# Central Administrative Office of the Catholic Diocese of Arlington

**Financial Statements**
**as of June 30, 2015 and 2014 and Report Thereon**

# Central Administrative Office of the Catholic Diocese of Arlington
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## June 30, 2015 and 2014

CliftonLarsonAllen LLP
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## INDEPENDENT AUDITORS' REPORT

Most Reverend Paul S. Loverde
Bishop of the Catholic Diocese of Arlington
Central Administrative Office of the Catholic Diocese
Arlington, Virginia

We have audited the accompanying financial statements of the Central Administrative Office of the Catholic Diocese of Arlington (the Chancery), which comprise the statements of financial position as of June 30, 2015 and 2014, and the related statements of activities 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.

### *Auditors' 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 auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

### *Opinion*

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

CliftonLarsonAllen LLP

**CliftonLarsonAllen LLP**

St. Cloud, Minnesota
October 27, 2015

## Central Administrative Office of the Catholic Diocese of Arlington
## Statements of Financial Position
## As of June 30, 2015 and 2014

| | 2015 | 2014 |
|---|---|---|
| **Assets** | | |
| Cash and cash equivalents | $ 11,314,349 | $ 9,828,762 |
| Accounts receivable, net | 1,702,237 | 1,782,586 |
| Accrued interest receivable | 158,645 | 157,131 |
| Bishop's Lenten Appeal pledges receivable | 3,296,887 | 3,771,899 |
| Bequests and major gifts pledges receivable | 8,833,438 | 10,779,755 |
| Beneficial interest in residuary estates | 14,500,000 | - |
| Investments | 214,787,578 | 200,950,676 |
| Prepaid expenses and other assets | 1,139,932 | 852,589 |
| Unamortized bond costs | 158,416 | 171,174 |
| Interest rate swap agreement | 93,245 | 338,502 |
| Demand notes and loans receivable | | |
| Paul VI High School | 3,558,760 | 3,798,634 |
| 200 North Glebe Road, Inc. | 3,454,286 | 4,034,286 |
| Property, equipment and land, net | 106,635,211 | 106,710,155 |
| Construction in progress and assets not yet placed in service | 116,880 | 1,583,282 |
| Land restricted for high school | 14,500,000 | 14,500,000 |
| Total assets | $ 384,249,864 | $ 359,259,431 |
| **Liabilities and Net Assets** | | |
| Liabilities | | |
| Deposits held in custody for others | $ 1,723,259 | $ 1,683,260 |
| Accounts payable and accrued expenses | 6,095,209 | 5,444,284 |
| Accrued interest payable | 39,653 | 41,892 |
| Unearned revenue | 477,660 | 57,393 |
| Notes payable, net of discount | 41,269 | 103,130 |
| Amounts held on behalf of other diocesan entities | 92,642,400 | 89,131,460 |
| Annuity payment liability | 257,075 | 270,189 |
| Arlington Diocese Educational Foundation (ADEF) funds held for schools | 2,614,255 | 2,651,903 |
| Accrued pension liability, priests | 8,680,358 | 6,707,287 |
| Postretirement health benefit obligation | 11,724,650 | 8,677,709 |
| Bonds payable | 19,601,783 | 20,479,836 |
| Total liabilities | 143,897,571 | 135,248,343 |
| Net assets | | |
| Unrestricted | | |
| Current operations | 32,995,036 | 35,856,836 |
| Invested in property, equipment and land | 90,841,769 | 91,838,276 |
| Functioning as endowment | 12,112,628 | 11,761,241 |
| Designated | 14,734,587 | 10,395,939 |
| Total unrestricted | 150,684,020 | 149,852,292 |
| Temporarily restricted | 51,864,791 | 50,368,033 |
| Permanently restricted | 37,803,482 | 23,790,763 |
| Total net assets | 240,352,293 | 224,011,088 |
| Total liabilities and net assets | $ 384,249,864 | $ 359,259,431 |

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

## Central Administrative Office of the Catholic Diocese of Arlington
## Statement of Activities
## For the year ended June 30, 2015

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---|---|---|---|
| Operating revenues and support | | | | |
| Bishop's Lenten Appeal | $ 16,134,102 | $ - | $ - | $ 16,134,102 |
| Operational assessment | 7,451,644 | - | - | 7,451,644 |
| Investment income for operations | 1,800,000 | - | - | 1,800,000 |
| Transmittal fees | 157,502 | - | - | 157,502 |
| Contributions, bequests and major gifts | 5,609,114 | 10,125,212 | 12,862,719 | 28,597,045 |
| Program revenue | 2,867,786 | - | - | 2,867,786 |
| Reclassification of donor restricted net assets | - | (1,150,000) | 1,150,000 | - |
| Satisfaction of temporary restrictions | 8,494,760 | (8,494,760) | - | - |
| Total operating revenues and support | 42,514,908 | 480,452 | 14,012,719 | 57,008,079 |
| Operating expenses | | | | |
| Program services | | | | |
| Pastoral | 9,384,216 | - | - | 9,384,216 |
| Religious personnel development | 3,225,510 | - | - | 3,225,510 |
| Education | 7,399,253 | - | - | 7,399,253 |
| Social services | 4,410,636 | - | - | 4,410,636 |
| Supporting services | | | | |
| Diocesan administration and parochial support | 12,613,368 | - | - | 12,613,368 |
| Bishop's Lenten Appeal | 854,882 | - | - | 854,882 |
| Total operating expenses | 37,887,865 | - | - | 37,887,865 |
| Change in net assets from operations | 4,627,043 | 480,452 | 14,012,719 | 19,120,214 |
| Other changes in net assets | | | | |
| Investment income less amount included in operations, net | (516,594) | 1,393,908 | - | 877,314 |
| Bond interest and related expenses | (404,127) | - | - | (404,127) |
| Unrealized loss on swap agreement | (245,257) | - | - | (245,257) |
| Insurance programs | 1,526,841 | - | - | 1,526,841 |
| Change in unfunded pension liability, priests | (2,232,590) | - | - | (2,232,590) |
| Change in unfunded postretirement health obligation | (3,046,941) | - | - | (3,046,941) |
| Net property gains | - | - | - | - |
| Rental income - diocesan properties | 1,579,007 | - | - | 1,579,007 |
| Loan reserve increase - related party | (833,256) | - | - | (833,256) |
| Satisfaction of temporary restrictions | 377,602 | (377,602) | - | - |
| Total other changes in net assets | (3,795,315) | 1,016,306 | - | (2,779,009) |
| Change in net assets | 831,728 | 1,496,758 | 14,012,719 | 16,341,205 |
| Net assets, beginning of year | 149,852,292 | 50,368,033 | 23,790,763 | 224,011,088 |
| Net assets, end of year | $150,684,020 | $ 51,864,791 | $ 37,803,482 | $ 240,352,293 |

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

## Central Administrative Office of the Catholic Diocese of Arlington
## Statement of Activities
## For the year ended June 30, 2014

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---|---|---|---|
| Operating revenues and support | | | | |
| Bishop's Lenten Appeal | $ 16,244,788 | $ - | $ - | $ 16,244,788 |
| Operational assessment | 7,428,795 | - | - | 7,428,795 |
| Investment income for operations | 1,460,000 | - | - | 1,460,000 |
| Transmittal fees | 149,142 | - | - | 149,142 |
| Contributions, bequests and major gifts | 1,098,700 | 17,552,803 | 2,300,281 | 20,951,784 |
| Program revenue | 2,518,054 | - | - | 2,518,054 |
| Satisfaction of temporary restrictions | 10,731,374 | (10,731,374) | - | - |
| Total operating revenues and support | 39,630,853 | 6,821,429 | 2,300,281 | 48,752,563 |
| Operating expenses | | | | |
| Program services | | | | |
| Pastoral | 8,953,819 | - | - | 8,953,819 |
| Religious personnel development | 3,314,166 | - | - | 3,314,166 |
| Education | 10,374,890 | - | - | 10,374,890 |
| Social services | 4,170,585 | - | - | 4,170,585 |
| Supporting services | | | | |
| Diocesan administration and parochial support | 11,838,556 | - | - | 11,838,556 |
| Bishop's Lenten Appeal | 783,085 | - | - | 783,085 |
| Total operating expenses | 39,435,101 | - | - | 39,435,101 |
| Change in net assets from operations | 195,752 | 6,821,429 | 2,300,281 | 9,317,462 |
| Other changes in net assets | | | | |
| Investment income less amount included in operations, net | 8,298,281 | 7,201,456 | - | 15,499,737 |
| Bond interest and related expenses | (1,273,900) | - | - | (1,273,900) |
| Unrealized loss on swap agreement | (214,897) | - | - | (214,897) |
| Insurance programs | 318,199 | - | - | 318,199 |
| Change in unfunded pension liability, priests | (1,158,012) | - | - | (1,158,012) |
| Change in unfunded postretirement health obligation | (1,193,647) | - | - | (1,193,647) |
| Net property gains | 310,104 | - | - | 310,104 |
| Rental income - diocesan properties | 1,459,152 | - | - | 1,459,152 |
| Loan reserve increase - related party | (1,314,918) | - | - | (1,314,918) |
| Satisfaction of temporary restrictions | 1,526,000 | (1,526,000) | - | - |
| Total other changes in net assets | 6,756,362 | 5,675,456 | - | 12,431,818 |
| Change in net assets | 6,952,114 | 12,496,885 | 2,300,281 | 21,749,280 |
| Net assets, beginning of year | 142,900,178 | 37,871,148 | 21,490,482 | 202,261,808 |
| Net assets, end of year | $149,852,292 | $ 50,368,033 | $ 23,790,763 | $ 224,011,088 |

