

EPISCOPAL DIOCESE OF  
NORTH CAROLINA AND  
RELATED ENTITY

Combined Financial Statements

December 31, 2019 and 2018

(With Independent Auditors' Report Thereon)

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## **Independent Auditors' Report**

The Bishop and Diocesan Council  
Episcopal Diocese of North Carolina:

We have audited the accompanying combined financial statements of the Episcopal Diocese of North Carolina and the North Carolina Episcopal Church Foundation, Inc. (collectively the "Diocese" and each a nonprofit organization), which comprise the combined statements of financial position as of December 31, 2019 and 2018, and the related combined statements of activities, functional expenses and cash flows for the years then ended, and the related notes to the combined financial statements.

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

Management is responsible for the preparation and fair presentation of these combined 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 combined financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these combined 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 combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the combined financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the Diocese's preparation and fair presentation of the combined 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 combined financial statements.

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

### **Basis for Qualified Opinion**

As explained in note 1(q) to the combined financial statements, the Diocese elected not to have an actuarial valuation of its postretirement benefit obligation as of December 31, 2019 and 2018. Accounting principles generally accepted in the United States of America require an entity that sponsors a defined benefit postretirement plan to report the current economic status of the plan in its statement of financial position and to include enhanced disclosures about the plan. The effects on the accompanying combined financial statements of the failure to properly record and disclose the postretirement benefit obligation have not been determined.

### **Qualified Opinion**

In our opinion, except for the matter described in the Basis for Qualified Opinion paragraph, the combined financial statements referred to above present fairly, in all material respects, the financial position of the Diocese as of December 31, 2019 and 2018, 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.

### **Report on Supplementary Information**

Our audit was conducted for the purpose of forming an opinion on the combined financial statements as a whole. The accompanying schedules of combining statements of financial position and combining statements of activities are presented for purposes of additional analysis of the 2019 combined financial statements rather than to present the financial position and change in net assets of the individual entities, and is not a required part of the combined financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the combined financial statements. The information has been subjected to the auditing procedures applied in the audit of the combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the combined financial statements or to the combined financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the combined financial statements as a whole, except for the matter described in the Basis for Qualified Opinion paragraph.

*Batchelor, Jillogy & Roberts, LLP*

August 20, 2020

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Combined Statements of Financial Position

December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
<u>Assets</u>		
Cash and cash equivalents	\$ 6,551,650	6,050,980
Accounts receivable, net:		
Churches	10,736	824
Other	23,745	30,703
Grant receivable	-	896,550
Prepaid expenses	19,905	13,566
Installment notes receivable-churches	172,647	208,375
Investments, at fair value	46,876,522	40,603,060
Investments - other	569,706	559,279
Property and equipment, net	<u>2,257,144</u>	<u>2,380,625</u>
	<u>\$ 56,482,055</u>	<u>50,743,962</u>
<u>Liabilities and Net Assets</u>		
Liabilities:		
Accounts payable	131,914	89,625
Deferred revenue	9,257	4,291
Custodian funds	19,553,097	17,364,099
Postretirement benefit obligation	<u>4,994,003</u>	<u>4,878,462</u>
Total liabilities	<u>24,688,271</u>	<u>22,336,477</u>
Net assets:		
Without donor restrictions - board designated	9,775,991	9,061,580
Without donor restrictions	<u>8,948,496</u>	<u>8,640,501</u>
	18,724,487	17,702,081
With donor restrictions	<u>13,069,297</u>	<u>10,705,404</u>
Total net assets	<u>31,793,784</u>	<u>28,407,485</u>
	<u>\$ 56,482,055</u>	<u>50,743,962</u>

See accompanying notes to combined financial statements.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Combined Statements of Activities

Year ended December 31, 2019, with comparative totals for 2018

	2019			<u>2018</u>
	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>	
Revenues, gains, and other support:				
Shares, net	\$ 4,603,497	-	4,603,497	4,559,245
Grants and contributions	-	-	-	1,052,501
Investment return	1,579,023	2,666,684	4,245,707	(996,133)
Rental income	120,092	-	120,092	222,584
Chaplaincy income	60,995	-	60,995	61,955
Convention	85,715	-	85,715	81,307
Other income	101,798	-	101,798	72,952
Youth program revenue	77,748	-	77,748	80,890
	<u>6,628,868</u>	<u>2,666,684</u>	<u>9,295,552</u>	<u>5,135,301</u>
Net assets released from restrictions	<u>302,791</u>	<u>(302,791)</u>	<u>-</u>	<u>-</u>
Total revenues, gains, and other support	<u>6,931,659</u>	<u>2,363,893</u>	<u>9,295,552</u>	<u>5,135,301</u>
Expenses:				
Program services	3,646,783	-	3,646,783	3,828,586
Supporting services:				
Management and general	2,247,327	-	2,247,327	1,772,626
Fundraising	15,143	-	15,143	14,755
Total expenses	<u>5,909,253</u>	<u>-</u>	<u>5,909,253</u>	<u>5,615,967</u>
Change in net assets	1,022,406	2,363,893	3,386,299	(480,666)
Net assets, beginning of year	<u>17,702,081</u>	<u>10,705,404</u>	<u>28,407,485</u>	<u>28,888,151</u>
Net assets, end of year	\$ <u>18,724,487</u>	<u>13,069,297</u>	<u>31,793,784</u>	<u>28,407,485</u>

