certified Public Accountants

**Archdiocese of Philadelphia,  
Office of Catholic Education  
Administration Account**

June 30, 2015 and 2014

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## Report of Independent Certified Public Accountants

To the Secretary of Catholic Education  
Archdiocese of Philadelphia

Grant Thornton LLP  
Two Commerce Square  
2001 Market St., Suite 700  
Philadelphia, PA 19103  
T 215.561.4200  
F 215.561.1066  
[GrantThornton.com](http://GrantThornton.com)  
[linkd.in/GrantThorntonUS](https://www.linkedin.com/company/grantthorntonus)  
[twitter.com/GrantThorntonUS](https://twitter.com/GrantThorntonUS)

### **Report on the financial statements**

We have audited the accompanying financial statements of the Archdiocese of Philadelphia, Office of Catholic Education Administration Account (“OCE”), which comprise the statements of financial position as of June 30, 2015 and 2014, and the related statements of activities and changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

### **Management’s responsibility for the financial statements**

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

### **Auditor’s responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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 OCE’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 OCE’s internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

**Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Archdiocese of Philadelphia, Office of Catholic Education Administration Account as of June 30, 2015 and 2014, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

**Emphasis of matter**

We draw attention to Note A to the financial statements, which describes the legal structure of OCE within the Archdiocese of Philadelphia. Our opinion is not modified with respect to this matter.

*Grant Thornton LLP*

Philadelphia, Pennsylvania

November 30, 2015

Archdiocese of Philadelphia, Office of Catholic Education  
Administration Account

**STATEMENTS OF FINANCIAL POSITION**

June 30,

ASSETS	2015	2014
Cash and cash equivalents, including amounts held by affiliate	\$ 2,541,795	\$ 3,448,593
Accounts receivable	412,099	55,049
Due from other Archdiocesan entities (Note I)	44,902	18,409
Other assets	53,922	82,435
Investments (Note C)	8,895,861	9,064,142
Beneficial interest in perpetual trust	28,505,186	29,684,809
 Total assets	 \$ 40,453,765	 \$ 42,353,437
 LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable	\$ 101,012	\$ 180,725
Accrued vacation	92,432	86,098
Accrued severance	24,696	28,994
Accrued salaries	20,894	29,295
Due to other Archdiocesan entities (Note I)	33,986	147,226
Deferred revenue	13,754	14,894
 Total liabilities	 286,774	 487,232
Net assets		
Unrestricted	1,159,997	1,239,409
Unrestricted - designated	1,188,444	1,404,197
Temporarily restricted (Note E)	6,545,339	6,794,038
Permanently restricted (Note F)	31,273,211	32,428,561
 Total net assets	 40,166,991	 41,866,205
 Total liabilities and net assets	 \$ 40,453,765	 \$ 42,353,437

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

Archdiocese of Philadelphia, Office of Catholic Education  
Administration Account

**STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS**

Year ended June 30, 2015

	Unrestricted	Unrestricted - designated	Temporarily restricted	Permanently restricted	Total
Revenues					
Subsidies					
Office of Catholic Education - Diocesan High Schools					
Operations Account	\$ 3,699,998	\$ -	\$ -	\$ -	\$ 3,699,998
Schools of Special Education	100,000	-	-	-	100,000
Contributions					
Archdiocesan Educational Fund	560,000	-	-	-	560,000
Donations	1,043,220	-	564,733	-	1,607,953
Contributed services (Note J)	49,271	-	-	-	49,271
Program revenues	891,651	-	-	-	891,651
Investment income	19,425	23,600	122,608	18,687	184,320
Net realized and unrealized gains on investments	-	8,553	36,024	5,586	50,163
Change in beneficial interest in perpetual trust	-	-	-	(1,179,623)	(1,179,623)
Distribution of beneficial interest in perpetual trust	-	-	1,450,000	-	1,450,000
Other revenue	84,936	-	-	-	84,936
Funds with deficiencies (Note G)	(35,157)	-	35,157	-	-
Net assets released from restrictions	2,705,127	(247,906)	(2,457,221)	-	-
Total revenues	9,118,471	(215,753)	(248,699)	(1,155,350)	7,498,669
Expenses					
Salaries and benefits	3,862,260	-	-	-	3,862,260
Cost of sales	12,663	-	-	-	12,663
Purchased services	2,522,082	-	-	-	2,522,082
Intradiocesan expenses	322,130	-	-	-	322,130
Support expenses	2,478,748	-	-	-	2,478,748
Total expenses	9,197,883	-	-	-	9,197,883
Change in net assets	(79,412)	(215,753)	(248,699)	(1,155,350)	(1,699,214)
Net assets, beginning of year	1,239,409	1,404,197	6,794,038	32,428,561	41,866,205
Net assets, end of year	\$ 1,159,997	\$ 1,188,444	\$ 6,545,339	\$ 31,273,211	\$ 40,166,991