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

# Central Administrative Office of the Catholic Diocese of Arlington
# Statements of Cash Flows
# For the years ended June 30, 2015 and 2014

| | 2015 | 2014 |
|---|---|---|
| Cash flows from operating activities | | |
| Change in net assets | 16,341,205 | 21,749,280 |
| Adjustments to reconcile change in net assets to net cash and cash equivalents provided by operating activities | | |
| Depreciation of property | 2,738,188 | 2,622,656 |
| Gain on sale of assets | - | (310,104) |
| Contributed real and personal property | - | (204,500) |
| (Decrease) in allowance for uncollectible accounts receivable | (433) | (1,246) |
| Decrease (increase) in discount on major gifts pledges receivable | (44,835) | 430,654 |
| Loan reserve - related party | 833,257 | 1,314,918 |
| Unrealized and realized (gains) on investments, net | (1,370,217) | (15,838,221) |
| Unrealized loss on interest rate swap | 245,257 | 214,897 |
| Increase in amounts held on behalf of other diocesan entities | 1,937,409 | 4,127,511 |
| Decrease (increase) in accounts receivable | 81,277 | (522,055) |
| (Increase) decrease in accrued interest receivable | (1,514) | 30,135 |
| Decrease (increase) in BLA pledges receivable | 475,012 | (776,920) |
| Decrease (increase) in bequests and major gift pledges receivable | 1,991,152 | (9,204,372) |
| (Increase) in beneficial interest in residuary estates | (14,500,000) | - |
| (Increase) in prepaid expenses and other assets | (287,343) | (221,560) |
| Decrease in unamortized bond costs | 12,758 | 354,542 |
| Increase in deposits held in custody for others | 54,874 | 347,973 |
| Increase in accounts payable and accrued expenses | 753,739 | 390,604 |
| (Decrease) in ADEF funds held for schools | (46,882) | (50,913) |
| (Decrease) in accrued interest payable | (2,239) | (277,689) |
| Increase in unearned revenue | 420,267 | 917 |
| Increase (decrease) in accrued pension liability, priests | 1,973,071 | (341,988) |
| Increase in postretirement health benefit obligation | 3,046,941 | 1,193,647 |
| (Decrease) increase in annuity payment liability | (13,114) | 9,648 |
| Net cash and cash equivalents provided by operating activities | 14,637,830 | 5,037,814 |
| Cash flows from investing activities | | |
| Purchases of equipment | (1,299,656) | (2,469,478) |
| Proceeds from sale of property | - | 338,607 |
| Decrease in 200 North Glebe Road loan receivable | 580,000 | 300,000 |
| Loans to Saint John Paul the Great Catholic High School | (833,257) | (1,314,918) |
| Purchases of investments | (234,576,933) | (171,221,721) |
| Sales of investments | 223,678,138 | 165,488,797 |
| Net cash and cash equivalents (used in) investing activities | (12,451,708) | (8,878,713) |
| Cash flows from financing activities | | |
| Decrease in Paul VI High School loan receivable | 239,379 | 204,124 |
| Repayments of notes payable | (61,861) | (60,957) |
| Repayments of bonds payable and defeasance of bonds | (878,053) | (22,925,737) |
| Disbursements from bond defeasance escrow | - | 22,849,681 |
| Net cash and cash equivalents (used in) provided by financing activities | (700,535) | 67,111 |
| Net increase (decrease) in cash and cash equivalents | 1,485,587 | (3,773,788) |
| Cash and cash equivalents, at beginning of year | 9,828,762 | 13,602,550 |
| Cash and cash equivalents, at end of year | $ 11,314,349 | $ 9,828,762 |

*Continued*

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

## Central Administrative Office of the Catholic Diocese of Arlington
## Statements of Cash Flows
## For the years ended June 30, 2015 and 2014

| | | 2015 | | 2014 |
|---|---|---|---|---|
| Supplemental cash flow information | | | | |
| Interest paid on debt | $ | 497,248 | $ | 817,838 |
| | | | | |
| Supplemental schedule of non-cash investing and financing activities | | | | |
| Equipment purchases in accounts payable | $ | 77,691 | $ | 180,505 |
| Contributed investment, real property and personal property | $ | - | $ | 204,500 |

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

## 1. Nature of operations

The content of these financial statements is limited to the Central Administrative Office of the Catholic Diocese of Arlington (the Chancery). The Catholic Diocese of Arlington (the Diocese) consists of the 21 counties of the northern tier of Virginia, including the Northern Neck. The Chancery consists of various offices in order to organize events, monitor activities, coordinate efforts, and support the parishes and schools throughout the Diocese. The offices are classified into the following programs:

- Pastoral includes all offices primarily concerned with evangelization and communicating the Faith, such as the Office for Family Life, Office of Youth Ministry, Tribunal, Spanish Apostolate, Multicultural Ministries, Campus Ministries, the San Damiano Spiritual Life Center, and the St. Rose of Lima Priests' Retirement Villa.

- Religious Personnel Development includes offices associated with the formational and educational needs of priests and deacons and related activities, including the Office of Vocations.

- Education includes offices associated with Catholic school administration and oversight of parish-based religious education programs.

- Social Services includes diocesan support of Catholic Charities of the Diocese of Arlington, the Campaign for Human Development, Rice Bowl, Office for Protection of Children and Young People and other charitable contributions.

- Diocesan Administration and Parochial Support includes offices concerned with the overall diocesan administration including the Chancery, Communications, Planning, Construction and Facilities, Finance and Accounting, Human Resources and Employee Benefits, Development and Information Services. These offices also provide services in support of the parishes and schools of the Diocese.

- Bishop's Lenten Appeal (BLA) includes all expenses associated with the annual fundraising drive.

In fiscal year 2013, the Chancery launched the Leadership Gift Initiative (LGI), a targeted major gift campaign. The goal of the LGI is to raise a minimum of $55 million by the year 2015 in support of the most critical needs of the diocese in the areas of Catholic education, New Evangelization, support for our retired priests, Catholic Charities programs and various capital improvements.

## 2. Basis of presentation and summary of significant accounting policies

### Basis of presentation and combination

The financial statements include the accounts of the Chancery and centralized administrative and diocesan functions under the control of the Bishop of Arlington (the Diocesan Bishop). They do not include the accounts for the Catholic Charities of the Diocese of Arlington (Catholic Charities), the Arlington Catholic Herald, 200 North Glebe Road, Inc. Arlington Diocesan Investment and Loan Corporation (DIAL Corp), The Foundation for the Catholic Diocese of Arlington, Inc. (The Foundation), or the Diocese of Arlington Scholarship Foundation, Inc. (Scholarship Foundation), over which the Diocesan Bishop exercises control, and are reported separately. All intercompany transactions and balances have been eliminated.

The financial statements also do not include the accounts of organizations within the Diocese such as parishes, parish schools, diocesan high schools, cemeteries, homes, and offices and other institutions owned and operated by religious orders of men and women. These organizations may or may not be separate corporations under civil law; however, each is an operating entity distinct from the Chancery, maintains separate accounts and carries on its own services and programs. Transactions between the Chancery and such organizations are recorded on bases agreed upon by the parties.

All properties of parishes and other diocesan-owned entities are legally titled to the Diocesan Bishop and his successors in office. The cost of new properties for future parish sites and diocesan high schools is included in these financial statements. At the time approval is given to proceed with formal planning of construction of a new parish, the parish is granted free use of the property by the Diocesan Bishop. Although civil ownership resides with the Diocese, the parish, a separate canonical entity, receives ownership of the property at the time of donation from the Chancery. Proceeds of the sale of any excess property shall accrue to the Diocese.

### Basis of accounting

The Chancery’s financial statements are presented on the accrual basis of accounting in accordance with generally accepted accounting principles in the United States of America.

### Classification of net assets

The Chancery's net assets have been grouped into the following three categories:

*Unrestricted Net Assets* - Net assets that are not subject to donor-imposed restrictions.

*Temporarily Restricted Net Assets* - Assets whose use is subject to explicit or implicit donor-imposed restrictions that either expire by the passage of time or can be fulfilled and removed by actions of the Chancery pursuant to these donor restrictions.

*Permanently Restricted Net Assets* - Net assets that are subject to explicit or implicit donor-imposed restrictions that require the original contribution be maintained in perpetuity by the Chancery, but permits the use of the investment earnings for general or specific purposes.

Unrealized and realized gains and losses and dividends and interest from investing in income-producing assets may be included in any of these net classifications depending on donor restrictions related to the principal investment.

**Unrestricted net assets**
To ensure observances of internally designated limitations and restrictions placed on the use of the resources available to the Chancery, the net assets of the Chancery are maintained in distinct subgroups, whereby, resources for various purposes are classified for accounting and reporting purposes into funds determined in accordance with the internally designated nature and purpose of such funds as follows:

Current operations include all resources available for support of Chancery operations.