(Continued)

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Combined Statements of Activities, Continued

Year ended December 31, 2018

	Without Donor <u>Restrictions</u>	With Donor <u>Restrictions</u>	<u>Total</u>
Revenues, gains, and other support:			
Shares, net	\$ 4,559,245	-	4,559,245
Grants and contributions	55,951	996,550	1,052,501
Investment return	(644,617)	(351,516)	(996,133)
Rental income	222,584	-	222,584
Chaplaincy income	61,955	-	61,955
Convention	81,307	-	81,307
Other income	72,952	-	72,952
Youth program revenue	80,890	-	80,890
	<u>4,490,267</u>	<u>645,034</u>	<u>5,135,301</u>
Net assets released from restrictions	<u>340,537</u>	<u>(340,537)</u>	<u>-</u>
Total revenues, gains, and other support	<u>4,830,804</u>	<u>304,497</u>	<u>5,135,301</u>
Expenses:			
Program services	3,828,586	-	3,828,586
Supporting services:			
Management and general	1,772,626	-	1,772,626
Fundraising	14,755	-	14,755
Total expenses	<u>5,615,967</u>	<u>-</u>	<u>5,615,967</u>
Change in net assets	(785,163)	304,497	(480,666)
Net assets, beginning of year	<u>18,487,244</u>	<u>10,400,907</u>	<u>28,888,151</u>
Net assets, end of year	\$ <u>17,702,081</u>	<u>10,705,404</u>	<u>28,407,485</u>

(Continued)

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Consolidated Statements of Functional Expenses

Year ended December 31, 2019, with Comparative Totals for 2018

	2019				
	<u>Program</u>	<u>Management and general</u>	<u>Fund- raising</u>	<u>Total</u>	<u>2018</u>
Salaries and benefits	\$ 1,536,047	1,363,613	15,143	2,914,803	2,801,166
Annual commitment	621,156	-	-	621,156	570,273
Travel and convention	281,521	316,669	-	598,190	304,223
Outreach	569,573	-	-	569,573	409,340
Foundation grants	202,600	-	-	202,600	112,425
Mission grants	176,382	-	-	176,382	401,698
Office expense	-	205,928	-	205,928	255,284
Chaplaincy	160,177	-	-	160,177	136,522
Maintenance	4,367	141,857	-	146,224	64,225
Depreciation	-	130,760	-	130,760	125,358
Publication and network	75,640	32,409	-	108,049	94,828
Professional services	-	56,091	-	56,091	81,763
Other	19,320	-	-	19,320	258,862
	<u>\$ 3,646,783</u>	<u>2,247,327</u>	<u>15,143</u>	<u>5,909,253</u>	<u>5,615,967</u>

(Continued)

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Consolidated Statements of Functional Expenses, Continued

Year ended December 31, 2018

	<u>Program</u>	<u>Management and general</u>	<u>Fund- raising</u>	<u>Total</u>
Salaries and benefits	\$ 1,714,644	1,071,767	14,755	2,801,166
Annual commitment	570,273	-	-	570,273
Outreach	409,340	-	-	409,340
Mission grants	401,698	-	-	401,698
Travel and convention	223,885	80,338	-	304,223
Office expense	3,976	251,308	-	255,284
Chaplaincy	136,522	-	-	136,522
Depreciation	-	125,358	-	125,358
Foundation grants	112,425	-	-	112,425
Publication and network	12,425	82,403	-	94,828
Professional services	44,313	37,450	-	81,763
Maintenance	-	64,225	-	64,225
Other	199,085	59,777	-	258,862
	<u>\$ 3,828,586</u>	<u>1,772,626</u>	<u>14,755</u>	<u>5,615,967</u>

(Continued)



EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Combined Statements of Cash Flows

Years ended December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Cash flows from operating activities:		
Change in net assets	\$ 3,386,299	(480,666)
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Depreciation and amortization	130,760	125,358
Realized and unrealized (gains) losses on investments	(3,972,501)	786,403
Gain on disposal of property and equipment	-	(11,846)
Changes in operating assets and liabilities:		
Grants and other receivables	893,596	(891,432)
Prepaid expenses	(6,339)	(5,043)
Other assets	35,728	(115,217)
Accounts payable	42,289	(113,617)
Deferred revenue	4,966	(5,737)
Postretirement benefit obligation	115,541	(26,237)
Net cash (used in) provided by operating activities	<u>630,339</u>	<u>(738,034)</u>
Cash flows from investing activities:		
Purchases of property and equipment	(7,279)	(58,662)
Proceeds from sale of property and equipment	-	18,367
Purchases of investments	(1,091,660)	(180,318)
Proceeds from sales of investments	977,604	1,132,473
Proceeds from (repayments of) custodian funds, net	<u>(8,334)</u>	<u>338,683</u>
Net cash provided by investing activities	<u>(129,669)</u>	<u>1,250,543</u>
Net increase in cash and cash equivalents	500,670	512,509
Cash and cash equivalents, beginning of year	<u>6,050,980</u>	<u>5,538,471</u>
Cash and cash equivalents, end of year	\$ <u>6,551,650</u>	<u>6,050,980</u>

See accompanying notes to combined financial statements.

# EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

## Notes to Combined Financial Statements

December 31, 2019 and 2018

### (1) Organization and Summary of Significant Accounting Policies

#### (a) Organization

The Episcopal Diocese of North Carolina (the "Episcopal Diocese") is a nonprofit organization that serves as an administrative division of the Episcopal Church. It is a geographical area under the jurisdiction of a Bishop and is made up of parishes, missions, chaplaincies and other entities. The Diocese collects share revenue from member churches based on an equal flat rate for each church based on previous year's income. The staff offers support for local stewardship efforts, congregational development, outreach ministry, youth work, Christian education, and financial and business concerns. These combined financial statements do not include the individual activities of the parishes, missions, chaplaincies and other entities.

The North Carolina Episcopal Church Foundation, Inc. (the "Church Foundation") makes loans and grants to churches within the Episcopal Diocese of North Carolina.

The Church Foundation is an organization of the Episcopal Diocese and is, therefore, combined with the Episcopal Diocese. The combined entities are collectively referred to as the "Diocese".

#### (b) Basis of Accounting

The combined financial statements of the Diocese have been prepared on the accrual basis in accordance with U.S. generally accepted accounting principles (GAAP), except for the effects of the GAAP departure described in note 1(q).

#### (c) Basis of Combination

The combined financial statements include the accounts of the Episcopal Diocese and the Church Foundation. All significant intercompany accounts and transactions have been eliminated in the combination.

#### (d) Basis of Presentation

The Diocese presents its net assets and its support and revenue based upon the absence or existence of donor-imposed restrictions as follows:

Net assets without donor restrictions – net assets that are not restricted by donors or for which donor-imposed restrictions have expired.

Net assets with donor restrictions – net assets that contain donor-imposed time or purpose restrictions that have not currently been met or net assets that contain donor-imposed restrictions stipulating that amounts be maintained in perpetuity. The Diocese may expend part, or all the income earned according to donor stipulations.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(1) Organization and Summary of Significant Accounting Policies, Continued

(d) Basis of Presentation, Continued

Expenses are reported as decreases in net assets without donor restrictions. Expirations of net assets with donor restrictions (i.e., the stipulated time period has elapsed, or purpose was satisfied) are reported as net assets released from restrictions.

(e) Grants and Contributions

Grants and contributions are generally recorded when received or when an unconditional promise to give to the Diocese is received. Contributions of assets other than cash are recorded at their estimated fair value.

(f) Cash and Cash Equivalents

The Diocese considers cash on hand, deposits in banks, and all highly liquid temporary cash instruments purchased with an initial maturity of three months or less to be cash equivalents.

The Diocese holds cash receipt and disbursement records open for approximately one week after the end of the year in order to record year-end transactions with member churches which are postmarked as of December 31.

(g) Grants and Other Receivables

The Diocese periodically evaluates the balances in the various aging categories as well as the status of any significant past due accounts to determine the need for an allowance for doubtful accounts. Changes in the allowance are charged to the period in which management determines the change to be necessary.

When management determines that a receivable is uncollectible, the balance is removed from the receivables balance and is charged against the allowance. Subsequent recoveries of amounts previously written off are credited directly to revenues. The allowance for uncollectible accounts was \$5,000 as of December 31, 2019 and 2018.

Installment notes receivable represents funds advanced to churches within the Episcopal Diocese through the Church Foundation. Loans are stated at unpaid principal balances less an allowance for uncollectible amounts. Principal and interest on notes are due quarterly. These notes bear interest at 4%, with maturities through 2033. The loans are unsecured. The amount of the allowance for uncollectible amounts is based on management's evaluation of the collectability of specific notes. The allowance is increased by a provision for uncollectible accounts, which is charged to expense. No allowance for uncollectible accounts was deemed necessary as of December 31, 2019 and 2018.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(1) Organization and Summary of Significant Accounting Policies, Continued

(h) Property and Equipment

Property and equipment are stated at cost at the date of acquisition, appraised value for assets for which original cost cannot be determined, or fair value at the date of donation in the case of gifts. Depreciation is computed over the estimated useful lives of the related assets using the straight-line method, generally as follows:

Buildings and building improvements	31.5 - 39 years
Leasehold improvements	15 years
Furniture and equipment	5 - 7 years
Land	nondepreciable

In accordance with the Diocese's policy, property and equipment are included in net assets without donor restrictions. The Diocese capitalizes expenditures for such items in excess of \$1,500, and lesser amounts are expensed.