The accompanying notes are an integral part of this financial statement.

Archdiocese of Philadelphia, Office of Catholic Education  
Administration Account

**STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS**

Year ended June 30, 2014

	<u>Unrestricted</u>	<u>Unrestricted - designated</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Revenues					
Subsidies					
Office of Catholic Education - Diocesan High Schools					
Operations Account	\$ 3,100,386	\$ -	\$ -	\$ -	\$ 3,100,386
Schools of Special Education	100,000	-	-	-	100,000
Contributions					
Archdiocesan Educational Fund	760,000	-	-	-	760,000
Donations	30,775	-	586,187	-	616,962
Contributed services (Note J)	122,781	-	-	-	122,781
Program revenues	679,983	-	-	-	679,983
Investment income	29,518	27,653	126,940	20,432	204,543
Net realized and unrealized gains on investments	-	184,156	841,110	136,283	1,161,549
Change in beneficial interest in perpetual trust	-	-	-	2,637,992	2,637,992
Distribution of beneficial interest in perpetual trust	-	-	1,501,000	-	1,501,000
Other revenue	154,887	-	-	-	154,887
Funds with deficiencies (Note G)	148,979	-	(148,979)	-	-
Net assets released from restrictions	<u>1,562,882</u>	<u>(86,846)</u>	<u>(1,476,036)</u>	<u>-</u>	<u>-</u>
Total revenues	<u>6,690,191</u>	<u>124,963</u>	<u>1,430,222</u>	<u>2,794,707</u>	<u>11,040,083</u>
Expenses					
Salaries and benefits	3,152,876	-	-	-	3,152,876
Cost of sales	25,327	-	-	-	25,327
Purchased services	888,621	-	-	-	888,621
Intradiocesan expenses	318,258	-	-	-	318,258
Support expenses	<u>2,022,195</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,022,195</u>
		<u>-</u>			
Total expenses	<u>6,407,277</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,407,277</u>
Change in net assets	282,914	124,963	1,430,222	2,794,707	4,632,806
Net assets, beginning of year	<u>956,495</u>	<u>1,279,234</u>	<u>5,363,816</u>	<u>29,633,854</u>	<u>37,233,399</u>
Net assets, end of year	<u>\$ 1,239,409</u>	<u>\$ 1,404,197</u>	<u>\$ 6,794,038</u>	<u>\$ 32,428,561</u>	<u>\$ 41,866,205</u>

The accompanying notes are an integral part of this financial statement.

Archdiocese of Philadelphia, Office of Catholic Education  
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**STATEMENTS OF CASH FLOWS**