Invested in property, equipment and land includes depreciated amounts invested in real property, computer hardware and software, office equipment and furniture and property held for future projects and parish sites, as well as construction in progress, net of outstanding bonds and accounts payable used for these investments.

Functioning as endowment are quasi-endowment funds available for investment as the Diocesan Bishop designates and includes original patrimony of the Diocese. Income from these investments can be used at the discretion of the Diocesan Bishop.

Designated includes monies for the priests' mutual aid fund, medical and property insurance fund, scholarship fund, the Rosa Bente Lee fund and the Bishop Keating fund.

**Cash and cash equivalents**
Cash and short-term investments with maturities at dates of purchase of three months or less are classified as cash equivalents, except that any such investments with cash held in trusts or by external endowment investment managers are classified with the deposits and investments, respectively. Cash equivalents are carried at cost which approximates fair value.

**Accounts and loans receivable**
Accounts and loans receivable are stated at the amount management expects to collect from outstanding balances. The Chancery provides for probable uncollectible amounts through a provision for bad debt expense and an adjustment to a valuation allowance based on its assessment of the current status of accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and credit to accounts and loans receivable.

**Property, equipment and land**
Property, equipment and land are carried at cost or, in the case of donated or bequeathed property, at fair value at date of donation. Property, equipment and land include real property, equipment, land and the original buildings and grounds of four regional high schools and other affiliated organizations under the control of the Diocesan Bishop. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, generally over 3 to 50 years. The cost of repairs

and maintenance is expensed as incurred. It is the general policy of the Chancery to capitalize all expenditures for property and equipment in excess of $5,000.

**Investments and investment valuation**
Investments are stated at fair value, as described in Note 8, *Fair value measurements*. Investments consist of money market funds, U.S. Government and sponsored enterprises securities, corporate bonds and equities, and alternative investments.

**Investment income and expense**
Realized gains and losses on investment transactions are recorded on the average cost method and are included in investment income in the statement of activities. Changes in unrealized appreciation and depreciation for the year are similarly reported. Interest and dividend income are recorded on the accrual basis.

**Investment pools**
The Chancery maintains master investment accounts for long-term assets, including certain reserves held on behalf of DIAL Corp and endowments, including those amounts held on behalf of Catholic Charities and The Foundation. Realized and unrealized gains and losses from securities in the master investment accounts are allocated monthly to the individual participants based on the relationship of the market value of each participant to the total market value of the master investment accounts, as adjusted for additions to or deductions from those accounts.

**Derivative instruments**
A derivative financial instrument is used to manage a variable interest rate on long-term debt. The Chancery has entered into an interest rate swap agreement to reduce the impact of changes in the variable interest rate. The Chancery recognizes the interest rate swap agreement as a net asset or liability at fair value on the statements of financial position. Changes in fair value on this agreement are recorded in the statement of activities as non-operating gains or losses.

**Unearned revenue**
Income from program activities received in advance is deferred and recognized in the period the event is held.

**Contributions**
Contributions are recognized when the donor makes an unconditional promise to transfer assets. These contributions are recorded as unrestricted, temporarily restricted, or permanently restricted revenue depending on the existence or nature of any donor restrictions.

Contributions that are restricted by the donor are reported as increases in unrestricted net assets in the fiscal year in which the restrictions expire or are satisfied. All other donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When restrictions are satisfied, temporarily restricted net assets are released to unrestricted net assets.

Contributions received by the Chancery on behalf of other related entities are not recorded as contributions on the Chancery's statement of activities. Rather these amounts are agency transactions since the other related entities carry the variance power and not the Chancery.

**Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure 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.

**Concentration of credit risk**

Financial instruments which potentially subject the Chancery to a concentration of credit risk principally consist of cash and cash equivalents, accounts receivable, and investments. The Chancery maintains cash and investments with several financial institutions. The Chancery performs periodic evaluations of these institutions for relative credit standing. The total deposits at these institutions at times exceed the amount guaranteed by federal agencies and therefore bear some risk since they are not collateralized. Cash on deposit with financial institutions exceeded the federally insured limit by $4,824,116 and $3,753,739 as of June 30, 2015 and 2014, respectively. The Chancery also invests excess funds in overnight investment agreements which are not federally insured but are collateralized by U.S. treasuries or mortgage-backed securities of U.S. government-sponsored enterprises. Amounts held in overnight investments as of June 30, 2015 and 2014 were $6,307,614 and $5,746,201 respectively. Pledges receivable, which have been adjusted for doubtful accounts, are due from individuals, corporations, and foundations. The amount due from one contributor comprises 42% of the total bequest and major gifts pledges receivable balance at June 30, 2015. To date, no permanent losses or impairments have been experienced due to concentration in these areas.

**Income taxes**

The Chancery is exempt from federal and state income tax under the provisions of Section 501(c)(3) of the Internal Revenue Code and related provisions of the Commonwealth of Virginia. They are not subject to the filing requirements of the Form 990. The Chancery may be subject to tax to the extent it has taxable unrelated business income. The Chancery has no unrelated business income and accordingly, no provision for income taxes is provided in the accompanying financial statements. The Chancery believes that it has appropriate support for any tax provisions taken, and as such, does not have any uncertain tax positions that are material to the financial statements.

**Subsequent events**

In preparing these financial statements, the Chancery has evaluated events and transactions for potential recognition or disclosure through October 27, 2015, the date the financial statements were available to be issued.

## 3. Accounts receivable

The Chancery bills the parishes, schools, other related entities and individuals on a monthly basis for various items paid by the Chancery or covered under the diocesan structure. These include the retirement programs for priests and lay employees, diocesan tuition assistance program, unemployment compensation, and health and property insurance. The Chancery also bills the parishes on a monthly basis for the operational assessment, a percentage of the parish offertory income to help offset the administration of diocesan programs. Accounts receivable are not collateralized.

Accounts receivable are as follows as of June 30:

| | 2015 | 2014 |
|---|---|---|
| Parishes | $ 452,779 | $ 537,778 |
| Schools | 802,490 | 1,095,414 |
| Other diocesan entities | 219,370 | 90,941 |
| Employee advances | 7,750 | 4,315 |
| Due from brokers | 126,743 | 74,326 |
| Miscellaneous | 214,597 | 101,737 |
| Total accounts receivable | 1,823,729 | 1,904,511 |
| Less: allowance for doubtful accounts | (121,492) | (121,925) |
| Total accounts receivable, net | $ 1,702,237 | $ 1,782,586 |

## 4. Bishop's Lenten Appeal pledges receivable

As of June 30, 2015 and 2014, contributors to the Bishop’s Lenten Appeal (BLA) have unconditionally promised to give $3,296,887 and $3,771,899. As the Bishop’s Lenten Appeal is an annual campaign, the pledges are due within one year.

## 5. Bequests and major gifts pledges receivable and Beneficial interest in residuary estates

Unconditional promises to give are as follows as of June 30:

| | 2015 | 2014 |
|---|---|---|
| Receivables due in one year or less | $ 10,000 | $ 400,000 |
| Receivables due in one to five years | 9,245,861 | 10,847,013 |
| Total unconditional promises to give | 9,255,861 | 11,247,013 |
| Less: discount to present value | (422,423) | (467,258) |
| Pledges receivable | $ 8,833,438 | $ 10,779,755 |

Pledges receivable include amounts related to the Leadership Gift Initiative campaign (Note 1). Unconditional promises to give due in more than one year are discounted at rates ranging from 1.24% to 2.63%.

### Beneficial interest in residuary estates

Beneficial interest in residuary estates as of June 30, 2015 includes amounts due from two estates which the Chancery has been notified it is a beneficiary. One is a residuary interest in cash and real property with an estimated value of $1,900,000, the use of which is unrestricted. The second is a residuary interest in the Rosa Bente Lee Trust with an estimated value of $12,600,000. The distribution from the residuary estate is donor-restricted and will be used to establish a permanent endowment, with investment earnings available for general purposes.

## 6. Investments

Investments are stated at fair value. The cost of investments and related fair values at June 30, 2015 and 2014 consist of the following:

| | 2015 | | 2014 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Short-term investments | $ 16,318,582 | $ 16,318,582 | $ 10,994,157 | $ 10,994,157 |
| U.S. Government and sponsored enterprises securities | 5,152,560 | 5,117,428 | 3,645,317 | 3,600,885 |
| Corporate, municipal and foreign bonds and other fixed instruments | 38,344,477 | 40,673,685 | 36,950,904 | 40,567,661 |
| Equities, including publicly traded REITs | 116,708,925 | 138,608,126 | 107,203,509 | 137,603,974 |
| Real property held for investment | 2,908,599 | 2,908,599 | 2,908,599 | 2,908,599 |
| Alternative investments | 10,316,783 | 11,161,158 | 4,307,516 | 5,275,400 |
| | $ 189,749,926 | $ 214,787,578 | $ 166,010,002 | $ 200,950,676 |

Also included in investments at June 30, 2015 and 2014 is $447,460 and $457,872, respectively, representing the fair market value of assets held under split interest agreements for which the Chancery is the trustee. Monthly, quarterly or semiannual distributions are made to the donors. The ultimate beneficiaries are the Chancery, Catholic Charities and parishes. The proceeds are expected to be received in three to eighteen years, based on published actuarial tables, and are calculated using discount rates which represent the risk-free rates in existence at the date of the gift. Amounts due to annuitants and related parties are disclosed as annuity payment liability in the accompanying statements of financial position.

