

**Diocese of Southern Ohio,
ECSF and Gabriel's Place**

Combined Financial Statements

December 31, 2012 and 2011

(with Independent Auditors' Report)



CLARK SCHAEFER HACKETT
STRENGTH IN NUMBERS

To the Bishop and Trustees
Diocese of Southern Ohio, ECSF and Gabriel's Place

In planning and performing our audit of the combined financial statements of Diocese of Southern Ohio, ECSF and Gabriel's Place ("Diocese") as of and for the year ended December 31, 2012, in accordance with auditing standards generally accepted in the United States of America, we considered Diocese of Southern Ohio, ECSF and Gabriel's Place's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the combined financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Diocese's internal control. Accordingly, we do not express an opinion on the effectiveness of the Diocese's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the following deficiencies in Diocese of Southern Ohio, ECSF and Gabriel's Place's internal control to be material weaknesses:

Segregation of Duties

The small number of people employed by the Diocese in the accounting department creates an inherent weakness in the ability to segregate incompatible accounting functions among different individuals. While we recognize these limitations, we want to remind the Diocese of the situation, and encourage the Financial Officer to segregate functions and provide more oversight to the daily accounting functions. Given the size of the staff, presently, there are limited permutations which would provide for stronger segregation controls. Additional staff or automated options may allow for better segregation of duties.

Audit Adjustment

As part of our audit, an audit adjustment to the combined financial statements was required to write-off an uncollectible receivable in accordance with generally accepted accounting principles. The net effect of this audit adjustment was to decrease the change in net assets by approximately \$787,000.

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This communication is intended solely for the information and use of the Bishop, Trustees and management and others within the organization, and is not intended to be, and should not be, used by anyone other than these specified parties.

Clark, Schaefer, Hockett + Co.

Cincinnati, Ohio
September 6, 2013

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1. ORGANIZATION:

The Episcopal Diocese of Southern Ohio (Diocese) is the Episcopal Church Headquarters for seventy-seven congregations in southern Ohio. The congregations' financial activities are not included in the accompanying financial statements.

ECSF is a foundation that supports Episcopal Church congregations in Southern Ohio in their volunteer response to community needs for educational, poverty relief, trauma counseling, and other social services.

Gabriel's Place is incorporated in the State of Ohio as a charitable corporation and is exempt from federal, state and local income taxes. The mission of Gabriel's Place is to provide a safe, beautiful and spiritually nourishing place for the Avondale Community. Gabriel's Place received their IRS tax determination of 501(c)(3) status in August 2012. The Diocese has a controlling interest in the Gabriel's Place board.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Basis of presentation

Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Diocese and changes therein are classified and reported as follows:

Unrestricted net assets – net assets are not subject to donor-imposed stipulations.

Temporarily restricted net assets – net assets are subject to donor-imposed stipulations that will likely be met either by actions of the Diocese and/or the passage of time.

Permanently restricted net assets – net assets are subject to donor-imposed stipulations that require the assets be maintained permanently by the Diocese. Generally, the donors of these assets permit the Diocese to use all or part of the income earned on related investments for general or specific purposes.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Contributions in which the donor-imposed restrictions were met within the same period are recorded in unrestricted net assets. All expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Investment income in which the donor-imposed restrictions were met within the same period are recorded in unrestricted net assets.

Principles of combination

These financial statements are the result of the combination of the operations of the Episcopal Diocese of Southern Ohio (the Diocese), ECSF and Gabriel's Place. All intercompany transactions are eliminated upon combination.

Investments

Investments in marketable securities with readily determinable fair values and all investments in debt securities and alternative investments are valued at their fair values in the statement of financial position. Unrealized appreciation (depreciation) on investments is included in the statement of activities.

Property and equipment

Property and equipment are stated at cost as of the date of acquisition or fair value as of the date of donation in the case of gifts. Depreciation is provided over the estimated useful lives of the respective assets on a straight-line basis. Estimated useful lives are as follows:

Buildings	20 - 31.5 years
Building and leasehold improvements	15 years
Equipment, furniture and fixtures	3 -10 years

Use of estimates

Management of the Diocese has made estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities, as well as the reported amounts of revenue and expenses, to prepare these financial statements in conformity with generally accepted accounting principles. Actual results could differ from those estimates.

Cash equivalents

Cash equivalents consist primarily of investments in money market funds. At times, cash and money market balances may be in excess of the insurance coverage provided by the Federal Deposit Insurance Corporation. The Diocese has not experienced any losses in such accounts. The Diocese believes it is not exposed to any significant credit risk on cash.