Year ended June 30,

	2015	2014
Cash flows from operating activities		
Change in net assets	\$ (1,699,214)	\$ 4,632,806
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Net realized and unrealized gains on investments	(50,163)	(1,161,549)
Change in beneficial interest in perpetual trust	1,179,623	(2,637,992)
Changes in operating assets and liabilities		
Accounts receivable	(357,050)	(22,111)
Due from other Archdiocesan entities	(26,493)	77,612
Other assets	28,513	(74,307)
Accounts payable	(79,713)	9,198
Accrued vacation	6,334	2,798
Accrued severance	(4,298)	(143,663)
Accrued salaries	(8,401)	13,432
Due to other Archdiocesan entities	(113,240)	39,140
Deferred revenue	(1,140)	(42,498)
Net cash (used in) provided by operating activities	(1,125,242)	692,866
Cash flows from investing activities		
Purchase of investments	(129,835)	(163,277)
Proceeds from sale of investments	348,279	386,973
Net cash provided by investing activities	218,444	223,696
Net (decrease) increase in cash and cash equivalents, including amounts held by affiliate	(906,798)	916,562
Cash and cash equivalents, including amounts held by affiliate, beginning of year	3,448,593	2,532,031
Cash and cash equivalents, including amounts held by affiliate, end of year	\$ 2,541,795	\$ 3,448,593

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

**NOTES TO FINANCIAL STATEMENTS**

June 30, 2015 and 2014

NOTE A - NATURE OF OPERATIONS

The accompanying financial statements of the Archdiocese of Philadelphia, Office of Catholic Education Administration Account (“OCE”) include the Office of Catholic Education and the departments of elementary and secondary schools, the Office of Catechetical Formation and Educational Financial Services. The financial statements exclude certain entities of the Archdiocese of Philadelphia, which relate to OCE but are considered separate reporting entities. These entities are as follows:

- Diocesan High Schools
- Individual High School Presidents’ Accounts
- Schools of Special Education
- Office for Financial Services
- Trustee Account of the Archdiocese of Philadelphia for Estates and Trusts
- Archdiocesan Educational Fund

OCE is considered to be a component of the Archdiocese of Philadelphia and not a separate legal entity. Effective September 1, 2012, the Archdiocese of Philadelphia entered into an agreement with Faith in the Future Foundation (“FIF”). The agreement is for the period of five school years and shall automatically renew for successive three-year periods unless prior written notification is provided 90 days before the scheduled expiration date. Pursuant to the aforementioned agreement, FIF assumes strategic and operational management of the 17 Catholic secondary schools and the four individual Schools of Special Education and provides certain financial assistance to the schools. OCE has primary responsibility for, and FIF has oversight and approval responsibility over, school operations. The Secretary for Catholic Education/Chief Operating Officer of OCE reports directly to FIF’s Chief Executive Officer. All facilities continue to be owned by the Archdiocese of Philadelphia.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis. Net assets and their revenues, expenses, gains and losses are classified into three categories, based on the existence or absence of donor-imposed restrictions. The categories are temporarily restricted, permanently restricted and unrestricted net assets.

Temporarily restricted net assets include gifts, trusts, income and gains which have either a time or use restriction but which may ultimately be expended. Since endowment investment income and net realized and unrealized gains and losses may eventually be spent by OCE, such earnings are recorded in the financial statements as temporarily restricted net assets, unless donor restricted for the corpus, until transferred to unrestricted net assets.

Permanently restricted net assets include the historical dollar amounts of gifts, which require by donor restriction that the corpus be invested in perpetuity and only the investment income be made available for operations in accordance with donor restrictions. Investment income and net realized and unrealized gains and losses, if permanently restricted by the donor, are included in permanently restricted net assets.

(Continued)

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Unrestricted net assets are free from donor-imposed restrictions and are all the remaining net assets of OCE.

2. Revenue Recognition

Various programs for the benefit of the schools are operated by OCE. Revenues from the programs are reported gross in the statement of activities and changes in net assets, and expenses are reported in the appropriate category of administration expenses when the services are performed.

Cash contributions are recorded as revenue when received. Unconditional promises to give are recorded at their fair value when OCE is notified of these gifts. Conditional promises to give are recognized when the conditions are substantially met. Donor-restricted gifts which are received and expended within the same year are reported as unrestricted revenues.

Gifts of cash and other assets are recorded as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the accompanying statement of activities and changes in net assets as net assets released from restrictions.

