

Financial Statements and Report of
Independent Certified Public Accountants

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

June 30, 2017 and 2016

Contents

	Page
Report of Independent Certified Public Accountants	3
Financial statements	
Statements of financial position	5
Statements of activities and changes in net assets	6
Statements of cash flows	8
Notes to financial statements	9



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
[linkd.in/GrantThorntonUS](https://www.linkedin.com/company/grantthorntonus)
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, 2017 and 2016, 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, 2017 and 2016, 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

December 5, 2017

Archdiocese of Philadelphia, Office of Catholic Education
Administration Account

STATEMENTS OF FINANCIAL POSITION

June 30,

ASSETS	<u>2017</u>	<u>2016</u>
Cash and cash equivalents, including amounts held by affiliate	\$ 3,243,171	\$ 2,278,041
Accounts receivable	114,644	670,210
Due from other Archdiocesan entities (Note I)	53,875	30,660
Other assets	218,432	62,755
Investments (Note C)	9,439,481	8,508,063
Beneficial interest in perpetual trust	<u>28,909,471</u>	<u>28,252,784</u>
 Total assets	 <u>\$ 41,979,074</u>	 <u>\$ 39,802,513</u>
 LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable	\$ 254,768	\$ 219,671
Accrued vacation	112,765	116,338
Accrued severance	18,950	21,823
Accrued salaries	70,040	53,136
Due to other Archdiocesan entities (Note I)	311,454	31,965
Deferred revenue	<u>27,247</u>	<u>5,225</u>
 Total liabilities	 <u>795,224</u>	 <u>448,158</u>
 Net assets		
Unrestricted	1,329,393	828,582
Unrestricted - designated	1,201,053	1,088,275
Temporarily restricted (Note E)	6,845,906	6,423,059
Permanently restricted (Note F)	<u>31,807,498</u>	<u>31,014,439</u>
 Total net assets	 <u>41,183,850</u>	 <u>39,354,355</u>
 Total liabilities and net assets	 <u>\$ 41,979,074</u>	 <u>\$ 39,802,513</u>

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, 2017

	Unrestricted	Unrestricted - designated	Temporarily restricted	Permanently restricted	Total
Revenues					
Subsidies					
Office of Catholic Education -					
Diocesan High Schools					
Operations Account	\$ 4,989,500	\$ -	\$ -	\$ -	\$ 4,989,500
Schools of Special Education	215,000	-	-	-	215,000
Parishes	959,615	-	-	-	959,615
Contributions					
Archdiocesan Educational Fund	188,680	-	320,175	-	508,855
Donations	586,452	-	399,590	-	986,042
Contributed services (Note J)	109,453	-	-	-	109,453
Program revenues	1,438,030	-	196	-	1,438,226
Investment income	20,668	20,528	116,618	18,169	175,983
Net realized and unrealized (losses) gains on investments	(96)	132,262	736,116	118,203	986,485
Funds with deficiencies (Note G)	144,734	-	(144,734)	-	-
Change in beneficial interest in perpetual trust	-	-	-	656,687	656,687
Distribution of beneficial interest in perpetual trust	-	-	1,425,000	-	1,425,000
Release of unrestricted - designated funds	40,012	(40,012)	-	-	-
Net assets released from restrictions	2,430,114	-	(2,430,114)	-	-
 Total revenues	11,122,162	112,778	422,847	793,059	12,450,846
 Expenses					
Salaries and benefits	5,151,717	-	-	-	5,151,717
Purchased services	2,704,077	-	-	-	2,704,077
Intradiocesan expenses	345,958	-	-	-	345,958
Support expenses	2,419,599	-	-	-	2,419,599
 Total expenses	10,621,351	-	-	-	10,621,351
 Change in net assets	500,811	112,778	422,847	793,059	1,829,495
Net assets, beginning of year	828,582	1,088,275	6,423,059	31,014,439	39,354,355
Net assets, end of year	\$ 1,329,393	\$ 1,201,053	\$ 6,845,906	\$ 31,807,498	\$ 41,183,850