Allowance for doubtful accounts

The Diocese carries its accounts receivable and notes receivable at cost less an allowance for doubtful accounts. Included in notes receivable are mortgages on churches due from the congregations. On a periodic basis, the Diocese evaluates its accounts receivable and notes receivable and establishes an allowance for doubtful accounts, based on a history of past write-offs and collections and current credit conditions. An allowance for accounts receivable and notes receivable of \$1,976,897 and \$1,190,396 existed at December 31, 2012 and 2011.

Grants payable

Grants payable are approved for payment and are scheduled to be disbursed the next fiscal year.

Subsequent events

The Diocese evaluates events and transactions occurring subsequent to the date of the financial statements for matters requiring recognition or disclosure in the financial statements. The accompanying financial statements consider events through September 6, 2013, the date on which the financial statements were available to be issued.

Income taxes

The Episcopal Diocese of Southern Ohio, ECSF and Gabriel's Place are exempt from Federal income taxes under Section 501(c)(3) of the Internal Revenue Code (Code) as charitable organizations. The Diocese and ECSF are not required to file returns with the IRS under a religious exception.

The Financial Accounting Standards Board ("FASB") has issued guidance which clarifies generally accepted accounting principles for recognition, measurement, presentation and disclosure relating to uncertain tax positions. This guidance clarifies the accounting and recognition for income tax positions taken or expected to be taken in the organizations' income tax returns. The Diocese and ECSF are not

required to file an annual information return due to their religious origins but are subject to tax on any unrelated business income. The Diocese and ECSF believes they did not earn any unrelated business income for 2011, estimated no tax due and, thus, determined that an accrual for taxes is not needed for the year ended December 31, 2011. Beginning in 2012, the Diocese is subject to unrelated business income tax regulations on a portion of its income. The Diocese has determined that no liability for unrelated business income tax exists as of December 31, 2012. The Diocese and Gabriel's Place's income tax filings are subject to audit by various taxing authorities. The Diocese and Gabriel's Place's first year of filing with the IRS will be for the year ended December 31, 2012. The Diocese and Gabriel's Place's policy with regards to interest and penalties is to recognize interest through interest expense and penalties through other expense. In evaluating the Diocese and Gabriel's Place's tax provision and tax exempt status, interpretations and tax planning strategies were considered. The Diocese, ECSF and Gabriel's Place believe their estimates are appropriate based on the current facts and circumstances.

Reclassifications

Certain items from 2011 have been reclassified to conform to current year presentation.

3. NOTES RECEIVABLE:

Notes receivable, secured by mortgages, and other notes receivable are comprised of the following as of December 31:

	<u>2012</u>	<u>2011</u>
Clergy	\$ 427,831	451,533
Congregations	<u>3,591,038</u>	<u>3,715,367</u>
	4,018,869	4,166,900
Other notes receivable	628,583	634,129
Allowance for doubtful accounts	<u>(1,971,897)</u>	<u>(1,190,396)</u>
Total notes receivable	<u>\$ 2,675,555</u>	<u>3,610,633</u>

The interest rates on the notes receivable range from 2.00% to 5.75%. Based on current market rates, the carrying value of notes receivable approximate fair value.

During 2012, the Diocese took possession of a church building from a congregation that collateralized a note receivable. The allowance for doubtful accounts was increased by \$786,501 at December 31, 2012 for the related note receivable. The building was recorded at fair value of \$850,000, based upon an option to purchase included in a lease agreement with a third party.

4. INVESTMENTS:

Investments are held for the benefit of the Diocese and ECSF at fair value as follows at December 31:

	<u>2012</u>	<u>2011</u>
Cash equivalents	\$ 2,101,567	1,987,554
Common stocks	41,255,581	41,059,394
United States government and agency securities	10,693,570	6,598,022
Proportionate share of assets in:		
Consolidated I fund	12,960,692	12,636,394
Consolidated G fund	8,902,621	8,085,176
Corporate bonds	5,368,948	4,855,808
Mutual funds	<u>10,664,114</u>	<u>10,396,620</u>
	<u>\$ 91,947,093</u>	<u>85,618,968</u>

The investments noted above are summarized on the statement of financial position as follows at December 31:

	<u>2012</u>	<u>2011</u>
Investments	\$ 72,049,409	67,063,437
Investment funds held in trust for others	19,824,569	18,485,541
Investment funds held for the benefit of others	<u>73,115</u>	<u>69,990</u>
	<u>\$ 91,947,093</u>	<u>85,618,968</u>

The Consolidated Income (I) and Consolidated Growth (G) funds are assets maintained on deposit with a bank. These funds consist primarily of United States government and agency securities (I fund) and common stocks of major corporations (G fund), and are being administered as open-end investment trusts. The Diocese has included its proportionate share of the assets based upon current fair values. See Note 12 for fair value disclosures.