3. Uses of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make significant estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

4. Cash and Cash Equivalents, Including Amounts Held by Affiliate

Cash and cash equivalents, including amounts held by affiliate represent demand deposits and other investments with a maturity date of three months or less. The carrying amount approximates fair value.

OCE maintains cash balances with financial institutions that at times may exceed Federal Deposit Insurance Corporation limits. Management does not believe the credit risk related to these deposits to be significant.

(Continued)

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

5. Investments

On April 30, 2015, Trustee Accounts previously held in the Non-Pension Assets Portfolio (the "NPAP") were liquidated and re-invested with two publicly traded SEI Catholic Values public mutual funds. The Catholic Values Equity Fund and the Catholic Values Fixed Income Fund ("Catholic Values Funds") provide Catholic institutions with high quality products that align with their core values, without sacrificing diversification or return potential. Specifically, the funds align with the investment directives set forth by the United States Conference of Catholic Bishops ("USCCB"). The Archdiocese of Philadelphia appointed SEI Private Trust Company to act as custodian (the "Custodian") of the Trustee Accounts. The investment in the Trustee Accounts and other investments are reported at fair value.

Realized gains and losses are reported to the participant monthly. Gains and losses created at the participant level due to sales are recorded in the specific participant accounts. Unrealized gains and losses are included in the statements of activities and changes in net assets as net appreciation or depreciation in the fair value of investments.

6. Beneficial Interest in Perpetual Trust

OCE is the sole beneficiary of the income of a trust established by Francis W. Sullivan held in perpetuity by a third party. The supporting perpetual trust requires the income to be paid to OCE. The beneficial interest in perpetual trust is recorded at the fair value of the assets. At June 30, 2015, the allocable fair value of the net assets of the trust is \$28,505,186. The underlying investments of the beneficial interest in perpetual trust consist of cash, government obligations, corporate obligations, mutual funds, mortgage-backed securities and equity securities. OCE receives statements from the trustees, which detail the fair value of each investment in the perpetual trust.

NOTE C - INVESTMENTS

The investments in the Trustee Accounts and other investments are reported at fair value and consist of the following:

*Catholic Values Equity Fund (or "fund")* - Invests in common stocks and is managed by SEI.

*Catholic Values Fixed Income Fund (or "fund")* - Invests in mutual funds, corporate obligations, United States Treasury obligations and municipal obligations and is managed by SEI.

*Liquidity Sub-Account (or "fund")* - Investments are liquid in nature and invests in short-duration U.S. government bonds.

Account holders have the option of six asset classifications in which to invest. The options include a short-duration U.S. government bond fund, a 100% fixed income bond fund and four equity funds with varying fixed income to equity mixes of 30/70, 50/50, 60/40 or 70/30. The Investment Committee of the Archdiocese of Philadelphia ("Investment Committee") has primary responsibility for determining fixed income to equity mix. The asset mix of the mutual funds is SEI's responsibility.

(Continued)

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE C - INVESTMENTS - Continued

At June 30, 2015, OCE's investments are summarized and classified as follows:

	Unrestricted - designated	Temporarily restricted	Permanently restricted	Total
<u>2015</u>				
SEI mutual funds	\$ <u>1,233,187</u>	\$ <u>4,894,649</u>	\$ <u>2,768,025</u>	\$ <u>8,895,861</u>

At June 30, 2015, OCE held the following categories of investments:

Catholic Values Equity Fund	\$ 5,304,170
Catholic Values Fixed Income Fund	<u>3,591,691</u>
 Total ownership	 \$ <u>8,895,861</u>

Prior to April 30, 2015, the investment in the Trustee Accounts consisted of investments in the NPAP and other investment accounts. For administrative and other needs, the Archdiocese of Philadelphia formed the NPAP to pool together certain investments in order to more efficiently manage the investments of various entities and related organizations within the Archdiocese of Philadelphia. The investments in the NPAP were held by a custodian and were managed based on sub-accounts as follows:

*Equity Sub-Account (or "fund")* - Invested in common stocks and was managed by multiple investment managers.

*Fixed Income Sub-Account (or "fund")* - Invested in mutual funds, corporate obligations, United States Treasury obligations and municipal obligations and was managed by multiple investment managers.