Investments are held for the following purposes:

| | 2015 | 2014 |
|---|---|---|
| Current operations and programs | $ 61,843,364 | $ 53,835,493 |
| Long-term purposes, including endowments | 56,402,652 | 53,984,128 |
| Assets held on behalf of other dicoesan entities, including DIAL Corp | 92,293,485 | 88,878,601 |
| Arlington Diocese Educational Fund (ADEF) | 4,248,077 | 4,252,454 |
| Total | $ 214,787,578 | $ 200,950,676 |

Investments in the amount of $175,272,204 and $168,622,515 as of June 30, 2015 and 2014, respectively, are held in a pool under a trust agreement with a bank in which participants share in allocated investment income and loss.

Investment income is reported on the statement of activities as follows:

| | 2015 | 2014 |
|---|---|---|
| For Operations | $ 1,800,000 | $ 1,460,000 |
| In Other changes in net assets | 877,314 | 15,499,737 |
| Net investment gains - Chancery | $ 2,677,314 | $ 16,959,737 |

Investment income represented in operating revenue represents the amount included in the approved budget based on a spending rate formula.

Total net investment income for the years ended June 30, 2015 and 2014, respectively, consists of the following:

| | 2015 | 2014 |
|---|---|---|
| **Chancery** | | |
| Interest, dividends and other investment income | $ 2,098,635 | $ 1,762,968 |
| Realized gains, net | 6,464,315 | 9,038,901 |
| Unrealized (losses) gains, net | (5,094,098) | 6,799,320 |
| Less - investment management expenses | (791,538) | (641,452) |
| Net investment gains - Chancery | $ 2,677,314 | $ 16,959,737 |
| **Funds held for diocesan entities** | | |
| Investment income allocated to diocesan entities | $ 2,753,102 | $ 16,028,808 |
| Total net investment gains - Chancery and funds held for diocesan entities | $ 5,430,416 | $ 32,988,545 |

The Chancery invests in a variety of investment securities and therefore, is subject to various risks such as interest rate, credit and overall market volatility risk. Due to continuing market risk and fluctuations, it is reasonably possible that significant changes in investment values will occur in the near term that could materially affect the amounts reported in the statement of financial position and the results of operations.

## 7. Fair value of financial instruments

Estimated fair values of the Chancery's financial instruments (all of which are held for nontrading purposes) are as follows:

| | 2015 | | 2014 | |
|---|---|---|---|---|
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| Cash and cash equivalents | $ 11,314,349 | $ 11,314,349 | $ 9,828,762 | $ 9,828,762 |
| Beneficial interest in residuary estates | $ 14,500,000 | $ 14,500,000 | $ - | $ - |
| Investments | $ 214,787,578 | $ 214,787,578 | $ 200,950,676 | $ 200,950,676 |
| Interest rate swap agreement | $ 93,245 | $ 93,245 | $ 338,502 | $ 338,502 |
| Demand notes and loans receivable | $ 7,013,046 | $ 6,683,053 | $ 7,832,920 | $ 7,395,381 |
| Bonds payable | $ 19,601,783 | $ 19,601,783 | $ 20,479,836 | $ 20,479,836 |

The carrying amount for cash and cash equivalents approximates fair value.

Beneficial interest in residuary estates is measured using the fair value of the assets held in the trusts reported by the trustees.

The fair value of demand notes and loans receivable are based on quoted market rates of debt securities with similar repayment terms.

The carrying value of the 2012 bonds, which accrue interest at a floating market rate, approximates the market value.

Investments and interest rate swap agreements are carried at fair value as described in Note 8.

## 8. Fair value measurements

The Chancery measures fair value using a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability. Inputs may be observable or unobservable and refer broadly to the assumptions that market participants would use in pricing the asset or liability. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from sources independent of the reporting entity. Unobservable inputs reflect the reporting entity's own assumptions about the assumptions that market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The objective of a fair value measurement is to determine 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 (an exit price). Accordingly, the fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The Chancery may use valuation techniques consistent with the market, income and cost approaches to measure fair value.

The inputs used to measure fair value are categorized into the following three categories:

- Level 1 Inputs – Unadjusted quoted prices in active markets for identical assets or liabilities such as stocks and government bonds.

- Level 2 Inputs – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, or other inputs that can be corroborated by observable market data for substantially the full term of the assets or liabilities.

- Level 3 Inputs – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or other valuation techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Fair values of assets measured on a recurring basis by level at June 30, 2015 are as follows:

| | Fair Value | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| **Assets** | | | | |
| Investments | | | | |
| Short-term investments | $ 16,318,582 | $ 16,318,582 | $ - | $ - |
| U.S. Government and sponsored enterprises securities | 5,117,428 | 4,317,263 | 800,165 | - |
| Corporate,municipal and foreign bonds and other fixed instruments | 40,673,685 | - | 40,673,685 | - |
| Equities, including publicly traded REITs | 138,608,126 | 138,608,126 | - | - |
| Real property held for investment | 2,908,599 | - | 2,908,599 | |
| Alternative investments | 11,161,158 | - | - | 11,161,158 |
| Total | $ 214,787,578 | $ 159,243,971 | $ 44,382,449 | $11,161,158 |
| Interest rate swap agreement | $ 93,245 | $ - | $ 93,245 | $ - |

Fair values of assets measured on a recurring basis by level at June 30, 2014 are as follows:

| | Fair Value | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| **Assets** | | | | |
| Investments | | | | |
| Short-term investments | $ 10,994,157 | $ 10,994,157 | $ - | $ - |
| U.S. Government and sponsored enterprises securities | 3,600,885 | 2,578,095 | 1,022,790 | - |
| Corporate,municipal and foreign bonds and other fixed instruments | 40,567,661 | - | 40,567,661 | - |
| Equities, including publicly traded REITs | 137,603,974 | 137,603,974 | - | - |
| Real property held for investment | 2,908,599 | - | 2,908,599 | |
| Alternative investments | 5,275,400 | - | - | 5,275,400 |
| Total | $ 200,950,676 | $ 151,176,226 | $ 44,499,050 | $ 5,275,400 |
| Interest rate swap agreement | $ 338,502 | $ - | $ 338,502 | $ - |

The following is a description of what is included in the categories of investments, along with the valuation methodologies used for measuring assets at fair value.

Short-term investments – These include money market and money market mutual funds, investing primarily in cash, U.S. Treasury obligations, or short-term, high quality fixed income securities.

U.S. Government and sponsored enterprises securities – U.S. Treasury notes and bonds are valued by independent pricing services based on active market data and are categorized as Level 1. Government sponsored enterprises securities and mortgage-backed securities, categorized as Level 2, are valued by independent pricing services based on inputs that may include issuer type, coupon, cash flows, benchmark yields, reported trades, and bids and offers.

Corporate, municipal and foreign bonds and other fixed instruments – These primarily include holdings in three diverse bond funds, two fixed bond funds and one high yield bond fund. The bond funds invest primarily in U.S. Government, agency, corporate and mortgage-backed securities. The fair value of the bond fund investments are estimated using the net asset value per share of investments provided by the fund manager. Holdings also include fixed rate corporate and foreign bonds that are valued based on yields currently available for comparable securities. All investments are categorized as Level 2.

Equity securities, including publicly traded REITs – These investments are individual securities and are valued based on their published closing price in an active market.

Real property held for investment – Real estate investment properties, categorized as Level 2, are valued using a market approach based primarily on current appraised values and other information for similar property.

Alternative investments – comprised of separate private equity interests focusing on venture and/or buy-out strategies, investments in real assets leased to the U.S. government, a diversified portfolio with concentrations in timber, energy and real estate, and investment in a private investment partnership. The private investment partnership seeks to attain current income and capital appreciation promoting strategies that are in accordance with Catholic social teaching. These investments are classified within Level 3 as the value of these interests is primarily based on the net asset value reported by external fund managers as described in the investment funds' financial statements, all of which are subject to a third party annual audit.

Alternative investments reported at net asset value are reflected below:

| | 2015 Fair Value | 2014 Fair Value | Unfunded Commitments June 30, 2015 | Redemption Frequency | Redemption Notice Period |
|---|---|---|---|---|---|
| Private equity - venture/buyout | $ 859,547 | $ 483,479 | $ 1,168,499 | N/A | N/A |
| Private equity - real assets, U.S. government leased | 4,226,577 | 3,572,207 | - | N/A | N/A |
| Private equity - diversifed portfolio | 973,607 | 1,219,714 | 152,998 | N/A | N/A |
| Private investment partnership | 5,101,427 | - | - | Up to 50% of capital each rolling 3-month period | 95 days |
| | $ 11,161,158 | $ 5,275,400 | $ 1,321,497 | | |

The Chancery may not sell, transfer or pledge their interest in the private equity funds, except with the consent of the general partner. For these investments, periodic distributions are received through liquidation of the underlying investments of the fund. In February 2015, the private equity, real assets fund obtained shares in a newly formed public REIT in exchange for portfolio holdings. Liquidation of the fund is expected following a 15 month lock-up period.