5. GIFT ANNUITY:

ECSF is the recipient of a split-interest gift annuity consisting of common stock with fair value of \$57,366 and \$61,124 at December 31, 2012 and 2011, respectively. The agreement for this annuity (dated December 20, 1999), provides for the irrevocable transfer of this gift to ECSF in exchange for the payment to the donors of an annuity at a rate of 7.1% or an annual sum of \$10,650. Upon death of the donors, the Trustee shall surrender the funds and distribute a payment of such proceeds as follows: 75% is retained by ECSF and 25% to St. Timothy's Episcopal Church, Anderson Township. The recorded liability is calculated by an actuary and is based on the expected lives of the donors. The gift annuity payable was \$55,328 and \$59,720 at December 31, 2012 and 2011 and is included in accrued liabilities.

6. PROPERTY AND EQUIPMENT:

Property and equipment consist of the following as of December 31:

	<u>2012</u>	<u>2011</u>
Congregation properties	\$ 1,295,427	445,427
Camp and conference center	7,013,888	6,961,478
Diocesan office	1,201,705	1,201,705
Procter farm	349,461	349,461
Other properties	921,508	1,709,499
Furniture and equipment	<u>269,089</u>	<u>297,689</u>
	11,051,078	10,965,259
Less accumulated depreciation	<u>5,051,062</u>	<u>4,706,623</u>
	<u>\$ 6,000,016</u>	<u>6,258,636</u>

7. OPERATING LEASES:

The Diocese leases office equipment for the offices and an automobile for the Diocesan Bishop. The leases expire on various dates through 2016. Total rent expense was \$11,357 and \$17,092 in 2012 and 2011, respectively. The required minimum future rental payments for the operating leases are as follows:

2013	\$ 8,733
2014	8,733
2015	3,816
2016	<u>3,369</u>
Total minimum future lease payments	<u>\$ 24,651</u>

8. NET ASSETS:

Temporarily restricted net assets as of December 31, 2012 and 2011 of \$325,837 and \$541,204 respectively, are primarily available for the purposes of capital improvements and property maintenance, and congregational development. Permanently restricted net assets consist of the following as of December 31:

	<u>2012</u>	<u>2011</u>
Endowment funds	\$ 34,325,363	34,325,363
Trust funds held by others	758,317	758,317
Donor restricted loan funds	<u>628,684</u>	<u>628,684</u>
	<u>\$ 35,712,364</u>	<u>35,712,364</u>

The income from the endowment investments is primarily available for relief to the needy, missionary work and operations of the Diocese.

9. ENDOWMENT AND QUASI-ENDOWMENT FUNDS:

Generally accepted accounting principles require that the net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments (quasi-endowments), are classified and reported based on the existence or absence of donor-imposed restrictions. The Diocese's endowments and quasi-endowments fund consists of the funds established to provide income to operations, and consists of both donor-restricted (endowment) and board-designated funds.

The Diocese has interpreted the State Prudent Management of Institutional Funds Act (SPMIFA) 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 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, (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 the Diocese in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA,

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 fund
2. The purposes of the Diocese and the donor-restricted endowment fund
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
7. The investment policies of the Diocese

The Diocese classifies the unappropriated portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets as unrestricted when donor stipulations have been satisfied through expenditures from other Diocesan resources.

Endowment and quasi-endowments fund net asset composition by type of fund is as follows at December 31, 2012:

	<u>Unrestricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor – restricted endowment	\$ -	34,325,363	34,325,363
Board – designated endowment	<u>36,532,965</u>	<u>-</u>	<u>36,532,965</u>
Total	\$ <u>36,532,965</u>	<u>34,325,363</u>	<u>70,858,328</u>

Diocese of Southern Ohio, ECSF and Gabriel's Place
Notes to the Combined Financial Statements
December 31, 2012 and 2011

Endowment and quasi-endowments fund net asset composition by type of fund is as follows at December 31, 2011:

	<u>Unrestricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Donor - restricted endowment	\$ -	34,325,363	34,325,363
Board - designated endowment	<u>31,906,231</u>	-	<u>31,906,231</u>
Total	<u>\$ 31,906,231</u>	<u>34,325,363</u>	<u>66,231,594</u>

Changes in endowment and quasi-endowments fund net assets are as follows for the year ended December 31, 2012:

	<u>Unrestricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Endowment and quasi-endowments fund net assets at beginning of year	\$ 31,906,231	34,325,363	66,231,594
Interest and dividend income	1,665,326	-	1,665,326
Realized and unrealized gain on investments	5,697,451	-	5,697,451
Contributions	-	-	-
Spending appropriation	(2,608,111)	-	(2,608,111)
Investment fees	<u>(127,932)</u>	-	<u>(127,932)</u>
Endowments and quasi endowments fund net assets at end of year	<u>\$ 36,532,965</u>	<u>34,325,363</u>	<u>70,858,328</u>

Changes in endowment and quasi-endowments fund are as follows for the year ended December 31, 2011:

	<u>Unrestricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Endowment and quasi-endowments fund net assets at beginning of year	\$ 32,559,232	34,325,363	66,884,595
Interest and dividend income	1,533,007	-	1,533,007
Realized and unrealized gain on investments	471,271	-	471,271
Contributions	-	-	-
Spending appropriation	(2,534,375)	-	(2,534,375)
Investment fees	<u>(122,904)</u>	-	<u>(122,904)</u>
Endowments and quasi endowments fund net assets at end of year	<u>\$ 31,906,231</u>	<u>34,325,363</u>	<u>66,231,594</u>

Reconciliation of endowments and quasi-endowments funds net assets to total net assets for the year ended December 31, 2012:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment and quasi-endowments fund net assets	\$ 36,532,965	-	34,325,363	70,858,328
Other funds net assets	<u>10,503,981</u>	<u>325,837</u>	<u>1,387,001</u>	<u>12,216,819</u>
Total net assets at end of year	\$ <u>47,036,946</u>	<u>325,837</u>	<u>35,712,364</u>	<u>83,075,147</u>

Reconciliation of endowments and quasi-endowments funds net assets to total net assets for the year ended December 31, 2011:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment and quasi-endowments fund net assets	\$ 31,906,231	-	34,325,363	66,231,594
Other funds net assets (deficit)	<u>9,965,529</u>	<u>541,204</u>	<u>1,387,001</u>	<u>11,893,734</u>
Total net assets at end of year	\$ <u>41,871,760</u>	<u>541,204</u>	<u>35,712,364</u>	<u>78,125,328</u>

Return objectives and risk parameters

The Diocese has adopted investment and spending policies for endowment assets that attempt to provide long-term portfolio growth and the desired annual payout as specified in the applicable spending policy. Under this policy as approved by the Board of Trustees, the endowment assets are invested as follows:

Equity	60% to 80%
Fixed Income	20% to 40%
Cash Equivalents	0% to 10%

The performance objectives will be measured against appropriate industry benchmarks such as the S&P 500, Russell Mid Cap, Russell 2000 and MSCI EAFE for equities and benchmarked by the Barclays Capital Aggregate Bond Index for its fixed income endowment investments.

Strategies employed for achieving objectives

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 that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending policy and how the investment objectives relate to spending policy

The Diocese has a policy of appropriating for distribution up to 4.5% of its endowment funds' average fair value over the prior 12 quarters through the December 31 fiscal year in which the distribution is planned.

In establishing this policy, the Diocese considered the long-term expected return on its endowment. Accordingly, this spending policy should, over time, protect the inflation-adjusted value of the endowment and, consequently, allow inflation-adjusted spending to occur into the distant future. This is consistent with the Diocese's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

10. EMPLOYEE BENEFIT PLANS:

The Diocese contributed \$193,962 and \$184,036 during the years ended December 31, 2012 and 2011, respectively, to multi-employer defined benefit plans. All clergy and lay employees of the Diocese are covered by multi-employer defined benefit plans. These plans are not administered by the Diocese. The plans are provided by the Church Pension Group. These plans require Diocese contributions equal to 18% of cash compensation for clergy and 9% of cash compensation for lay employees. During 2011, the plans were amended to include supplemental health insurance options for retired personnel. The Diocese may be liable, in the event of plan terminations or its withdrawal from the plans, for a portion of the plans' unfunded vested benefits. Currently there is no unfunded withdrawal liability nor does the Diocese have any present intentions to withdraw from the plans.

Information on the Diocese specific plan is detailed below.