*Liquidity Sub-Account (or "fund")* - Investments were liquid in nature and were used to buy and sell units of the equity and fixed income funds or for expected short-term needs.

The Trustee Account is unitized on a periodic basis to allow for the investment, at unit value, by entities in the NPAP. OCE's investment in the Trustee Accounts is stated at unit value.

The Investment Committee has primary responsibility for determining the asset investment allocations to be used. Management is responsible for ensuring that asset investment allocations among the funds are maintained as determined by the Investment Committee.

At June 30, 2014, OCE's investments are summarized and classified as follows:

	Unrestricted - designated	Temporarily restricted	Permanently restricted	Total
<u>2014</u>				
Archdiocese of Philadelphia NPAP	\$ <u>1,329,197</u>	\$ <u>4,991,193</u>	\$ <u>2,743,752</u>	\$ <u>9,064,142</u>

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE D - PENSION PLAN

1. Lay Employees' Retirement Plan - Frozen Effective June 30, 2014

Through June 30, 2014, the eligible lay employees of OCE were covered under the Archdiocese of Philadelphia Lay Employees' Retirement Plan (the "Plan"), which is a defined benefit pension plan covering substantially all lay employees of the Archdiocese of Philadelphia, based on age and service requirements. The Plan is administered by the Trustees of the Plan. OCE made annual contributions to the Plan at an average rate of 4.0% and 7.5% of the salaries of eligible teachers and non-teachers for the years ended June 30, 2015 and 2014, respectively. The amount expensed by OCE for contributions to the Plan was \$113,074 and \$127,546 for the years ended June 30, 2015 and 2014, respectively. The expense of such contributions is included in employee benefits. Separate accounts for vested benefits and pension fund assets are not maintained for each institution.

2. Archdiocese of Philadelphia 403(b) Retirement Plan

Effective July 1, 2014, the Archdiocese of Philadelphia established a 403(b) defined contribution plan. Under the 403(b) plan, and subject to statutory limits, all employees at least 18 years of age are immediately eligible to make voluntary deferred salary contributions into the 403(b) plan.

Employer contributions, which cover employees meeting the eligibility requirements below, are discretionary. The following are the eligibility requirements for the employer contributions:

*Grandfathered Employees* - Any employee who was accruing benefits as an active participant in the Lay Employees' Retirement Plan as of its freeze date of June 30, 2014 is a grandfathered employee and will be eligible to receive employer contributions beginning with the first payroll on or after July 1, 2014. A grandfathered 10-month employee will be eligible to receive employer contributions beginning with the first payroll on or after September 1, 2014.

*Non-Grandfathered Employees* - Non-grandfathered employees are eligible to receive the employer contribution beginning with the first payroll coinciding with or immediately following the completion of 1,000 hours of service during the 18-month period beginning July 1, 2014 through December 31, 2015. The employee must also have attained at least 18 years of age to be eligible. For a non-grandfathered employee hired prior to July 1, 2014 who does not meet the eligibility requirements for an employer contribution in the time frame described above, the period for determining whether or not one meets the 1,000-hour service requirement will shift to the calendar year beginning January 1, 2016.

*Vesting* - Vesting in employer contributions to a 403(b) plan account will be immediate for any grandfathered employee who has completed 12 months of service as of June 30, 2014. Vesting in employer contributions for all other employees will take place after the completion of 12 months of service.

In fiscal 2015, OCE's contribution rate was 5.0% of base salary for eligible employees. The contributions into the 403(b) plan totaled \$141,342 for the year ended June 30, 2015.

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**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE E - TEMPORARILY RESTRICTED NET ASSETS

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

	<u>2015</u>	<u>2014</u>
Tuition assistance/scholarships	\$ 5,026,618	\$ 5,244,106
Programs/grants	1,267,515	1,188,119
Scholarships/programs	241,999	298,279
Accumulated earnings in excess of spending of endowments:		
Tuition assistance/scholarships	6,950	6,631
Other	<u>2,257</u>	<u>56,903</u>
	<u>\$ 6,545,339</u>	<u>\$ 6,794,038</u>

During 2015 and 2014, net assets were released from donor restrictions by incurring expenses satisfying the restricted purpose of \$2,705,127 and \$1,562,882, respectively.