The Diocese also holds title to mission properties and vacant churches. This arrangement is for canonical purposes rather than for actual utilization; therefore, the properties are not included in the accompanying combined financial statements.

(i) Investments

The Diocese carries investments in marketable securities with readily determinable fair values and all investments in debt securities at their fair market values in the combined statements of financial position. Realized and unrealized gains and losses are included in the change in net assets in the accompanying combined statements of activities. Net unrealized gains and losses on investments, whose income is without donor restrictions or with donor restriction as to use, is reported as without donor restriction or with donor restriction net assets as restricted by donor or by law.

The Diocese maintains investment accounts for its invested funds, which have been pooled with funds held for other Episcopal churches and institutions, under the direction of a professional investment manager. Realized and unrealized gains and losses from securities in the pooled investment fund account are allocated to the individual funds.

Expenses relating to investment income, including custodial fees and investment advisory fees, have been netted against investment income or custodian funds in the financial statements.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(1) Organization and Summary of Significant Accounting Policies, Continued

(j) Fair Value Measurements

Financial assets and liabilities required to be measured on a recurring basis (at least annually) are classified under a three-tier hierarchy. Fair value is the amount that would be received to sell an asset, or paid to settle a liability, in an orderly transaction between market participants at the measurement date.

The classification of assets and liabilities within the hierarchy is based on whether inputs to the valuation methodology used for measurement are observable or unobservable. Observable inputs reflect market-derived or market-based information obtained from independent sources while unobservable inputs reflect estimates about market data. See note 5 for assets of the Diocese measured at fair value on a recurring basis.

Valuation techniques used to measure fair value are prioritized in the following hierarchy:

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Diocese can access.

Level 2: Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

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

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The Diocese diversifies its investments both by asset class and within asset classes. As a general practice, all investments of the Diocese are managed by external investment management firms and observed by the Investment committee. The following is a description of the valuation methodologies used by the Diocese for assets measured at fair value:

- Common Stocks, certain Mutual Funds, and Money Market and Short-Term Reserve Funds: Valued at the closing price reported on the active markets on which the individual securities are traded (Level 1).

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(1) Organization and Summary of Significant Accounting Policies, Continued

(j) Fair Value Measurements, Continued

- **Alternative Investments:** Alternative funds are composed of real estate funds (investments in real estate related assets). These investments are recorded at fair value based on relevant information available to the investment advisor such as type and nature of the investment, cost of the investment at the acquisition date, size of the investment, information from analysts, brokers, agents and market participants, and changes in market indicators. These investments are reported at their net asset values (NAV) as calculated by the investment managers.

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

(k) Endowment Funds

The endowment funds of the Diocese consist of donor-restricted funds included in investments in the accompanying combined statements of financial position. The Diocese accounts for the endowment funds in accordance with the Uniform Prudent Management of Institutional Funds Act (UPMIFA) and GAAP.

The Diocese has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Diocese retains in perpetuity (a) the original value of gifts donated to the endowment, (b) the original value of subsequent gifts to the endowment, and (c) accumulations to the endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the funds. The remaining portion of the amounts not retained in perpetuity are appropriated for expenditure by the Diocese in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Diocese considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the various funds, (2) the purposes of the donor-restricted endowment funds, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments, (6) other resources of the Diocese, and (7) the investment policies of the Diocese.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(1) Business Operations and Summary of Significant Accounting Policies, Continued

(k) Endowment Funds, Continued

*Funds with Deficiencies.* From time to time, the fair value of the assets associated with the donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Diocese to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature are reported in net assets with donor restrictions. There were no endowment fund deficiencies as of December 31, 2019 and 2018.

*Investment Return Objectives, Risk Parameters, and Strategies.* The Diocese has adopted investment and spending policies, approved by the Diocesan Council, for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment funds while also maintaining the purchasing power of those endowment assets over the long-term. Accordingly, the investment process seeks to achieve a rate of return, including investment income as well as capital appreciation, which exceeds the annual distribution with acceptable levels of risk. Endowment assets are invested in a well-diversified asset mix that is intended to result in a consistent rate of return that has sufficient liquidity to make an annual distribution of 4%, while growing the fund, if possible. Investment risk is measured in terms of the total endowment funds; investment assets and allocation between asset classes, and strategies are managed to not expose the funds to unacceptable levels of risk.

*Spending Policy.* The Diocese has a policy of appropriating for distribution each year 4% of its endowment fund's average fair value of the prior rolling three-year average through September 30th of the preceding fiscal year in which the distribution is planned. In establishing this policy, the Diocese considered the long-term expected return on its investment assets, the nature and duration of the endowment funds, a portion of which must be maintained in perpetuity because of donor restrictions, and the possible effect of inflation. The Diocese expects the current spending policy to allow its endowment funds to grow at a rate consistent with the Diocese's objective to maintain the purchasing power of the endowment assets as well as to provide additional growth through investment return.

(l) Deferred Revenue

Deferred revenue consists of share amounts received related to a future period, which will be recognized as revenue in the following year.