The changes in investment measured at fair value using Level 3 inputs are reflected below:

| | 2015 | 2014 |
|---|---|---|
| Balance, beginning of year | $ 5,275,400 | $ 3,351,937 |
| Contributions | 6,227,396 | 1,766,103 |
| Distributions | (218,130) | (332,883) |
| Change in value - unrealized (loss) gain | (123,508) | 490,243 |
| Balance, end of year | $ 11,161,158 | $ 5,275,400 |

Unrealized gains recorded for Level 3 investments are reported as investment income under other changes in net assets on the statement of activities. Certain distributions from alternative investments are recorded as dividend income when identified by the fund manager as a distribution from earnings and profits from the underlying investments. Distributions from Level 3 investments recorded as dividend income amounts to $185,457 and $190,149 for the years ended June 30, 2015 and 2014.

The Chancery recognizes transfers into and out of levels at the end of the reporting period. There were no transfers between levels in the years ended June 30, 2015 and 2014.

The Chancery has entered into an interest rate swap agreement in association with a financing arrangement of bonds payable (Note 11). The fair value of the interest rate swap agreement is determined by comparing the difference between the present value of the fixed monthly payments and the estimated present value of the floating monthly payments based on estimated forward rates derived from yield curves. The Chancery has recognized in the statement of activities a decrease in fair value of the interest rate swap agreement of $245,257 for the year ended June 30, 2015 and a decrease of $214,897 for the year ended June 30, 2014.

Due to the inherent uncertainty involving assumptions and estimation methods, the fair value of the investments and interest rate swap agreements may differ materially from actual results.

## 9. Related-party transactions

The Chancery has transactions with diocesan parishes, schools, and other related entities. Below is a summary of the impact of significant transactions with these related parties on the statements of financial position and statements of activities:

| | 2015 | 2014 |
|---|---|---|
| Assets: | | |
| Accounts receivable, parishes, schools and other related entities, net | $ 1,371,090 | $ 2,230,579 |
| Due from Catholic Charities, split interest annuity | 89,520 | 78,962 |
| Paul VI Catholic High School loan receivable, for $4,839,917 in bond proceeds used for renovations and additions | 3,558,760 | 3,798,634 |
| Saint John Paul the Great Catholic High School loan receivable, interest waived for 2015 and 2014, no fixed repayment, repayments accepted as cash is available, net of allowance | - | - |
| 200 North Glebe Road, Inc., interest waived for 2015 and 2014, due on demand, repayments accepted as cash is available | 3,454,286 | 4,034,286 |
| | $ 8,473,656 | $ 10,142,461 |

| | 2015 | 2014 |
|---|---|---|
| Liabilities: | | |
| Accounts payable, parishes, schools, other related entities | $ 115,361 | $ 18,785 |
| Due to parishes, split interest annuities | 501 | 6,555 |
| Amounts held on behalf of other diocesan entities: | | |
| DIAL Corp, funds held in investment pool | 76,729,182 | 75,123,510 |
| Catholic Charities, endowment funds held in investment pool | 12,708,499 | 12,028,549 |
| The Foundation, endowment funds held in investment pool | 2,594,814 | 1,403,833 |
| Catholic Charities, capital campaign pledges | 4,128 | 6,128 |
| Parishes, capital campaign and major gift pledges | 605,777 | 569,440 |
| ADEF funds held for schools | 2,614,255 | 2,651,903 |
| | $ 95,372,517 | $ 91,808,703 |

| | 2015 | 2014 |
|---|---|---|
| Revenues and Support: | | |
| Operational assessment, parishes | $ 7,451,644 | $ 7,428,795 |
| Contributions, diocesan tuition assistance program | 2,328,639 | 2,321,499 |
| Program fees | 1,518,031 | 1,312,229 |
| Information technology, accounting and administrative support | 347,327 | 280,398 |
| Rental income, Catholic Charities | 295,605 | 277,753 |
| Rental income, Arlington Catholic Herald | 126,128 | 118,802 |
| Rental income, Saint John Paul the Great Catholc High School | 1,434,456 | 1,314,918 |
| Insurance and risk management premiums billed | 17,639,503 | 16,534,965 |
| | $ 31,141,333 | $ 29,589,359 |

| | 2015 | 2014 |
|---|---|---|
| Expenses: | | |
| Rent paid to 200 N. Glebe Road, Inc. | $ 2,089,705 | $ 1,994,019 |
| Contributions, tuition assistance program | 2,338,870 | 2,285,528 |
| Contributions, tuition assistance endowment grants | 730,000 | 627,000 |
| Contributions, student financial aid (LGI) | 240,958 | - |
| Contribution, subsidy to Catholic Charities | 1,757,185 | 1,653,399 |
| Contribution, Catholic Charities endowment fund (LGI) | 670,600 | 75,313 |
| Contribution, restricted for Catholic Charities programs (LGI) | 847,497 | 1,000,000 |
| Contribution, restricted, diocesan high schools capital needs (LGI) | 741,745 | 4,000,000 |
| Contribution, other program service subsidies | 30,000 | 434,000 |
| Contribuiton, Cathedral of St. Thomas More renovations | 461,574 | 510,623 |
| Contributions made to Lay Retirement Plan | 1,011,942 | 985,746 |
| Contributions made to Priest Retirement Plan, including LGI | 549,519 | 1,375,000 |
| Advertising expense to Arlington Catholic Herald | 124,622 | 153,470 |
| Loan reserve, Saint John Paul the Great Catholc High School | 833,256 | 1,314,918 |
| | $ 12,427,473 | $ 16,409,016 |

Affiliates participating in the diocesan sponsored insurance plans are charged premiums to cover estimated claims and program expenses. The net revenue or expense of these programs is reflected under other changes in net assets.

Certain parishes have chosen to participate in the Arlington Diocese Educational Foundation (ADEF) program. This program was established to support the cause of Catholic education through endowments or quasi-endowment investment accounts. The assets of ADEF are held in trust with the Chancery being steward and guardian of such endowments.

The Chancery administers a master investment pool (Notes 2 and 6). Endowment funds and long term investments of certain affiliates are held in the master pool at their request. Investment income is allocated based on the proportionate market value of investments held by participants.

The Chancery has entered into services agreements with certain affiliates to provide information technology, accounting and administrative support.

Property and equipment includes the original buildings and grounds of four diocesan high schools and a regional elementary school acquired by the Chancery. The Chancery does not charge Bishop O'Connell, Paul VI and Bishop Ireton High Schools, as well as the regional school, Epiphany Elementary, for use of the facilities. Improvements and repairs necessary to maintain the property are financed by the schools and carried on their financial statements. The Chancery has joined with Catholic Charities in providing transitional housing and counseling services by providing use of a family housing facility at no charge.

The Chancery has advanced funds to Saint John Paul the Great Catholic High School periodically since its opening in August 2008, to supplement tuition in covering operating costs. The collectability of the loan was reviewed in 2015 and 2014 and based on current enrollment and operating financial position a reserve was established on the loan balance, $12,116,013 and $11,282,757 at June 30, 2015 and 2014, respectively. It is at least reasonably possible that the estimated loan to be collected may change as school enrollment and fundraising activities increase.

The Chancery obtained financing through issuance of tax-exempt revenue bonds with the Prince William County Industrial Authority, a portion of which was used for building renovations and improvements to Paul VI Catholic High School (PVI) (Note 11). The Chancery established a loan with PVI in the amount of $4,960,000, the amount of bond proceeds used to cover these costs. Through December 2012, the terms of this loan were equivalent to those contained in the Diocese's bond agreement. In December 2012, the Chancery refinanced the bonds outstanding. The Chancery has re-amortized the principal outstanding with PVI based on the effective fixed rate of 2.482% which was secured by the refinancing and related interest rate swap. Monthly principal and interest payments of $27,563 are expected to be paid by PVI to the Chancery through maturity, December 1, 2027.

Loans have been made to 200 N. Glebe Road, Inc., a related entity and lessor of office space to the Chancery. The loan to 200 N. Glebe Road, Inc. is due on demand, with repayments accepted as cash is available. Amounts repaid by 200 N. Glebe Road, Inc. were $580,000 and $300,000 for the years ended June 30, 2015 and 2014, respectively.

Annually, management assesses the adequacy of the allowance for credit losses evaluating required and expected repayment on loans. Changes in the allowance for related party loans receivable as of June 30 are as follows:

| | 2015 | 2014 |
|---|---|---|
| Balance, beginning of year | $ 11,282,757 | $ 9,967,839 |
| Provision for credit losses | 833,256 | 1,314,918 |
| Balance, end of year | $ 12,116,013 | $11,282,757 |

The Chancery granted three diocesan high schools $741,745 and $4,000,000 for the years ended June 30, 2015 and 2014, respectively. These funds were raised through the Leadership Gift Initiative campaign and restricted for the capital needs of the schools. The grants may only be used for capital improvements approved by the Chancery.