NOTE F - PERMANENTLY RESTRICTED NET ASSETS

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

	<u>2015</u>	<u>2014</u>
Programs/grants (beneficial interest in trust)	\$ 28,505,186	\$ 29,684,809
Endowment net assets		
Tuition assistance/scholarships	2,700,004	2,675,731
Other	<u>68,021</u>	<u>68,021</u>
	<u>\$ 31,273,211</u>	<u>\$ 32,428,561</u>

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE G - ENDOWMENTS

OCE's endowments consist of donor-restricted endowment funds established for a variety of purposes. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

1. Interpretation of Relevant Law

In accordance with Commonwealth of Pennsylvania Act 141, and unless directed otherwise by the donor, OCE classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment; (b) the original value of subsequent gifts to the permanent endowment; and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by OCE in a manner consistent with the standard of prudence prescribed by relevant law. OCE does not release any portion of the permanently restricted funds. Pennsylvania law permits the Archdiocese of Philadelphia to release a percentage, which is elected annually, of the market value of its endowment funds into unrestricted income. The spending rate percentage, between 2% and 7%, is applied to the three-year average of the market value of the endowment funds' assets.

2. Return Objectives and Risk Parameters

OCE has adopted investment policies established by the Archdiocese of Philadelphia's investment committee and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity. Under this policy, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of plus-3% over the consumer price index while assuming a moderate level of investment risk. OCE expects its endowment funds, over time, to provide an average rate of return of approximately 5% annually. Actual returns in any given year may vary from that amount.

3. Spending Policy

In accordance with state law, net realized and unrealized gains on permanently restricted investments are included as temporarily restricted net assets, unless subject to donor restrictions for the corpus. Commonwealth of Pennsylvania law permits OCE to adopt a spending policy for endowment earnings, subject to certain limitations. OCE follows the total return concept of endowment investment and spending. Under this concept, a prudent amount of appreciation earned on the investments may be spent in the event that the interest and dividends earned are insufficient to meet that period's spending rate. The Archdiocese of Philadelphia's spending policy for the years ended June 30, 2015 and 2014 allowed for a 3% draw of the three-year average market value of the permanently restricted endowments, unless directed otherwise by the donor.

(Continued)

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE G - ENDOWMENTS - Continued

4. Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the original gift amount maintained as permanently restricted net assets. Deficiencies of this nature totaled \$(35,157) and \$148,979 as of June 30, 2015 and 2014, respectively. Such deficiencies are recorded as unrestricted net assets. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions.

As of June 30, 2015 and 2014, \$2,768,025 and \$2,743,752, respectively, in donor-restricted endowment funds were recorded within permanently restricted net assets.

Changes in endowment net assets for the year ended June 30, 2015:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, June 30, 2014	\$ -	\$ 63,534	\$ 2,743,752	\$ 2,807,286
Investment income	-	30,543	18,687	49,230
Net appreciation (realized and unrealized gains)	<u>-</u>	<u>10,018</u>	<u>5,586</u>	<u>15,604</u>
Total investment return	-	40,561	24,273	64,834
Contributions	-	-	-	-
Appropriation of endowment assets for expenditure	-	(130,045)	-	(130,045)
Funds with deficiencies	<u>-</u>	<u>35,157</u>	<u>-</u>	<u>35,157</u>
Endowment net assets, June 30, 2015	<u>\$ -</u>	<u>\$ 9,207</u>	<u>\$ 2,768,025</u>	<u>\$ 2,777,232</u>

(Continued)

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**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE G - ENDOWMENTS - Continued

