

Combined Financial Statements Together with  
Report of Independent Certified Public Accountants

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**

June 30, 2012 and 2011

# CHANCERY OFFICE OF THE ROMAN CATHOLIC DIOCESE OF PATERSON AND AFFILIATE

## TABLE OF CONTENTS

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	<b>Page</b>
Report of Independent Certified Public Accountants	1
Combined Financial Statements	
Combined Statements of Financial Position as of June 30, 2012 and 2011	2
Combined Statement of Activities for the year ended June 30, 2012	3
Combined Statement of Activities for the year ended June 30, 2011	4
Combined Statements of Cash Flows for the years ended June 30, 2012 and 2011	5
Notes to Combined Financial Statements	6 - 28

## REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Most Reverend Arthur J. Serratelli  
**Bishop of the Roman Catholic Diocese of Paterson:**

We have audited the accompanying combined statements of financial position of the Chancery Office of the Roman Catholic Diocese of Paterson and Affiliate (the “Chancery”) as of June 30, 2012 and 2011 and the related combined statements of activities and cash flows for the years then ended. These combined financial statements are the responsibility of the Chancery’s management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America as established by the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Chancery’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall combined financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the combined financial position of the Chancery Office of the Roman Catholic Diocese of Paterson and Affiliate as of June 30, 2012 and 2011, and the changes in their net assets and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

*Grant Thornton LLP*

Edison, New Jersey  
November 26, 2012

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Combined Statements of Financial Position**  
**As of June 30, 2012 and 2011**

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<b>ASSETS</b>	<b>2012</b>	<b>2011</b>
Cash and cash equivalents	\$ 3,022,905	\$ 2,511,466
Accounts and loans receivable, net	13,560,010	16,969,243
Contributions receivable, net	839,356	1,449,342
Investments, at fair value	15,292,463	15,507,585
Mortgage receivables	5,500,938	7,091,672
Crypt inventory	12,141,037	11,940,761
Land, buildings and equipment, net	17,801,826	17,491,677
Other assets	<u>1,691,756</u>	<u>1,198,002</u>
Total assets	<u>\$ 69,850,291</u>	<u>\$ 74,159,748</u>
 <b>LIABILITIES AND NET ASSETS</b>		
<b>LIABILITIES</b>		
Accounts payable and accrued expenses	\$ 3,135,211	\$ 3,194,990
Amounts payable to related parties	24,430,168	24,646,978
Debt obligations	4,082,919	7,038,040
Conditional asset retirement obligations	5,152,243	4,815,630
Reserves for self-insurance	6,500,069	4,648,448
Liability for postretirement benefits	<u>23,800,420</u>	<u>21,886,327</u>
Total liabilities	<u>67,101,030</u>	<u>66,230,413</u>
 Commitments and contingencies		
<b>NET ASSETS</b>		
Unrestricted	(2,164,335)	2,740,189
Temporarily restricted	684,873	1,011,797
Permanently restricted	<u>4,228,723</u>	<u>4,177,349</u>
Total net assets	<u>2,749,261</u>	<u>7,929,335</u>
Total liabilities and net assets	<u>\$ 69,850,291</u>	<u>\$ 74,159,748</u>