## 10. Property, equipment and land, net

Property, equipment and land, net, consist of the following at June 30:

| | 2015 | 2014 |
|---|---|---|
| Operating properties-buildings | $ 85,463,929 | $ 84,378,316 |
| Operating properties-land and land development | 25,834,566 | 25,414,566 |
| Operating properties-improvements | 8,760,205 | 7,811,278 |
| Operating properties-furniture and equipment | 3,915,755 | 3,900,839 |
| Land held for future projects and parishes | 10,935,532 | 10,935,532 |
| Office furniture and equipment | 783,762 | 777,094 |
| Computer hardware | 408,942 | 273,041 |
| Computer software | 1,012,889 | 992,343 |
| Vehicles | 669,006 | 669,006 |
| Leasehold improvements | 1,042,610 | 1,030,509 |
| Total property, equipment and land | 138,827,196 | 136,182,524 |
| Less: accumulated depreciation | (32,191,985) | (29,472,369) |
| Property, equipment and land, net | $ 106,635,211 | $ 106,710,155 |

Depreciation expense was $2,738,188 and $2,622,656 during the years ended June 30, 2015 and 2014, respectively. Of the total assets listed above, $13,605,249 and $13,440,993 were fully depreciated at June 30, 2015 and 2014, respectively.

As of June 30, 2014 construction in progress and assets not yet placed in service is land and buildings purchased for a new location of an existing diocesan regional elementary school in Culpeper, Virginia. Assets approximating $2,300,000 and representing the originally purchased 20 acre campus plus improvements were placed in service in August 2014.

In 1998, a conditional gift of approximately forty acres of land in Prince William County was donated to the Chancery. In August 2006, the conditions of this gift were satisfied and the donation was recorded at the appraised value of $14,500,000. The land must be used for educational purposes for a period of thirty years and therefore the donation will remain in temporarily restricted net assets until such time this restriction expires.

Construction of Saint John Paul the Great Catholic High School was funded, in part, from tax-exempt bonds (Note 11). Once it was reasonably assured that the high school would be constructed, interest costs, net of interest earned from the temporary investment of the bonds were capitalized. Upon completion of the high school, bond interest cost was charged to expense.

Capitalized interest is included in operating properties. Amortization of capitalized interest is included in depreciation expense. Capitalized interest at June 30 was:

| | 2015 | 2014 |
|---|---|---|
| Net amount capitalized, beginning of year | $ 866,274 | $ 885,906 |
| Less: amortization expense | 19,632 | 19,632 |
| Net amount capitalized, end of year | $ 846,642 | $ 866,274 |

Cumulative investment earnings do not exceed cumulative investment expenses, and therefore the Diocese does not have an arbitrage recapture obligation.

## 11. Bonds payable

In December 2012, the Chancery entered into a refinancing arrangement of prior indebtedness obtaining $21,808,515 in bank qualified tax-exempt financing (2012 bonds payable) for the purpose of defeasing that debt. This debt financed the construction of Saint John Paul the Great Catholic High School and, in part, building renovations and improvements to Paul VI Catholic High School.

The outstanding balance on the bonds payable is $19,601,783 and $20,479,836 at June 30, 2015 and 2014, respectively. The 2012 bonds payable bear interest at a floating rate, 78% of the 30-day London Interbank Offered Rate (LIBOR) plus 1.002%. The average interest rate for the fiscal year ended June 30, 2015 and 2014 is 1.13%. The Chancery entered into an interest rate swap agreement in May 2013 related to the 2012 bonds payable securing an effective fixed rate of 2.482% in exchange for the floating LIBOR rate. The original notional amount under the agreement was $21,405,966, decreasing based on a 15 year amortization, terminating December 1, 2027. The notional amount at June 30, 2015 and 2014 is $18,802,778 and $20,068,648, respectively.

The 2012 bonds contain no pre-payment penalties but require compliance with certain covenants such as operating liquidity, additional indebtedness, maintenance of insurance on the project, use of the bond proceeds, maintenance of tax-exempt status of the Diocese and financial reporting.

Bond interest expense is $404,127 and $721,650, reflective of the swap agreement and net of amount received from Paul VI Catholic High School, for the years ended June 30, 2015 and 2014, respectively. Bond related costs for the year ended June 30, 2014, include the premium paid and write off of unamortized bond costs in connection with the redemption of 2003 bond payable.

Principal and interest are payable monthly based on a 20 year amortization with a balloon payment due in 15 years. Maturities on the bonds payable annually for the years through 2020 and thereafter are as follows:

| | |
|---|---|
| 2016 | $ 900,264 |
| 2017 | 923,740 |
| 2018 | 948,515 |
| 2019 | 973,249 |
| 2020 | 998,078 |
| Thereafter | 14,857,937 |
| | $ 19,601,783 |

## 12. Pension expense

### Pension plan - employees

The Diocese has a noncontributory defined benefit pension plan which covers substantially all lay employees within the Diocese. The plan provides benefits based on a formula which takes into account the lay employees' annual compensation, period of service, and age.

The lay employees' plan is administered by the Chancery, but is a multi-employer plan. The plan covers employees from other diocesan organizations, such as parishes and schools, the Arlington Catholic Herald, and diocesan high schools, which, as noted in Note 2, are not combined with the Chancery for financial reporting purposes. Premiums are calculated based on 10% of eligible participant salaries, and are used toward the quarterly funding of the plan. The cost of the plan for the Chancery and charged to expense was $1,011,942 and $985,746 for the years ended June 30, 2015 and 2014, respectively. The plan is not subject to ERISA funding requirements.

### Pension plan - priests

The Diocese also has a noncontributory defined benefit plan which covers diocesan priests incardinated in the Diocese and provides benefits based on age and compensation at retirement. As required by generally accepted accounting standards in the United States of America, the full funding status of the defined benefit pension plans, as of the statement of financial position date, has been recognized as an asset (overfunded plan) or as a liability (underfunded plan). The pension benefit obligation for retired priests has been actuarially determined.

The following amounts relate to the diocesan priests' defined benefit pension plan:

| | 2015 | 2014 |
|---|---|---|
| Change in benefit obligation: | | |
| Benefit obligation at beginning of year | $19,485,448 | $16,471,472 |
| Service cost | 683,814 | 616,261 |
| Interest cost | 839,310 | 823,451 |
| Actuarial loss/(gain) | 2,514,395 | 2,396,825 |
| Benefits paid | (754,632) | (822,561) |
| Benefit obligation at end of year | 22,768,335 | 19,485,448 |
| Change in plan assets: | | |
| Fair value of plan assets at beginning of year | 12,778,161 | 9,422,197 |
| Return on plan assets | 249,929 | 1,178,525 |
| Employer contributions | 1,814,519 | 3,000,000 |
| Benefits paid | (754,632) | (822,561) |
| Fair value of plan assets at end of year | 14,087,977 | 12,778,161 |
| Accrued pension liability, priests | $ 8,680,358 | $ 6,707,287 |

The accumulated benefit obligation at June 30, 2015 and 2014 was $21,132,931 and $18,029,233, respectively. The net periodic pension cost for the years ended June 30, 2015 and 2014 were $777,723 and $916,650, respectively. Amounts previously recognized in unrestricted net assets not yet recognized as periodic pension cost at June 30:

| | 2015 | 2014 |
|---|---|---|
| Net (loss) | $ (9,366,645) | $ (6,339,901) |
| Net prior service cost | (301,817) | (318,694) |
| Amounts previously recognized in unrestricted net assets, not yet recognized as periodic benefit cost | $ (9,668,462) | $ (6,658,595) |

The estimated net loss that will be amortized from changes in unrestricted net assets into net periodic benefit cost in 2016 is $372,078.

Assumptions used to determine the year-end benefit obligation:

| | 2015 | 2014 |
|---|---|---|
| Discount rate on the benefit obligation | 4.60% | 4.40% |
| Rate of expected return on plan assets | 7.50% | 7.00% |
| Rate of priests' compensation increase | 2.00% | 2.00% |

The expected return assumption was developed as the weighted average of expected returns determined under a forward looking approach and a historical approach using the plan's target asset assumption. The forward looking assumption was developed based on a market analysis applied to the plan's investment mix. The historical return assumption was developed from a proprietary database of prior investment returns.

The Diocese measures fair value of the plan's assets using a three-level hierarchy based upon observable inputs (Note 8).

Fair values of the plan's assets measured on a recurring basis by level at June 30, 2015 are as follows:

| | Fair Value | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Short-term investments | $ 1,284,413 | $ 1,284,413 | $ - | $ - |
| U.S. Government and sponsored enterprises securities | 2,563,515 | 1,547,668 | 1,015,847 | - |
| Corporate and foreign bonds | 1,265,820 | - | 1,265,820 | - |
| Equities | 8,974,229 | 8,974,229 | - | - |
| Total | $ 14,087,977 | $ 11,806,310 | $ 2,281,667 | $ - |

Fair values of the plan's assets measured on a recurring basis by level at June 30, 2014 are as follows:

| | Fair Value | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Short-term investments | $ 510,142 | $ 510,142 | $ - | $ - |
| U.S. Government and sponsored enterprises securities | 2,538,650 | 1,511,750 | 1,026,900 | - |
| Corporate and foreign bonds | 1,635,780 | - | 1,635,780 | - |
| Equities | 8,093,589 | 8,093,589 | - | - |
| Total | $ 12,778,161 | $ 10,115,481 | $ 2,662,680 | $ - |

The Diocese's overall strategy is to invest in high-grade securities and other assets with a minimum risk of market value fluctuation. In general, the Diocese's goal is to maintain the following allocation ranges:

| | |
|---|---|
| Equity securities | 50% - 60% |
| Fixed income securities | 40% - 50% |
| Short term cash/money market | 0% - 10% |

The Diocese expects to contribute approximately $1,540,000 to the plan in 2016. Benefits expected to be paid by the plan during the ensuing five years and thereafter are approximately as follows:

| | |
|---|---|
| 2016 | $ 860,595 |
| 2017 | 878,925 |
| 2018 | 920,720 |
| 2019 | 958,660 |
| 2020 | 1,062,685 |
| 2021-2025 | 6,065,187 |

**Tax-deferred retirement savings plan**

The Diocese also sponsors and maintains a tax-deferred 403(b) retirement savings plan for eligible employees and diocesan priests. All contributions are from employee elective salary reduction agreements. Since there is no employer match, there is no expense to the Chancery related to this plan.