(m) Custodian Funds

Custodian funds represent resources received on behalf of other organizations by the Diocese. These funds do not represent revenues and expenditures which are under Diocesan control. However, the Diocese is responsible for the custody of these funds until such funds have been used.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(1) Business Operations and Summary of Significant Accounting Policies, Continued

(m) Custodian Funds, Continued

Also, the Diocese acts as delegate agent for various groups receiving grants. As delegate agent, the Diocese can be held responsible for the grant if the recipient group does not comply with all grant requirements.

(n) Vacation Pay and Sick Leave

The Diocese's policy provides for a maximum accumulation of unused vacation leave of 34 days, depending on an employee's years of service, which can be carried forward at the end of each year, or for which an employee can be paid upon termination of employment with the Diocese.

The Diocese records the cost of sick leave when taken and paid rather than when the leave is earned. The maximum allowance accumulation of sick leave is 65 days. However, employees are not compensated for any unused sick leave upon termination of employment.

(o) Use of Estimates

The preparation of combined financial statements in conformity with GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

(p) Income Tax Status

The Episcopal Diocese and the Church Foundation are exempt from income taxes under Section 501(a) as organizations described in Section 501(c)(3) of the Internal Revenue Code. Accordingly, income tax expense is limited to activities that are deemed by the Internal Revenue Service to be unrelated to their exempt purpose. Each entity's primary tax positions relate to its status as a not-for-profit entity exempt from income taxes and classification of activities related to its exempt purpose. Each entity is not required to file a federal exempt organization tax return (Form 990) annually to retain its exempt status. However, the Diocese would be required to file an exempt organization business income tax return (federal and state) for any unrelated business income.

(q) GAAP Departure

*Postretirement Benefits Other Than Pension.* At retirement, Diocesan clergy and other certain employees who were employed as of June 30, 2002 receive lifetime family health insurance coverage if they have served full time continuously for their last ten years of service and remain enrolled in the plan. For employees retiring after attaining age 65, the Diocese will pay the Medicare supplement that would be paid if a person were age 65 and covered by Medicare. In the event retirement is necessary before age 65 as a result of medical disability, the Diocese will pay the full amount of insurance premiums until age 65 at which time it will pay the Medicare supplement. All spouses of deceased clergy who were already enrolled in the in the health coverage under Diocesan health and dental coverage can continue coverage at no cost to the spouse unless they remarry.



EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(1) Business Operations and Summary of Significant Accounting Policies, Continued

(q) GAAP Departure, Continued

GAAP requires an employer that sponsors a defined benefit postretirement plan to report the current economic status (the overfunded or underfunded status) of the plan in its statement of financial position, to measure the plan assets and plan obligations as of the statement of financial position date, and to include enhanced disclosures about the plan. Management of the Diocese elected to not have an actuarial valuation of this plan performed for 2019 or 2018. As such, the postretirement benefit obligation as of December 31, 2019 and 2018 and the change in the postretirement plan obligation other than net periodic postretirement expense for 2019 and 2018 are estimated and/or adjusted based on the Diocese's actuarial valuation performed as of December 31, 2013.

Furthermore, the enhanced disclosures required by GAAP are not available for disclosure for 2019 or 2018. Disclosure of this information is required to conform to GAAP. The effects of this departure from GAAP on the combined financial statements have not been determined.

The accrued post-retirement benefit obligation of the Diocese's post-retirement welfare plan was estimated to be \$4,994,003 and \$4,878,462 of December 31, 2019 and 2018, respectively, using actuarial assumptions from the December 31, 2013 actuarial valuation.

(r) Functional Allocation of Expenses

Management estimates the costs of providing the various programs and other activities on a functional basis in the statements of activities. The statements of functional expenses present the natural classification detail of expenses by function. Accordingly, certain costs have been allocated among the programs and supporting services benefited. Expenditures are allocated to programs or supporting services by management based on what is considered to be the best available objective criteria, such as allocation of time of relevant personnel.

(s) Adoption of New Accounting Standard

During 2019, the Diocese adopted the Financial Accounting Standards Board's Accounting Standards Update (ASU) No. 2014-09 (*Topic 606*): *Revenue from Contracts with Customers*. Under the new standard, revenue from contracts with customers is recognized based on a principle-based five-step model. Implementation of this standard has been applied retrospectively to 2018; however, management has determined that the impact of the standard is not material to the combined financial statements.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(2) Information Regarding Liquidity and Availability of Resources

The Diocese regularly monitors the availability of resources required to meet its operating needs and other contractual commitments. For purposes of analyzing resources available to meet general expenditures over a 12-month period, the Diocese considers all expenditures related to its ongoing activities, as well as the conduct of services undertaken to support those activities, to be general expenditures.