<u>Fund name</u>	<u>Clergy Pension Plan</u>	<u>Episcopal Church Lay Employees' Retirement Plan</u>
Employee identification number	13-5562193	13-5562193
Plan number	DSOH CLER F982 CLER	DSOH LAYO F982 LAYO
Pension protection act zone status	Not Available	Not Available
Rehabilitation plan	No	No
Surcharge	No	No
Expiration of labor contract	Not Applicable	Not Applicable
Diocese contributions > 5% of the plan	No	No
Diocese contributions	\$127,582	\$66,380

The pension protection act certified zone status was not available for the plans. The following table represents the plan assets, accumulated benefit obligations and funded status:

<u>March 31, 2013 (in thousands)</u>	<u>Clergy Pension Plan</u>	<u>Episcopal Church Lay Employees' Retirement Plan</u>
Plan net assets	\$ 7,594,930	121,527
Accumulated plan benefit obligations	<u>6,019,440</u>	<u>160,257</u>
Surplus (deficit)	\$ <u>1,575,490</u>	<u>(38,730)</u>
Funded Status	>80%	65-80%

11. POSTRETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS:

The Diocese provides certain health care and life insurance benefits for retired clergy and lay employees based on the number of years of service rendered. Diocesan clergy and lay employees will become eligible for those benefits if they reach retirement while employed in or by the Diocese. The Diocese funds these benefits on a current basis which totaled \$258,233 and \$202,362 in 2012 and 2011, respectively.

During 2011, the Diocese revised requirements for participants, thereby significantly decreasing the participation mix and the related postretirement benefit obligation. The burden of most of the retiree health insurance was transferred to a multi-employer pension fund.

Postretirement benefit (income) expense was \$(184,008) and \$834,729 in 2012 and 2011, respectively. The components of this expense were:

	<u>2012</u>	<u>2011</u>
Service cost of benefits earned	\$ 627	440,390
Interest cost on liability	1,941	508,381
Net amortization and deferral of actuarial gain	<u>(186,576)</u>	<u>(114,042)</u>
Net periodic postretirement (benefit) expense	\$ <u>(184,008)</u>	<u>834,729</u>

The accumulated postretirement benefit obligation is as follows at December 31:

	<u>2012</u>	<u>2011</u>
Retirees	\$ 1,700	73,659
Fully eligible active plan participants	250	5,356
Ineligible active plan participants	<u>419</u>	<u>2,688</u>
Postretirement benefits accrued other than pensions	\$ <u>2,369</u>	<u>81,703</u>

For measurement purposes, the annual rate of increase in the per capita cost of covered benefits (i.e., healthcare cost trend rate) was assumed for 2012 and 2011 as follows:

	<u>2012</u>	<u>2011</u>
Retirees - Lay	4%	6%
Retirees - Clergy	-	19%

The rate was assumed to change to 7% for subsequent years through 2024 and then 6% by the year 2025 and remain at that level thereafter. The healthcare cost trend rate assumption has a significant effect on the amounts reported. For example, increasing the assumed healthcare cost trend rates by one percentage point in each year would increase the accumulated postretirement benefit obligation as of December 31, 2012 by approximately \$238, and the aggregate service and interest cost components of net periodic postretirement benefit cost for the years ended December 31, 2012 by approximately \$44. The weighted average discount rate used in determining the accumulated postretirement benefit obligation was 4.5% as of December 31, 2012.

Benefits to be paid under the plan over the next ten years are as follows:

2013	\$ 276
2014	248
2015	222
2016	197
2017	176
2018 – 2022	<u>710</u>
	<u>\$ 1,829</u>

12. FAIR VALUES MEASUREMENTS:

Generally accepted accounting principles defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value as follows:

Level 1 – Valuations based on quoted price in active markets for identical assets or liabilities that the Diocese has the ability to access. Valuation adjustments are not applied to Level 1 instruments. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these items does not entail a significant degree of judgment.

Level 2 – Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly.

Level 3 – Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The availability of observable inputs can vary and is affected by a wide variety of factors. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the

determination of fair value requires more judgment. Accordingly, the degree of judgment exercised in determining fair value is greatest for instruments categorized in Level 3.

Fair value methods and assumptions on investments consisting of cash equivalents, common stocks, mutual funds and US Government securities are based on values in public exchange. Investments in agency bonds, corporate bonds, mortgage bonds, municipal bonds and hedge funds with regularly published net asset values that are not quoted on an exchange, but are traded in active markets are valued on Level 2 inputs using prices obtained from our custodian, which used third party data service providers. Investments in funds held in trust for others, investments in funds held for the benefit of others and gift annuities are valued on Level 3 inputs using prices of the underlying assets invested that are obtained from our custodians, which used third party data service providers, without adjustment.

The following tables present the assets and liabilities as of December 31, 2012 and 2011 that are measured at fair value on a recurring basis and are categorized using the fair value hierarchy.