## 13. Postretirement benefits

The Chancery sponsors a post-retirement Medicare supplemental plan for retired priests. The plan pays medical and prescription costs not covered by parts A and B of Medicare. The plan is noncontributory for diocesan priests. The Chancery also sponsors a lay-retiree postretirement plan which provides health benefits to retired lay employees meeting service and other participation requirements. The plan provides benefits to employees of the Chancery and other diocesan organizations, such as parishes, schools, the Arlington Catholic Herald, and diocesan high schools. The lay retirees pay 100% of the stated premium which is a blended rate for both active employees and retirees. Because the true medical costs are higher for retirees than for active employees, the plan is providing an “implicit subsidy” to the retirees. The postretirement obligation for both priests and lay retirees has been actuarially determined.

The following amounts relate to the postretirement health obligation:

| | 2015 | 2014 |
|---|---|---|
| Change in benefit obligation: | | |
| Benefit obligation at beginning of year | $ 8,677,709 | $ 7,484,062 |
| Service cost | 305,080 | 253,093 |
| Interest cost | 377,612 | 377,815 |
| Employee contributions | 121,288 | 146,020 |
| Actuarial loss (gain) | 2,857,285 | 655,310 |
| Benefits paid | (614,324) | (238,591) |
| Benefit obligation at end of year | 11,724,650 | 8,677,709 |
| Change in plan assets: | | |
| Fair value of plan assets at beginning of year | - | - |
| Employer contributions | 493,036 | 92,571 |
| Employee contributions | 121,288 | 146,020 |
| Benefits paid | (614,324) | (238,591) |
| Fair value of plan assets at end of year | - | - |
| Post retirement health benefit obligation | $ 11,724,650 | $ 8,677,709 |

The net periodic benefit cost for the years ended June 30, 2015 and 2014 were $594,176 and $509,448, respectively. Amounts previously recognized in unrestricted net assets not yet recognized as periodic benefit cost at June 30:

| | 2015 | 2014 |
|---|---|---|
| Net gain (loss) | $ (2,523,400) | $ 422,401 |
| Net prior service credit | - | - |
| Amounts previously recognized in unrestricted net assets, not yet recognized as periodic benefit cost | $ (2,523,400) | $ 422,401 |

The estimated net loss that will be amortized from changes in unrestricted net assets into net periodic benefit cost in 2016 is $46,233.

Assumptions used to determine the year-end benefit obligation:

| | **2015** | **2014** |
|---|---|---|
| Discount rate on the benefit obligation | 4.60% | 4.40% |

For measurement purposes, a 6.9% increase in the cost of health care benefits was assumed for 2015. This rate was assumed to decrease over a 12 year period to an ultimate rate of 4.5% by 2027. For 2014, a 7.1% increase in the cost of health care benefits was assumed. This rate was assumed to decrease over a 13 year period to an ultimate rate of 4.5% by 2027.

The Diocese expects to contribute approximately $208,000 to the plan in 2016. Benefits expected to be paid by the plan during the ensuing five years and thereafter are approximately as follows:

| | | |
|---|---|---|
| 2016 | $ | 208,000 |
| 2017 | | 231,000 |
| 2018 | | 253,000 |
| 2019 | | 291,000 |
| 2020 | | 339,000 |
| 2021-2025 | | 2,282,000 |

## 14. Temporarily restricted net assets

Expenses incurred for program activities such as seminarian education, educational programs, youth ministry, outreach, communications, and operations of the priests' retirement home resulted in a release of restricted net assets which is included in operations. Net assets were also released from restrictions with grants made to related parties for diocesan high school capital needs and charitable programs (Note 9). Affiliates are required to record these contributions as temporarily restricted and release from restrictions as funds are expended for the donor-specified purposes.

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

| | 2015 | 2014 |
|---|---|---|
| Catholic education, endowment income | $ 14,906,136 | $ 14,692,638 |
| Donated land restricted for high school | 14,500,000 | 14,500,000 |
| Bishop's targeted initiatives | 9,750,174 | 8,593,450 |
| Retired priests' needs | 5,031,046 | 4,825,077 |
| Student financial aid | 1,834,907 | 2,027,992 |
| New evangelization | 1,183,675 | 934,904 |
| ADEF education scholarships, endowment income | 729,035 | 709,783 |
| ADEF seminarian education | 548,321 | 538,173 |
| Youth ministry, endowment income | 462,743 | 458,614 |
| Continuing formation funds | 461,323 | 426,063 |
| Charitable progams | 422,828 | 772,703 |
| Project Rachel and Gabriel | 334,900 | 349,246 |
| Respect Life | 304,771 | 107,423 |
| High school capital | 207,878 | 222,002 |
| Major gifts pledges receivable for future period use | 198,456 | 393,851 |
| Spirituality Center | 156,212 | 4,758 |
| Catholic education | 148,047 | 129,744 |
| Charitable annuities | 139,304 | 131,289 |
| Diocesan work camp | 96,388 | 197,940 |
| Seminarian support | 94,428 | 80,259 |
| Campaign for human development | 75,602 | 67,463 |
| Black and Indian mission | 72,960 | 65,889 |
| Communications | 69,864 | 35,116 |
| Permanent diaconate | 61,768 | 56,742 |
| Others | 74,025 | 46,914 |
| Total | $ 51,864,791 | $ 50,368,033 |

Included in Bishop’s targeted initiatives are amounts raised through the LGI campaign, where the donors have expressed support for all the stated campaign goals (Note 1). The actual allocation of these funds among the stated goals will be determined based on need.

## 15. Permanently restricted endowments

As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the Diocesan Bishop to function as endowment funds, are classified and reported based on the existence of donor-imposed restrictions.

Permanently restricted endowments are for the following purposes at June 30:

| | 2015 | 2014 |
|---|---|---|
| Catholic education | $ 21,738,341 | $ 20,299,841 |
| Catechetics | 2,045,653 | 2,045,653 |
| Youth ministry | 510,988 | 510,988 |
| ADEF education scholarships | 310,500 | 310,500 |
| Diocesan operations | 50,000 | 50,000 |
| Original endowment corpus | 24,655,482 | 23,216,982 |
| Endowment major gifts/bequests receivable | 13,148,000 | 573,781 |
| Total | $ 37,803,482 | $ 23,790,763 |

**Interpretation of relevant law**

The Uniform Prudent Management of Institutional Funds Act (UPMIFA), effective July 1, 2008, in the Commonwealth of Virginia, has been interpreted as requiring the preservation of fair value of the original gift as of the date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Chancery 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 the Chancery in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Chancery considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the funds
2. The purposes of the Chancery and 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 Chancery
7. The investment policies of the Chancery

**Funds with deficiencies**

From time to time, the fair value of assets associated with individual donor-restricted funds may fall below the level that the donor or UPMIFA requires the Chancery to retain as a fund of perpetual duration. There were no such deficiencies as of June 30, 2015 and 2014.

**Investment return objectives, risk parameters and strategies**

The Chancery has adopted investment and spending policies 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 an after-cost total real 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, which includes equity and debt securities, which is intended to result in a consistent inflation-protected rate of return that has sufficient liquidity to make an annual distribution ranging from 4% to 5%, while growing the funds if possible. Therefore, the Chancery expects its endowment assets, over time, to produce an average rate of return of between 7% and 10% annually. Actual returns in any given year may vary from this amount. Investment risk is measured in terms of the total endowment fund; investment assets and allocation between asset classes and strategies are managed to not expose the fund to unacceptable levels of risk.

**Spending policy**

The Chancery has a policy of appropriating for distribution each year 4% of its endowment fund average fair value of the prior 12 quarters through the calendar year-end preceding the fiscal year in which the distribution is planned except for ADEF education scholarships which is 5% of the average fair value of the three previous calendar years. In establishing these policies, the Chancery considered the long-term expected return on its investment assets. The Chancery expects the current spending policy to allow its endowment funds to grow at a nominal average rate of between 3% and 4% annually over the spending rate. This is consistent with the Chancery's objective to maintain the purchasing power of the endowment assets as well as to provide additional real growth through new gifts and investment return.