The Diocese's financial assets as of December 31, 2019 and 2018 consist of cash, investments, and accounts receivable, reduced by appropriated funds, board designated, custodian and donor restricted funds, resulting in net financial assets, all of which are available to meet general expenditures within one year of the financial statement date, as follows:

	<u>2019</u>	<u>2018</u>
Financial assets, at year end:		
Cash and cash equivalents	\$ 6,551,650	6,050,980
Investments	47,446,228	41,162,339
Accounts receivable	34,481	31,527
Grants receivable	-	896,550
Total financial assets	<u>54,032,359</u>	<u>48,141,396</u>
Less:		
Appropriated funds	(8,292,405)	(8,105,151)
Board designated	(9,775,991)	(9,061,580)
Custodian funds	(19,553,097)	(17,364,099)
Donor-restricted funds	<u>(13,069,297)</u>	<u>(10,705,404)</u>
Financial assets not available to be used within one year	<u>(50,690,790)</u>	<u>(45,236,234)</u>
Financial assets available to meet cash needs for general expenditures within one year	\$ <u>3,341,569</u>	<u>2,905,162</u>

In addition to financial assets available to meet general expenditures over the next 12 months, the Diocese operates with a balanced budget and anticipates collecting sufficient revenue to cover general expenditures. See further discussion of donor restricted funds at note 7.

(3) Grant Receivable

During 2018, the Diocese was awarded a grant in the amount of \$996,550 of which \$100,000 of the grant was received during 2018. The total grant receivable balance of \$896,550 as of December 31, 2018 was collected in January of 2019.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(4) Concentrations of Credit and Market Risk

Financial instruments that potentially expose the Diocese to concentrations of credit and market risk consist primarily of cash, cash equivalents, receivables and investments.

The Diocese maintains its deposited cash balances in several financial institutions, and amounts held may at times exceed federally insured limits. The Diocese has not experienced any losses on these accounts. The Diocese's investments are mostly maintained in a pooled investment fund held by various custodians. This pooled investment portfolio is diversified among issuers. Receivables are discussed in note 1(g).

(5) Investments

Investments, at fair value, consist of the following:

	<u>2019</u>	<u>2018</u>
Money market and short-term reserves	\$ 707,567	1,180,100
Mutual funds	28,014,794	25,530,681
Equities	<u>18,154,161</u>	<u>13,892,279</u>
	<u>\$ 46,876,522</u>	<u>40,603,060</u>

Other investments totaling \$569,706 and \$559,279 as of December 31, 2019 and 2018, respectively, consist of time deposits that mature in 2020.

Custodian funds (which include custodial accounts and trust funds held for others) are included in total investments above. Custodian funds totaled \$19,553,097 and \$17,364,099 as of December 31, 2019 and 2018 respectively. See note 9 for detailed activity of these custodian funds.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(5) Investments, Continued

The following table sets forth by level, within the fair value hierarchy, the Diocese's assets measured at fair value on a recurring basis as of December 31, 2019 and 2018. Individual securities exceeding 10% of net assets are separately identified below.

	2019		2018	
	Total	Level 1	Total	Level 1
Investments:				
Money market and short-term reserve funds	\$ <u>707,567</u>	<u>707,567</u>	\$ <u>1,180,100</u>	<u>1,180,100</u>
Mutual funds:				
Vanguard S&P 500 ETF	5,072,083	5,072,083	4,186,908	4,186,908
Other	<u>21,730,275</u>	<u>21,730,275</u>	<u>19,865,285</u>	<u>19,865,285</u>
	<u>26,802,358</u>	<u>26,802,358</u>	<u>24,052,193</u>	<u>24,052,193</u>
Equities	<u>18,154,161</u>	<u>18,154,161</u>	<u>13,892,279</u>	<u>13,892,279</u>
Total investments at fair value	45,664,086	<u>45,664,086</u>	39,124,572	<u>39,124,572</u>
Investments measured at NAV, not in fair value hierarchy			<u>1,478,488</u>	
Total investments at fair value and NAV	\$ <u>46,876,522</u>		\$ <u>40,603,060</u>	

The cost of investments totaled \$40,930,410 and \$40,337,381 as of December 31, 2019 and 2018, respectively.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(5) Investments, Continued

Investment return consists of the following (investment return included in custodian funds is not included in the combined statements of activities):

	<u>2019</u>		
		<u>Custodian</u>	
	<u>Diocese</u>	<u>funds</u>	<u>Total</u>
Interest and dividends	\$ 966,320	485,475	1,451,795
Realized and unrealized gains	<u>3,352,553</u>	<u>2,604,537</u>	<u>5,957,090</u>
	4,318,873	3,090,012	7,408,885
Less management fees	<u>(73,166)</u>	<u>(60,568)</u>	<u>(133,734)</u>
Investment return	\$ <u>4,245,707</u>	<u>3,029,444</u>	<u>7,275,151</u>
	<u>2018</u>		
		<u>Custodian</u>	
	<u>Diocese</u>	<u>funds</u>	<u>Total</u>
Interest and dividends	\$ 923,328	404,960	1,328,288
Realized and unrealized losses	<u>(1,846,913)</u>	<u>(1,465,469)</u>	<u>(3,312,382)</u>
	(923,585)	(1,060,509)	(1,984,094)
Less management fees	<u>(72,548)</u>	<u>(59,563)</u>	<u>(132,111)</u>
Investment return	\$ <u>(996,133)</u>	<u>(1,120,072)</u>	<u>(2,116,205)</u>

The table below sets forth a summary of changes in investments, the values of which are estimated using NAV per share as of 2019 and 2018, respectively.