	December 31, <u>2012</u>	Quoted prices in active markets for identical assets or liabilities <u>(Level 1)</u>	Significant other observable inputs <u>(Level 2)</u>	Significant unobservable inputs <u>(Level 3)</u>
<u>Investments:</u>				
Cash and equivalents	\$ 1,520,140	1,520,140	-	-
Industrials	3,463,645	3,463,645	-	-
Consumer discretionary	4,265,737	4,265,737	-	-
Consumer staples	4,024,412	4,024,412	-	-
Energy	3,651,669	3,651,669	-	-
Financial	5,571,784	5,571,784	-	-
Materials	1,697,127	1,697,127	-	-
Information technology	6,310,702	6,310,702	-	-
Utilities	1,245,740	1,245,740	-	-
Health care	4,849,624	4,849,624	-	-
Telecommunications	901,165	901,165	-	-
International	5,491,497	5,491,497	-	-
Mid cap	455,835	455,835	-	-
Small cap	3,680,135	3,680,135	-	-
Treasury	10,117,890	10,117,890	-	-
Agency	4,833,237	-	4,833,237	-
Corporate	7,260,486	-	7,260,486	-
Mortgage	396,439	-	396,439	-
Municipal	268,369	-	268,369	-
Hedge funds	2,043,776	-	2,043,776	-
Investment funds held in trust for others	19,824,569	-	-	19,824,569
Investment funds held for the benefit of others	73,115	-	-	73,115
Investment - gift annuity	57,366	-	-	57,366
	<u>\$ 92,004,459</u>	<u>57,247,102</u>	<u>14,802,307</u>	<u>19,955,050</u>

Diocese of Southern Ohio, ECSF and Gabriel's Place
Notes to the Combined Financial Statements
December 31, 2012 and 2011

	December 31, <u>2011</u>	Quoted prices in active markets for identical assets or liabilities (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
<u>Investments:</u>				
Cash and equivalents	\$ 1,170,228	1,170,228	-	-
Industrials	3,855,480	3,855,480	-	-
Consumer discretionary	4,704,841	4,704,841	-	-
Consumer staples	4,083,373	4,083,373	-	-
Energy	4,040,383	4,040,383	-	-
Financial	4,338,196	4,338,196	-	-
Materials	1,556,048	1,556,048	-	-
Information technology	6,920,739	6,920,739	-	-
Utilities	965,649	965,649	-	-
Health care	4,333,740	4,333,740	-	-
Telecommunications	900,447	900,447	-	-
International	5,179,628	5,179,628	-	-
Mid cap	893,688	893,688	-	-
Small cap	3,284,970	3,284,970	-	-
Treasury	3,904,050	3,904,050	-	-
Agency	5,909,334	-	5,909,334	-
Corporate	7,625,114	-	7,625,114	-
Mortgage	694,012	-	694,012	-
Municipal	373,024	-	373,024	-
Hedge funds	2,330,493	-	2,330,493	-
Investment funds held In trust for others	18,485,541	-	-	18,485,541
Investment funds held For the benefit of others	69,990	-	-	69,990
Investment - gift annuity	61,124	-	-	61,124
	<u>\$ 85,680,092</u>	<u>50,131,460</u>	<u>16,931,977</u>	<u>18,616,655</u>

Diocese of Southern Ohio, ECSF and Gabriel's Place
Notes to the Combined Financial Statements
December 31, 2012 and 2011

The following is a reconciliation of the investments valued at Level 3 inputs as of December 31, 2012:

	Investment funds held in trust <u>for others</u>	Investment funds held for the benefit <u>of others</u>	Investment - <u>gift annuity</u>	<u>Total</u>
Balance as of January 1, 2012	\$ 18,485,541	69,990	61,124	18,616,655
Net realized and unrealized gains (losses), interest & dividends	1,339,028	-	-	1,339,028
Change in value of trusts held for the benefit of others	-	3,125	-	3,125
Change in value of gift annuity	<u>-</u>	<u>-</u>	<u>(3,758)</u>	<u>(3,758)</u>
Balance as of December 31, 2012	<u>\$ 19,824,569</u>	<u>73,115</u>	<u>57,366</u>	<u>19,955,050</u>

The following is a reconciliation of the investments valued at Level 3 inputs as of December 31, 2011:

	Investment funds held in trust <u>for others</u>	Investment funds held for the benefit <u>of others</u>	Investment - <u>gift annuity</u>	<u>Total</u>
Balance as of January 1, 2011	\$ 19,423,674	69,790	69,140	19,562,604
Net realized and unrealized gains (losses), interest & dividends	(938,133)	-	-	(938,133)
Change in value of trusts held for the benefit of others	-	200	-	200
Change in value of gift annuity	<u>-</u>	<u>-</u>	<u>(8,016)</u>	<u>(8,016)</u>
Balance as of December 31, 2011	<u>\$ 18,485,541</u>	<u>69,990</u>	<u>61,124</u>	<u>18,616,655</u>