Changes in endowment net assets for the year ended June 30, 2014:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, June 30, 2013	\$ -	\$ 43,605	\$ 2,587,037	\$ 2,630,642
Investment income	-	33,334	20,432	53,766
Net appreciation (realized and unrealized gains)	<u>-</u>	<u>222,331</u>	<u>136,283</u>	<u>358,614</u>
Total investment return	-	255,665	156,715	412,380
Contributions	-	-	-	-
Appropriation of endowment assets for expenditure	-	(86,757)	-	(86,757)
Funds with deficiencies	<u>-</u>	<u>(148,979)</u>	<u>-</u>	<u>(148,979)</u>
Endowment net assets, June 30, 2014	<u>\$ -</u>	<u>\$ 63,534</u>	<u>\$ 2,743,752</u>	<u>\$ 2,807,286</u>

NOTE H - INCOME TAXES

As part of the Archdiocese of Philadelphia, OCE has received exempt status from federal taxation under Section 501(c)(3) of the Internal Revenue Code.

OCE follows the accounting guidance for uncertainties in income tax positions which requires that a tax position be recognized or derecognized based on a "more likely than not" threshold. This applies to positions taken or expected to be taken in a tax return. OCE does not believe its financial statements include any material uncertain tax positions. As of June 30, 2015, the OCE tax years ended June 30, 2012 through June 30, 2014 for federal tax jurisdiction remain open to examination.

NOTE I - RELATED PARTY TRANSACTIONS

As of June 30, amounts due from related organizations consisted of the following:

	<u>2015</u>	<u>2014</u>
Catholic Cemeteries	\$ -	\$ 115
Individual high schools	11,902	-
Combined Diocesan High Schools	<u>33,000</u>	<u>18,294</u>
	<u>\$ 44,902</u>	<u>\$ 18,409</u>

(Continued)

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**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE I - RELATED PARTY TRANSACTIONS - Continued

As of June 30, amounts due to related organizations consisted of the following:

	2015	2014
Office for Communications	\$ 34	\$ 143
Lay Employees' Retirement Plan	-	110,657
Office of Child and Youth Protection	11,270	-
Office for General Services	2,378	-
Diocesan High Schools	13,367	16,207
Bishop Shanahan High School	538	-
Office of Human Resources	3,915	-
Office for Financial Services	2,484	20,219
	\$ 33,986	\$ 147,226

OCE receives subsidies from the Diocesan High Schools Operations Account. Subsidies totaled \$3,699,998 (\$3,399,998 for administration costs and \$300,000 for marketing expense) and \$3,100,386 (\$2,820,000 for administration costs and \$280,386 for marketing expense) for the years ended June 30, 2015 and 2014, respectively.

During both the fiscal years ended June 30, 2015 and 2014, OCE charged the Schools of Special Education \$100,000 for management services, which amounts are included in subsidies revenue.

Cash and cash equivalents include \$2,381,488 and \$2,824,576 at June 30, 2015 and 2014, respectively, held in trust funds maintained by the Office for Financial Services of the Archdiocese of Philadelphia. There are no conditions restricting the withdrawal of these funds.

NOTE J - CONTRIBUTED SERVICES

The value of contributed services performed by members of religious groups is based on the lay equivalent salaries of personnel performing similar duties, less the stipend allowances and housing allowances paid for the religious personnel. The value of contributed services is included as revenue and, correspondingly, charged to expenditures.

The following is a schedule of contributed services as of June 30:

	2015	2014
Salaries and benefits - lay equivalent value of religious services	\$ 105,436	\$ 228,277
Expended for religious services	(56,165)	(105,496)
Salaries, related employee benefits and faculty house expenses	\$ 49,271	\$ 122,781

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

**NOTE K - FAIR VALUE MEASUREMENTS**

Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 820, *Fair Value Measurements and Disclosures*, establishes a single authoritative definition of fair value, sets a framework for measuring fair value, and requires additional disclosures about fair value measurements. The framework 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 or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under ASC 820 are described as follows:

- Level 1 Quoted prices in active markets for identical assets or liabilities.
- Level 2 Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the same term of the assets or liabilities.
- Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

A financial instrument’s 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 used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Fair value calculations may not be indicative of net realizable value or reflective of future fair values. Furthermore, although OCE 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 financial instruments could result in a different fair value measurement at the reporting date.