	<u>2019</u>	<u>2018</u>
Balance, beginning of year	\$ 1,478,488	1,505,923
Purchases	11,441	22,881
Investment income, net	(64,633)	(9,820)
Unrealized and realized (losses) gains	(107,607)	98,086
Sales	<u>(105,253)</u>	<u>(138,582)</u>
Balance, end of year	\$ <u>1,212,436</u>	<u>1,478,488</u>

As of December 31, 2019 and 2018, this investment consisted of the MA Real Estate Fund 2 Limited Partnership, which is a private equity fund. The Diocese has a remaining capital commitment of \$275,086 as of December 31, 2019.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(6) Property and Equipment

Property and equipment is as follows:

	<u>2019</u>	<u>2018</u>
Land and buildings:		
Recorded at cost:		
NCSU Chaplaincy House	\$ 94,915	94,915
Duke Student Center	74,837	67,557
Land-Kernersville	43,215	43,215
200 W. Morgan Street	2,758,236	2,758,236
Recorded at January 1, 1978 appraised values:		
Holding Land	13,140	13,140
St. Mary's House	63,476	63,476
Caswell County property	28,760	28,760
Other property:		
Recorded at cost:		
Leasehold improvements - Diocesan House	571,809	571,809
Vehicles	58,661	58,661
Equipment and furniture	<u>305,625</u>	<u>305,625</u>
	4,012,674	4,005,394
Less accumulated depreciation and amortization	<u>(1,755,530)</u>	<u>(1,624,769)</u>
	<u>\$ 2,257,144</u>	<u>2,380,625</u>

Depreciation and amortization expense for 2019 and 2018 was \$130,760 and \$125,358, respectively.

Rental income is generated from a sublease of space in the Morgan Street building.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(7) Net Assets

Net assets with donor restrictions are restricted for the following purposes or periods:

	<u>2019</u>	<u>2018</u>
Subject to expenditure for specified purpose:		
Mission and Ministry Fund	\$ 531,454	463,849
Thriving in Pastoral Ministry	996,550	996,550
Diocesan Trusts Programs	<u>3,990,653</u>	<u>2,676,145</u>
	5,518,657	4,136,544
Endowments:		
Subject to Diocese spending policy and appropriation:	<u>7,550,640</u>	<u>6,568,860</u>
	\$ <u><u>13,069,297</u></u>	<u><u>10,705,404</u></u>

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purpose or other events specified by the donors as follows:

	<u>2019</u>	<u>2018</u>
Satisfaction of purpose restrictions:		
Diocesan Trust Programs	\$ <u><u>302,791</u></u>	<u><u>340,537</u></u>

Changes in endowment net assets during 2019 and 2018 are as follows:

	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, January 1, 2018	\$ -	\$ 7,247,747	7,247,747
Interest and dividend income, net	-	165,689	165,689
Realized and unrealized losses, net	-	(584,658)	(584,658)
Amounts appropriated for expenditure	<u>-</u>	<u>(259,918)</u>	<u>(259,918)</u>
Endowment net assets, December 31, 2018	-	6,568,860	6,568,860
Interest and dividend income, net	-	176,726	176,726
Realized and unrealized gains, net	-	1,063,095	1,063,095
Amounts appropriated for expenditure	<u>-</u>	<u>(258,041)</u>	<u>(258,041)</u>
Endowment net assets, December 31, 2019	\$ <u><u>-</u></u>	\$ <u><u>7,550,640</u></u>	<u><u>7,550,640</u></u>

Board designated net assets totaling \$9,775,991 and \$9,061,580 as of December 31, 2019 and 2018, respectively, may only be used for the purposes expressly assigned as approved by individual Committee boards.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(7) Net Assets, Continued

To satisfy its long-term rate-of-return objectives, the Diocese relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Diocese targets a diversified asset allocation for its entire investment portfolio that places an emphasis on equity-based and fixed income investments and cash equivalents to achieve its long-term return objectives within prudent risk constraints. The Committee boards have elected to allow the capital growth and investment income of the Board designated net assets to continue to accumulate within these net assets.

(8) Pension Plans

The Diocese has a non-contributory pension plan which covers substantially all clergy and lay employees. Total costs to the Diocese amounted to \$297,433 and \$232,592 for 2019 and 2018, respectively. The plan is comprised of individual contracts with The Church Pension Fund.