Endowment net asset composition by type of fund as of June 30, 2015 is as follows:

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total Net Endowment Assets |
|---|---|---|---|---|
| Donor-restricted endowment funds | $ - | $16,117,067 | $24,655,482 | $40,772,549 |
| Endowment major gifts/bequest receivable | - | - | 13,148,000 | 13,148,000 |
| Board-designated endowment funds | 12,112,628 | - | - | 12,112,628 |
| Total funds | $12,112,628 | $16,117,067 | $37,803,482 | $66,033,177 |

Endowment net asset composition by type of fund as of June 30, 2014 is as follows:

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total Net Endowment Assets |
|---|---|---|---|---|
| Donor-restricted endowment funds | $ - | $15,880,101 | $23,216,982 | $39,097,083 |
| Endowment major gifts receivable | - | - | 573,781 | 573,781 |
| Board-designated endowment funds | 11,761,241 | - | - | 11,761,241 |
| Total funds | $11,761,241 | $15,880,101 | $23,790,763 | $51,432,105 |

**Donor-restricted endowments**

Changes in donor-restricted endowment net assets as of June 30, 2015 are as follows:

| | Temporarily Restricted | Permanently Restricted | Total Net Endowment Assets |
|---|---|---|---|
| Endowment net assets, beginning of year | $ 15,880,101 | $ 23,216,982 | $ 39,097,083 |
| Contributions and reclassifications | - | 1,438,500 | 1,438,500 |
| Investment income | 475,713 | - | 475,713 |
| Net appreciation | 669,186 | - | 669,186 |
| Amounts appropriated for expenditure and satisfying purpose restrictions | (907,933) | - | (907,933) |
| Endowment net assets, end of year | $ 16,117,067 | $ 24,655,482 | $ 40,772,549 |

Included in contributions and reclassifications is $1,150,000 transferred from temporarily restricted net assets to the permanently restricted endowment for Catholic education, in accordance with LGI purposes.

Changes in donor-restricted endowment net assets as of June 30, 2014 are as follows:

| | Temporarily Restricted | Permanently Restricted | Total Net Endowment Assets |
|---|---|---|---|
| Endowment net assets, beginning of year | $ 9,750,716 | $ 21,485,982 | $ 31,236,698 |
| Contributions | - | 1,731,000 | 1,731,000 |
| Investment income | 383,692 | - | 383,692 |
| Net appreciation | 6,504,184 | - | 6,504,184 |
| Amounts appropriated for expenditure and satisfying purpose restrictions | (758,491) | - | (758,491) |
| Endowment net assets, end of year | $ 15,880,101 | $ 23,216,982 | $ 39,097,083 |

**Board-designated endowment (functioning as endowment)**
Certain amounts of unrestricted net assets, which include the original patrimony of the Diocese, have been designated by the Diocesan Bishop as functioning as endowment. Since these amounts resulted from an internal designation and are not donor-restricted, they are classified and reported as unrestricted net assets (functioning as endowment). This endowment's investment policy, strategy and objectives are similar to the donor-invested policies, except as it relates to investment spending. All investment returns are added to the endowment.

Composition of and changes in board-designated endowment net assets for the year ended June 30, are as follows:

| | Unrestricted | |
|---|---|---|
| | 2015 | 2014 |
| Board-designated endowment net assets, beginning of year | $ 11,761,241 | $ 9,625,921 |
| Investment income | 142,622 | 113,412 |
| Net appreciation | 208,765 | 2,021,908 |
| Board-designated endowment net assets, end of year | $ 12,112,628 | $ 11,761,241 |

## 16. Insurance programs

The Diocese maintains health, property, general liability and workers compensation insurance plans for the Chancery and participating affiliates. Each entity participating in the plans is charged premiums to cover estimated losses, administrative costs, and excess insurance policy premiums.

Under the medical plan, the self-insured retention layer includes an individual loss limit, $250,000 in plan year 2015 and $200,000 in plan year 2014, as well as an aggregate loss limit of up to 125% of expected claims, or about $16,210,000, in plan year March 2015-February 2016. Losses exceeding these amounts are covered by the stop-loss insurance policy with no annual limit on aggregate losses. Incurred but not reported health claims are estimated to be $1,290,000 and $1,477,000 at June 30, 2015 and 2014, respectively.

The Diocese continues to maintain a multi-tiered approach to its risk financing program which includes both risk retention and risk transferring strategies. With regard to workers' compensation, coverage is 100% insured and the Diocese does not retain any exposure for this coverage.

The Diocese retains the first layer of coverage for all other property and casualty exposures with the exception of workers' compensation which is fully insured. The self-insured retention layer is $500,000 per occurrence with an annual aggregate of $1,500,000. The retention amount applies cumulatively to property and liability exposures. The Chancery's estimated exposure for future payments of this layer is $1,247,000 and $618,000 at June 30, 2015 and 2014, respectively. Several layers of excess coverage from various carriers beyond the self-insured retention layer and primary insurance layer exist. The amount of excess coverage differs based on the given line of coverage, and at a minimum provides $1,000,000 of additional insurance.

Prior to July 2007, the second layer of coverage was retained by the Catholic Umbrella Pool II (CUP II) which is a risk retention pool consisting of member Dioceses of which Arlington is included. This coverage provided $5,500,000 in excess of the primary layer of $1,500,000 of insurance coverage. Currently there are 59 participants each with equal voting rights. Participation percentages vary annually based on the exposures of the Diocese and the number of participating entities. The Diocese participation interest has averaged 2% of the total contributions to the Pool.

The Diocese does retain an exposure equal to its participation level in any year should the claims in that year exceed contributions collected. The Chancery estimates no material loss with regard to this participation.

Included in accounts payable and accrued expenses are the following:

| | **2015** | **2014** |
|---|---|---|
| Incurred but not reported estimated health claims | $1,290,000 | $1,477,000 |
| Estimated property and general liability claims | $1,247,000 | $ 618,000 |

## 17. Commitments and contingencies

**Leases**

The Chancery leases office space under a non-cancelable lease agreement with 200 North Glebe Road, Inc., a related entity, which expires July 31, 2017. The lease provides for an automatic adjustment of 3% annually. The financial statements reflect rent expense on a straight-line basis with the excess expense over cash paid reflected in accrued expenses. In addition to lease payments, the office lease generally requires the Chancery to pay any incremental increases in taxes, insurance and utilities. The Chancery also leases office equipment under operating leases expiring through August 2018. Total rent expense, net of sublease rentals for years ended June 30, 2015 and 2014, is as follows:

| | 2015 | 2014 |
|---|---|---|
| Office space | $ 2,089,705 | $ 1,994,020 |
| Office equipment | 69,249 | 111,689 |
| Sublease office rental (related entities) | (421,881) | (361,257) |
| Net expense | $ 1,737,073 | $ 1,744,452 |

At June 30, 2015, future minimum lease payments are as follows:

| | Total Lease | Sublease | Net Lease |
|---|---|---|---|
| 2016 | $ 1,966,305 | $ 383,257 | $ 1,583,048 |
| 2017 | 2,005,454 | 394,755 | 1,610,699 |
| 2018 | 206,510 | 32,976 | 173,534 |
| 2019 | 7,062 | - | 7,062 |
| Total future minimum lease payments | $ 4,185,331 | $ 810,988 | $ 3,374,343 |

**Lines of credit and letters of credit**

The Chancery has obtained lines of credit as follows:

| | June 30, 2015 | | June 30, 2014 | |
|---|---|---|---|---|
| | Total Available | Outstanding | Total Available | Outstanding |
| Operating needs | $ 5,000,000 | $ - | $ 5,000,000 | $ - |
| Building and improvement programs | $ - | $ 4,797,197 | $ - | $ 5,633,503 |
| Standby letters of credit for various construction projects | $ 7,500,000 | $ 2,084,747 | $ 15,000,000 | $ 2,121,498 |

The outstanding building and improvement loans were obtained for the benefit of two parishes. In December 2014 one of the parishes paid its loan in full. The remaining parish is currently paying on and directly liable for the loan with the Chancery acting as guarantor. Under the loan agreement, the Chancery is subject to certain financial covenants such as operating liquidity, minimum net assets, additional indebtedness and financial reporting. The building improvement programs have interest rates ranging from 2.67% to 5.25% for the years ended June 30, 2015 and 2014.

In connection with the bond refinancing and issuance of bank qualified debt, the Chancery renewed its line of credit and letter of credit facility (Note 11). Under the new agreements, the Chancery is subject to certain covenants such as operating liquidity, additional indebtedness, and financial reporting. The line of credit for operating needs had a stated rate of interest based on the 30-day LIBOR plus 195 basis points for the years ended June 30, 2015 and 2014. The issuance fee for standby letters of credit for various parish and Chancery construction projects was 1.5% per annum with a minimum of $200 per letter for the years ended June 30, 2015 and 2014. These facilities are subject to annual renewals by our financial institutions.

**Litigation**

The Diocese has been named as a defendant in various lawsuits. Coverage for each of the lawsuits is provided by either a self-insurance fund or excess insurance coverage. When applicable, reserves have been established for those cases where the potential liability is estimable and probable. In instances where a loss is reasonably possible, but the amount is not estimable no reserve is established. There was no reserve for 2015 and 2014.

## 18. Subsequent event

In August 2015 the Diocese entered into an agreement for the construction of the second phase of the St. Rose of Lima Priests’ Retirement Villa at an estimated contract cost of $2,000,000.