SUPPLEMENTARY INFORMATION

Diocese of Southern Ohio, ECSF, and Gabriel's Place
Schedule of Combining Financial Position Fund Information
December 31, 2012

	DSO Funds	Church Foundation Funds	412 Sycamore Funds	Endowment and Quasi-Endowment Funds	Bishop's Discret Fd	Faith-in-Life Funds	Procter Cont Ctr	ECSF	Gabriel's Place	Subtotal	Eliminations	Total
Assets:												
Cash and cash equivalents	\$ 952,191	516,844	242,948	-	274,090	182,423	14,894	131,186	73,471	2,388,047	-	2,388,047
Accounts and interest receivable	539,339	-	-	-	-	-	16,136	29,650	-	585,125	-	585,125
Due from other funds	281,968	126,558	790,501	4,117,159	-	-	40,000	7,060	-	5,363,246	(5,363,246)	-
Notes receivable, net	103,000	151,635	1,895,337	525,583	-	-	-	-	-	2,675,555	-	2,675,555
Prepaid expenses	4,235	-	-	-	-	-	748	-	-	4,983	-	4,983
Investments	1,521,161	1,288,428	-	66,339,917	-	1,770,300	-	1,149,603	-	72,049,409	-	72,049,409
Investment funds held in trust by others	-	-	-	19,824,569	-	-	-	-	-	19,824,569	-	19,824,569
Investment funds held for the benefit of others	-	-	-	73,115	-	-	-	-	-	73,115	-	73,115
Investment - gift annuity	-	-	-	-	-	-	-	57,366	-	57,366	-	57,366
Property and equipment, net	-	5,996,907	-	-	-	-	-	-	3,109	6,000,016	-	6,000,016
Total assets	\$ 3,401,894	8,060,372	2,928,786	90,880,343	274,090	1,952,723	71,778	1,374,865	76,580	109,021,431	(5,363,246)	103,658,185
Liabilities:												
Accounts payable and accrued liabilities	\$ 183,440	48,682	-	-	-	-	12,829	57,273	6,317	308,541	-	308,541
Deferred revenue	-	-	-	-	-	-	20,244	-	-	20,244	-	20,244
Grants payable	334,200	20,000	-	-	-	-	-	-	-	354,200	-	354,200
Postretirement benefits accrued other than pensions	2,369	-	-	-	-	-	-	-	-	2,369	-	2,369
Funds held for the benefit of MP Lee Retirement Community	-	-	-	19,824,569	-	-	-	-	-	19,824,569	-	19,824,569
Funds held for the benefit of St. Luke, Cincinnati	-	-	-	73,115	-	-	-	-	-	73,115	-	73,115
Due to other funds	66,115	798,336	4,004,155	124,331	-	2,002	366,431	60	1,816	5,363,246	(5,363,246)	-
Total liabilities	586,124	867,018	4,004,155	20,022,015	-	2,002	399,504	57,333	8,133	25,946,284	(5,363,246)	20,583,038
Net assets:												
Unrestricted	2,719,127	6,461,436	(1,075,369)	36,532,965	274,090	1,192,404	(327,726)	1,218,354	41,665	47,036,946	-	47,036,946
Temporarily restricted	96,643	103,234	-	-	-	-	-	99,178	26,782	325,837	-	325,837
Permanently restricted	-	628,684	-	34,325,363	-	758,317	-	-	-	35,712,364	-	35,712,364
Total net assets	2,815,770	7,193,354	(1,075,369)	70,858,328	274,090	1,950,721	(327,726)	1,317,532	68,447	83,075,147	-	83,075,147
Total liabilities and net assets	\$ 3,401,894	8,060,372	2,928,786	90,880,343	274,090	1,952,723	71,778	1,374,865	76,580	109,021,431	(5,363,246)	103,658,185

Diocese of Southern Ohio and ECSF
Schedule of Combining Financial Position Fund Information
December 31, 2011