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, 2016

	Unrestricted	Unrestricted - designated	Temporarily restricted	Permanently restricted	Total
Revenues					
Subsidies					
Office of Catholic Education - Diocesan High Schools					
Operations Account	\$ 4,615,692	\$ -	\$ -	\$ -	\$ 4,615,692
Schools of Special Education	215,000	-	-	-	215,000
Contributions					
Archdiocesan Educational Fund	423,000	-	-	-	423,000
Donations	909,268	-	411,149	-	1,320,417
Contributed services (Note J)	133,081	-	-	-	133,081
Program revenues	1,158,869	-	10,000	-	1,168,869
Investment income	22,737	16,874	98,357	14,441	152,409
Net realized and unrealized losses on investments	-	(27,134)	(130,558)	(20,811)	(178,503)
Funds with deficiencies (Note G)	(80,834)	-	80,834	-	-
Change in beneficial interest in perpetual trust	-	-	-	(252,402)	(252,402)
Distribution of beneficial interest in perpetual trust	-	-	1,565,000	-	1,565,000
Other revenue	83,074	-	-	-	83,074
Release of unrestricted - designated funds	89,909	(89,909)	-	-	-
Net assets released from restrictions	<u>2,157,062</u>	<u>-</u>	<u>(2,157,062)</u>	<u>-</u>	<u>-</u>
 Total revenues	 <u>9,726,858</u>	 <u>(100,169)</u>	 <u>(122,280)</u>	 <u>(258,772)</u>	 <u>9,245,637</u>
 Expenses					
Salaries and benefits	4,692,560	-	-	-	4,692,560
Purchased services	3,119,375	-	-	-	3,119,375
Intradiocesan expenses	321,046	-	-	-	321,046
Support expenses	<u>1,925,292</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,925,292</u>
 Total expenses	 <u>10,058,273</u>	 <u>-</u>	 <u>-</u>	 <u>-</u>	 <u>10,058,273</u>
 Change in net assets	 (331,415)	 (100,169)	 (122,280)	 (258,772)	 (812,636)
Net assets, beginning of year	<u>1,159,997</u>	<u>1,188,444</u>	<u>6,545,339</u>	<u>31,273,211</u>	<u>40,166,991</u>
Net assets, end of year	<u>\$ 828,582</u>	<u>\$ 1,088,275</u>	<u>\$ 6,423,059</u>	<u>\$ 31,014,439</u>	<u>\$ 39,354,355</u>

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

Archdiocese of Philadelphia, Office of Catholic Education
Administration Account

STATEMENTS OF CASH FLOWS

Year ended June 30,

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities		
Change in net assets	\$ 1,829,495	\$ (812,636)
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Net realized and unrealized (gains) losses on investments	(986,485)	178,503
Change in beneficial interest in perpetual trust	(656,687)	252,402
Changes in operating assets and liabilities		
Accounts receivable	555,566	(258,111)
Due from other Archdiocesan entities	(23,215)	14,242
Other assets	(155,677)	(8,833)
Accounts payable	35,097	118,659
Accrued vacation	(3,573)	23,906
Accrued severance	(2,873)	(2,873)
Accrued salaries	16,904	32,242
Due to other Archdiocesan entities	279,489	(2,021)
Deferred revenue	<u>22,022</u>	<u>(8,529)</u>
Net cash provided by (used in) operating activities	<u>910,063</u>	<u>(473,049)</u>
Cash flows from investing activities		
Purchase of investments	(163,781)	(119,870)
Proceeds from sale of investments	<u>218,848</u>	<u>329,165</u>
Net cash provided by investing activities	<u>55,067</u>	<u>209,295</u>
Net increase (decrease) in cash and cash equivalents, including amounts held by affiliate	965,130	(263,754)
Cash and cash equivalents, including amounts held by affiliate, beginning of year	<u>2,278,041</u>	<u>2,541,795</u>
Cash and cash equivalents, including amounts held by affiliate, end of year	<u>\$ 3,243,171</u>	<u>\$ 2,278,041</u>

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

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

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:

- High School Operations Account (“DHS”)
- Individual High School Presidents’ Accounts (“DHS”)
- 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. This agreement was extended through 2022 in February of 2016. 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. Subsequent to year end, the Superintendent for Secondary Schools, the Chief Financial Officer and Deputy Secretary also report directly to the 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, 2017 and 2016

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Within the category of unrestricted net assets, management has elected to separately report as Designated Funds, funds which have internal purpose designations determined by the Archbishop or his designee. Although the funds are legally unrestricted, the management of OCE follows this designation in the use of these funds.

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 statements 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 statements 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 is significant.

(Continued)

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

5. Investments

Trustee Accounts are 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 (“SEI”) to act as custodian (the “Custodian”) of the Trustee Accounts. The investment in the Trustee Accounts and other investments are reported at fair value.