(9) Custodian Funds

The Diocese acts as an agent, or custodian, for certain assets owned by churches and other institutions by receiving, investing, and disbursing funds on their behalf. Changes in custodian funds for 2019 and 2018 are as follows:

	<u>Custodial</u> <u>Accounts</u>	<u>Held for</u> <u>Churches/</u> <u>Institutions</u>	<u>Total</u>
Balance, December 31, 2017	\$ 775,847	17,344,561	18,120,408
Receipts	1,719,350	709,262	2,428,612
Investment income	-	404,960	404,960
Realized and unrealized losses	-	(1,465,469)	(1,465,469)
Disbursements	<u>(1,376,843)</u>	<u>(747,569)</u>	<u>(2,124,412)</u>
Balance, December 31, 2018	1,118,354	16,245,745	17,364,099
Receipts	1,629,768	306,391	1,936,159
Investment income	-	485,472	485,472
Realized and unrealized gains	-	2,604,537	2,604,537
Disbursements	<u>(1,645,809)</u>	<u>(1,191,361)</u>	<u>(2,837,170)</u>
Balance, December 31, 2019	\$ <u>1,102,313</u>	<u>18,450,784</u>	<u>19,553,097</u>



EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Notes to Combined Financial Statements, Continued

December 31, 2019 and 2018

(10) Subsequent Events

In March 2020, the World Health Organization declared the global novel coronavirus disease 2019 (COVID-19) outbreak a pandemic. The extent of COVID-19's effect on the Diocese's operational and financial performance will depend on future developments, including the duration, spread and intensity of the pandemic, all of which are uncertain and difficult to predict considering the rapidly evolving landscape. As a result, it is not currently possible to ascertain the overall impact of COVID-19 on the Diocese's operations. However, the pandemic could have a material adverse effect on the Diocese's results of operations, financial condition and cash flows.

In April 2020, the Diocese received a loan from the Small Business Administration under the Paycheck Protection Program, which authorizes forgivable loans to small businesses to pay their employees during the COVID-19 crisis. This loan, in the amount of \$509,504, will be forgiven as long as the loan proceeds are used to cover payroll and certain other allowed costs over the 24 week period after the loan is made and certain other conditions are met.

The date to which events occurring after December 31, 2019, the date of the most recent combined statement of financial position, have been evaluated for possible adjustment to the combined financial statements or disclosure is August 20, 2020, the date the combined financial statements were available to be issued.

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Schedule of Combining Statements of Financial Position

December 31, 2019

<u>Assets</u>	<u>Episcopal Diocese</u>	<u>Church Foundation</u>	<u>Combined</u>
Cash and cash equivalents	\$ 6,230,096	321,554	6,551,650
Accounts receivable, net:			
Churches	10,736	-	10,736
Other	23,745	-	23,745
Prepaid expenses	19,905	-	19,905
Installment notes receivable-churches	-	172,647	172,647
Investments, at fair value	43,061,289	3,815,233	46,876,522
Investments - other	569,706	-	569,706
Property and equipment, net	<u>2,257,144</u>	<u>-</u>	<u>2,257,144</u>
	<u>\$ 52,172,621</u>	<u>4,309,434</u>	<u>56,482,055</u>
 <u>Liabilities and Net Assets</u> 			
Liabilities:			
Accounts payable	131,914	-	131,914
Deferred revenue	9,257	-	9,257
Custodian funds	19,553,097	-	19,553,097
Postretirement benefit obligation	<u>4,994,003</u>	<u>-</u>	<u>4,994,003</u>
Total liabilities	<u>24,688,271</u>	<u>-</u>	<u>24,688,271</u>
Net assets:			
Without donor restrictions- board designated	9,775,991	-	9,775,991
Without donor restrictions	4,639,062	4,309,434	8,948,496
With donor restrictions	<u>13,069,297</u>	<u>-</u>	<u>13,069,297</u>
Total net assets	<u>27,484,350</u>	<u>4,309,434</u>	<u>31,793,784</u>
	<u>\$ 52,172,621</u>	<u>4,309,434</u>	<u>56,482,055</u>

EPISCOPAL DIOCESE OF NORTH CAROLINA AND RELATED ENTITY

Schedule of Combining Statements of Activities

Year ended December 31, 2019

	Episcopal <u>Diocese</u>	Church <u>Foundation</u>	<u>Combined</u>
Revenues, gains, and other support:			
Shares, net	\$ 4,603,497	-	4,603,497
Investment return	3,620,123	625,584	4,245,707
Rental income	120,092	-	120,092
Chaplaincy income	60,995	-	60,995
Convention	85,715	-	85,715
Other income	98,517	3,281	101,798
Youth program revenue	<u>77,748</u>	<u>-</u>	<u>77,748</u>
Total revenues, gains, and other support	<u>8,666,687</u>	<u>628,865</u>	<u>9,295,552</u>
Expenses:			
Program services	3,572,087	74,696	3,646,783
Supporting services:			
Management and general	2,247,180	147	2,247,327
Fundraising	<u>15,143</u>	<u>-</u>	<u>15,143</u>
Total expenses	<u>5,834,410</u>	<u>74,843</u>	<u>5,909,253</u>
Change in net assets	2,832,277	554,022	3,386,299
Net assets, beginning of year	<u>24,652,073</u>	<u>3,755,412</u>	<u>28,407,485</u>
Net assets, end of year	\$ <u><u>27,484,350</u></u>	<u><u>4,309,434</u></u>	<u><u>31,793,784</u></u>