	DSO Funds	Church Foundation Funds	412 Sycamore Funds	Endowment and Quasi-Endowment Funds	Bishop's Discret. Fd	Faith-in-Life Funds	Procter Conf Ctr	ECSF	Subtotal	Eliminations	Total
Assets:											
Cash and cash equivalents	\$ 1,100,835	203,987	138,097	-	260,160	199,288	35,079	149,323	2,086,769	-	2,086,769
Accounts and interest receivable	532,102	-	-	-	-	-	9,211	29,580	570,893	-	570,893
Due from other funds	317,033	851,558	-	4,187,920	-	-	-	7,204	5,363,715	(5,363,715)	-
Notes receivable, net	109,129	187,028	2,789,476	525,000	-	-	-	-	3,610,633	-	3,610,633
Prepaid expenses	4,369	-	-	-	-	-	5,684	366	10,419	-	10,419
Investments	1,504,131	1,173,738	-	61,689,674	-	1,619,559	-	1,076,335	67,063,437	-	67,063,437
Investment funds held in trust by others	-	-	-	18,485,541	-	-	-	-	18,485,541	-	18,485,541
Investment funds held for the benefit of others	-	-	-	69,990	-	-	-	-	69,990	-	69,990
Investment - gift annuity	-	-	-	-	-	-	-	61,124	61,124	-	61,124
Property and equipment, net	-	6,258,636	-	-	-	-	-	-	6,258,636	-	6,258,636
Total assets	\$ 3,567,599	8,674,947	2,927,573	84,958,125	260,160	1,818,847	49,974	1,323,932	103,581,157	(5,363,715)	98,217,442
Liabilities:											
Accounts payable and accrued liabilities	\$ 79,035	58,046	-	-	11,584	-	10,427	59,814	218,906	-	218,906
Deferred revenue	-	-	-	-	-	-	7,739	-	7,739	-	7,739
Grants payable	392,650	60,000	-	-	-	-	-	-	452,650	-	452,650
Postretirement benefits accrued other than pensions	81,703	-	-	-	-	-	-	-	81,703	-	81,703
Funds held for the benefit of St. Mary Magdalene, Maineville	-	775,585	-	-	-	-	-	-	775,585	-	775,585
Funds held for the benefit of MP Lee Retirement Community	-	-	-	18,485,541	-	-	-	-	18,485,541	-	18,485,541
Funds held for the benefit of St. Luke, Cincinnati	-	-	-	69,990	-	-	-	-	69,990	-	69,990
Due to other funds	93,273	729,000	4,011,215	171,000	5,109	2,000	351,913	205	5,363,715	(5,363,715)	-
Total liabilities	646,661	1,522,631	4,011,215	18,728,531	16,693	2,000	370,079	60,019	25,455,829	(5,363,715)	20,092,114
Net assets:											
Unrestricted	2,616,341	6,320,398	(1,083,642)	31,906,231	243,467	1,058,530	(350,135)	1,160,570	41,871,760	-	41,871,760
Temporarily restricted	304,597	103,234	-	-	-	-	30,030	103,343	541,204	-	541,204
Permanently restricted	-	628,684	-	34,325,363	-	758,317	-	-	35,712,364	-	35,712,364
Total net assets	2,920,938	7,052,316	(1,083,642)	66,231,594	243,467	1,816,847	(320,105)	1,263,913	78,125,328	-	78,125,328
Total liabilities and net assets	\$ 3,567,599	8,674,947	2,927,573	84,958,125	260,160	1,818,847	49,974	1,323,932	103,581,157	(5,363,715)	98,217,442

The supplementary schedule has been included herein to provide information about funds which make up the combined statement of financial position. The assets, liabilities and net assets of the Diocese for internal record-keeping purposes are maintained in seven self-balancing fund groups, ECSF and Gabriel's Place as follows:

- DSO Funds include unrestricted, designated by Trustees of the Diocese, and restricted resources representing that portion of expendable funds available for the support of Diocesan operations.
- Church Foundation Funds include resources made available by the Trustees of the Church or ECSF related to property acquisition, maintenance and improvement, and funds previously expended for property.
- 412 Sycamore Funds include funds made available by Trustees of the Diocese for property acquisition and construction by congregations and Diocesan clergy.
- Endowments and Quasi-Endowment Funds represent funds that are subject to restrictions of gift instruments requiring that principal be invested and maintained in perpetuity with only the income and certain appreciation as limited by the donor or the law being available for expenditure. Quasi-endowment funds have been established by the Trustees of the Diocese for the same purposes as endowment funds and are included in this fund group; however, any portion of these funds may be expended.
- Bishop Discretionary Funds are used for Clergy Professional Development grants and Clergy emergency assistance. These funds are also used for closed congregation assistance to maintain the property.
- The Faith-in-Life Funds were raised during the Diocesan Second Century Campaign. The interest earned on the endowment finances the Faith-in-Life Committee's activities which are reported in its Operating Fund.
- Procter Conference Funds are used only for the operation of the Diocesan Camp and Conference Center.
- ECSF is organized to support Episcopal Church congregations in Southern Ohio in their volunteer response to community needs for educational, poverty relief, trauma counseling, and other social services.
- Gabriel's Place is organized to provide a safe, beautiful and spiritually nourishing place for the Avondale Community.