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, 2017 and 2016, the allocable fair value of the net assets of the trust was \$28,909,471 and \$28,252,784, respectively. 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 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.

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, 2017 and 2016

NOTE C - INVESTMENTS - Continued

At June 30, 2017 and 2016, OCE held the following categories of investments:

	2017	2016
Catholic Values Equity Fund	\$ 5,784,755	\$ 4,939,903
Catholic Values Fixed Income Fund	3,654,726	3,568,160
Total investments	\$ 9,439,481	\$ 8,508,063

OCE is the beneficiary of an individual trust held in perpetuity by a third party. At June 30, 2017 and 2016, the allocable fair value of this trust was \$28,909,471 and \$28,252,784, respectively. During 2017 and 2016, OCE recognized \$656,687 and \$(252,402), respectively, of permanently restricted appreciation (depreciation) related to this trust.

NOTE D - EMPLOYEE BENEFIT PLANS

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. On June 30, 2014, the Archdiocese froze the Plan. All active employees as of the freeze date retained benefits they had earned through June 30, 2014. After the date of the freeze, accrued pension benefits do not increase for additional service or increases in pay. The Plan is administered by the Trustees of the Plan. OCE made annual contributions to the Plan at an average rate of 5.9% and 4.0% of the salaries of eligible staff for the years ended June 30, 2017 and 2016, respectively. The amount expended by OCE for contributions to the Plan was \$169,842 and \$104,202 for the years ended June 30, 2017 and 2016, 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.

The assets available to fund Plan benefits were 82.1% of the preliminary estimate of the actuarially determined present value of the accumulated Plan benefits at June 30, 2017. At June 30, 2016, the assets available to fund Plan benefits were 70.7% of the actuarially determined present value of the accumulated Plan benefits.

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.

(Continued)

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE D - EMPLOYEE BENEFIT PLANS - Continued

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.

Non-Grandfathered Employees - Non-grandfathered employees are eligible to receive the employer contributions generally upon completion of 1,000 hours of service in the relevant measurement period.

Vesting in employer contributions is immediate for grandfathered employees who have 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 2017 and 2016, OCE's contribution rate was 4.5% of base salary for eligible employees and there was a 0.5% and 0.035% charge for administration in 2017 and 2016, respectively. The contributions into the 403(b) plan totaled \$170,783 and \$139,540 for the years ended June 30, 2017 and 2016, respectively.

NOTE E - TEMPORARILY RESTRICTED NET ASSETS

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

	2017	2016
Tuition assistance/scholarships	\$ 5,206,019	\$ 4,741,547
Programs/grants	1,582,717	1,475,993
Scholarships/programs	36,737	196,851
Accumulated earnings in excess of spending of endowments:		
Tuition assistance/scholarships	9,100	6,846
Other	11,333	1,822
	\$ 6,845,906	\$ 6,423,059

During 2017 and 2016, net assets were released from donor restrictions by incurring expenses satisfying the restricted purpose of \$2,430,114 and \$2,157,062, respectively.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE F - PERMANENTLY RESTRICTED NET ASSETS

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

	2017	2016
Programs/grants (through beneficial interest in perpetual trust)	\$ 28,909,471	\$ 28,252,784
Endowment net assets		
Tuition assistance/scholarships	2,830,006	2,693,634
Other	68,021	68,021
	\$ 31,807,498	\$ 31,014,439

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.

(Continued)

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE G - ENDOWMENTS - Continued

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, 2017 and 2016 allowed for a 3% draw of the three-year average market value of the permanently restricted endowments, unless directed otherwise by the donor.

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 \$-0- and \$80,834 as of June 30, 2017 and 2016, respectively. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions.

As of June 30, 2017 and 2016, \$2,898,027 and \$2,761,655, respectively, in donor-restricted endowment funds were recorded within permanently restricted net assets.