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**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE K - FAIR VALUE MEASUREMENTS - Continued

Fair value measurements of investments in entities that calculate the net asset value (“NAV”) per share or its equivalent as of June 30, 2015 and 2014 are as follows:

	Fair value		Unfunded	Redemption	Redemption
	2015	2014	commitments	frequency	notice
					period
Archdiocese of Philadelphia NPAP <sup>(a)</sup>	\$ <u>          -</u>	\$ <u>9,064,142</u>	\$ -	Daily	1 day

<sup>(a)</sup> A pooled investment portfolio comprised of equity and fixed income securities. The primary objective of the NPAP was preservation of capital while reducing, to the greatest extent possible, the possibility of loss. The Investment strategy and long-term asset allocation for the NPAP took into consideration the specific spending requirements and the present and future needs of the Archdiocese of Philadelphia and its respective participating Ecclesiastical Organizations. Therefore, the desired minimum rate of return was equal to the Consumer Price Index (“CPI”) plus three percent (3%) on an annualized basis. The fair values were estimated using the NAV per share of the investments.

The following table presents the fair values of the investments held by OCE by level within the fair value hierarchy, as of June 30:

	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total fair value
<u>2015</u>				
Assets				
Investments:				
SEI mutual funds	\$ 8,895,861	\$ -	\$ -	\$ 8,895,861
Beneficial interest in perpetual trust	<u>          -</u>	<u>          -</u>	<u>28,505,186</u>	<u>28,505,186</u>
Total of assets at June 30, 2015	<u>\$ 8,895,861</u>	<u>\$ -</u>	<u>\$ 28,505,186</u>	<u>\$ 37,401,047</u>
<u>2014</u>				
Assets				
Investments:				
Archdiocese NPAP	\$ -	\$ 9,064,142	\$ -	\$ 9,064,142
Beneficial interest in perpetual trust	<u>          -</u>	<u>          -</u>	<u>29,684,809</u>	<u>29,684,809</u>
Total of assets at June 30, 2014	<u>\$ -</u>	<u>\$ 9,064,142</u>	<u>\$ 29,684,809</u>	<u>\$ 38,748,951</u>

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**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE K - FAIR VALUE MEASUREMENTS - Continued

The following table presents assets under the beneficial interest in perpetual trust measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended June 30:

	2015	2014
Beginning balance	\$ 29,684,809	\$ 27,046,817
Change in fair value of assets	270,377	4,138,992
Distributions from perpetual trust	<u>(1,450,000)</u>	<u>(1,501,000)</u>
	<u>\$ 28,505,186</u>	<u>\$ 29,684,809</u>

NOTE L - FUNCTIONAL EXPENSES

OCE provides services to schools and entities included in Note A. Expenses related to providing these services are as follows for the years ended June 30:

	2015	2014
Program		
Tuition assistance/scholarships	\$ 1,415,759	\$ 471,743
Music and ministry programs	1,253,374	1,490,719
Sports	55,040	65,398
Administrative	<u>6,473,710</u>	<u>4,379,417</u>
	<u>\$ 9,197,883</u>	<u>\$ 6,407,277</u>

NOTE M - LEASE COMMITMENTS

OCE has entered into lease agreements with respect to equipment. The following is a schedule of future minimum lease payments for operating leases with noncancellable lease terms in excess of one year:

Year ending June 30,		
2016		\$ 20,479
2017		19,000
2018		15,860
2019		<u>1,771</u>
		<u>\$ 57,110</u>

Lease expenses for the years ended June 30, 2015 and 2014 totaled \$27,716 and \$24,545, respectively.

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**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2015 and 2014

NOTE N - SUBSEQUENT EVENTS

OCE evaluated its June 30, 2015 financial statements for subsequent events through November 30, 2015, the date the financial statements were available to be issued. OCE is not aware of any subsequent event which would require recognition or disclosure in the financial statements.