Changes in endowment net assets for the year ended June 30, 2017:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, June 30, 2016	\$ -	\$ 8,668	\$ 2,761,655	\$ 2,770,323
Investment income	-	28,854	18,169	47,023
Net appreciation (realized and unrealized gains)	-	187,445	118,203	305,648
Total investment return	-	216,299	136,372	352,671
Appropriation of endowment assets for expenditure	-	(59,800)	-	(59,800)
Funds with deficiencies	-	(144,734)	-	(144,734)
Endowment net assets, June 30, 2017	\$ -	\$ 20,433	\$ 2,898,027	\$ 2,918,460

(Continued)

Archdiocese of Philadelphia, Office of Catholic Education
Administration Account

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE G - ENDOWMENTS - Continued

Changes in endowment net assets for the year ended June 30, 2016:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, June 30, 2015	\$ -	\$ 9,207	\$ 2,768,025	\$ 2,777,232
Investment income	-	22,178	14,441	36,619
Net depreciation (realized and unrealized losses)	-	(32,951)	(20,811)	(53,762)
Total investment return	-	(10,773)	(6,370)	(17,143)
Appropriation of endowment assets for expenditure	-	(70,600)	-	(70,600)
Funds with deficiencies	-	80,834	-	80,834
Endowment net assets, June 30, 2016	\$ -	\$ 8,668	\$ 2,761,655	\$ 2,770,323

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, 2017, the OCE tax years ended June 30, 2014 through June 30, 2016 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>2017</u>	<u>2016</u>
Individual high schools	\$ 10,135	\$ -
Combined Diocesan High Schools	43,740	30,660
	\$ 53,875	\$ 30,660

(Continued)

Archdiocese of Philadelphia, Office of Catholic Education
Administration Account

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE I - RELATED PARTY TRANSACTIONS - Continued

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

	2017	2016
Office for Communications	\$ 90,000	\$ -
Office of Child and Youth Protection	50,013	22,466
Office for General Services	664	855
St. Hubert High School	-	2,267
Diocesan High Schools	114,629	-
Office of Human Resources	-	500
Office for Financial Services	56,148	5,877
	\$ 311,454	\$ 31,965

OCE receives subsidies from the Diocesan High Schools Operations Account. Subsidies totaled \$4,989,500 (\$4,201,500 for administration costs and \$788,000 for marketing expense) and \$4,615,692 (\$3,715,692 for administration costs and \$900,000 for marketing expense) for the years ended June 30, 2017 and 2016, respectively.

OCE charged the Schools of Special Education \$215,000 for each of the years ended June 30, 2017 and 2016, for management services, which amounts are included in subsidies revenue.

Cash and cash equivalents include \$525,382 and \$1,723,456 at June 30, 2017 and 2016, 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:

	2017	2016
Salaries and benefits - lay equivalent value of religious services	\$ 302,160	\$ 296,235
Expended for religious services	(192,707)	(163,154)
Salaries, related employee benefits and faculty house expenses	\$ 109,453	\$ 133,081

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

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.

(Continued)

Archdiocese of Philadelphia, Office of Catholic Education
Administration Account

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE K - FAIR VALUE MEASUREMENTS - Continued

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>2017</u>				
Assets				
Investments:				
SEI mutual funds	\$ 9,439,481	\$ -	\$ -	\$ 9,439,481
Beneficial interest in perpetual trust	-	-	28,909,471	28,909,471
Total of assets at June 30, 2017	\$ 9,439,481	\$ -	\$ 28,909,471	\$ 38,348,952
<u>2016</u>				
Assets				
Investments:				
SEI mutual funds	\$ 8,508,063	\$ -	\$ -	\$ 8,508,063
Beneficial interest in perpetual trust	-	-	28,252,784	28,252,784
Total of assets at June 30, 2016	\$ 8,508,063	\$ -	\$ 28,252,784	\$ 36,760,847

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 years ended June 30:

	2017	2016
Beginning balance	\$ 28,252,784	\$ 28,505,186
Change in fair value of assets	2,081,687	1,312,598
Distributions from perpetual trust	(1,425,000)	(1,565,000)
	\$ 28,909,471	\$ 28,252,784

Archdiocese of Philadelphia, Office of Catholic Education
Administration Account

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

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:

	2017	2016
Program		
Tuition assistance/scholarships	\$ 1,382,857	\$ 1,213,012
Music and ministry programs	1,038,184	1,131,698
Sports	59,067	85,593
Administrative	8,141,243	7,627,970
	\$ 10,621,351	\$ 10,058,273

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,		
2018		\$ 27,407
2019		13,082
		\$ 40,489

Lease expenses for the years ended June 30, 2017 and 2016 totaled \$30,440 and \$28,406, respectively.

NOTE N - SUBSEQUENT EVENTS

OCE evaluated its June 30, 2017 financial statements for subsequent events through December 5, 2017, 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, except as noted in Note A.