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

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Combined Statement of Activities**  
**For the year ended June 30, 2012**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
<b>REVENUES, GAINS AND OTHER SUPPORT</b>				
Parish assessments	\$ 4,699,511	\$ -	\$ -	\$ 4,699,511
Annual appeal	3,147,338	-	-	3,147,338
Contributions	1,326,854	20,451	56,641	1,403,946
Rental income	2,400,081	-	-	2,400,081
Cemetery income	1,120,221	-	-	1,120,221
Property and liability insurance program	6,568,650	-	-	6,568,650
Employee benefits program	20,226,648	-	-	20,226,648
Other	936,047	-	-	936,047
Central lending agency program	851,891	-	-	851,891
Interest and dividend income	1,052,961	10,250	-	1,063,211
Net unrealized and realized losses	(522,808)	(6,810)	-	(529,618)
Recovery of uncollectible accounts, net	4,146,390	-	-	4,146,390
Gain on sale of land	228,931	-	-	228,931
	<u>46,182,715</u>	<u>23,891</u>	<u>56,641</u>	<u>46,263,247</u>
Net assets released from restriction	320,815	(320,815)	-	-
Total revenues, gains and other support	<u>46,503,530</u>	<u>(296,924)</u>	<u>56,641</u>	<u>46,263,247</u>
<b>EXPENSES</b>				
Programs:				
Evangelization	1,766,105	-	-	1,766,105
Social ministry	1,817,499	-	-	1,817,499
Pastoral	4,487,131	-	-	4,487,131
Communications	123,317	-	-	123,317
Annual appeal	245,380	-	-	245,380
Schools subsidies and other educational expenses	2,051,517	-	-	2,051,517
Cemetery - cost of sales and expenses	853,786	-	-	853,786
Property and liability insurance program	7,410,689	-	-	7,410,689
Employee benefits program	22,021,182	-	-	22,021,182
Central lending agency program	330,151	-	-	330,151
Property rental	645,259	-	-	645,259
Total program expenses	<u>41,752,016</u>	<u>-</u>	<u>-</u>	<u>41,752,016</u>
Supporting services:				
General and administration	9,533,508	30,000	5,267	9,568,775
Total expenses	<u>51,285,524</u>	<u>30,000</u>	<u>5,267</u>	<u>51,320,791</u>
Change in net assets before postretirement-related changes other than net periodic benefit cost	(4,781,994)	(326,924)	51,374	(5,057,544)
Postretirement-related changes other than net periodic benefit cost	<u>(122,530)</u>	<u>-</u>	<u>-</u>	<u>(122,530)</u>
Change in net assets	(4,904,524)	(326,924)	51,374	(5,180,074)
Net assets, beginning of year	<u>2,740,189</u>	<u>1,011,797</u>	<u>4,177,349</u>	<u>7,929,335</u>
Net assets, end of year	<u>\$ (2,164,335)</u>	<u>\$ 684,873</u>	<u>\$ 4,228,723</u>	<u>\$ 2,749,261</u>

*The accompanying notes are an integral part of this combined statement.*

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Combined Statement of Activities**  
**For the year ended June 30, 2011**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
<b>REVENUES, GAINS AND OTHER SUPPORT</b>				
Parish assessments	\$ 5,381,054	\$ -	\$ -	\$ 5,381,054
Annual appeal	3,138,586	-	-	3,138,586
Contributions	870,842	387,463	918,455	2,176,760
Rental income	1,435,778	-	-	1,435,778
Cemetery income	1,059,109	-	-	1,059,109
Property and liability insurance program	8,243,197	-	-	8,243,197
Employee benefits program	19,446,001	-	-	19,446,001
Other	1,239,938	-	-	1,239,938
Central lending agency program	795,820	-	-	795,820
Interest and dividend income	1,210,667	10,276	-	1,220,943
Net unrealized and realized gains	567,992	5,896	-	573,888
Recovery of uncollectible accounts, net	1,684,763	-	-	1,684,763
Gain on sale of land	1,042,384	-	-	1,042,384
	<u>46,116,131</u>	<u>403,635</u>	<u>918,455</u>	<u>47,438,221</u>
Net assets released from restriction	303,303	(303,303)	-	-
Total revenues, gains and other support	<u>46,419,434</u>	<u>100,332</u>	<u>918,455</u>	<u>47,438,221</u>
<b>EXPENSES</b>				
Programs:				
Evangelization	2,016,161	-	-	2,016,161
Social ministry	1,815,653	-	-	1,815,653
Pastoral	4,858,525	-	-	4,858,525
Communications	113,685	-	-	113,685
Annual appeal	334,543	-	-	334,543
Schools subsidies and other educational expenses	4,787,062	-	-	4,787,062
Cemetery - cost of sales and expenses	911,012	-	-	911,012
Property and liability insurance program	4,485,790	-	-	4,485,790
Employee benefits program	19,646,745	-	-	19,646,745
Central lending agency program	342,866	-	-	342,866
Property rental	874,638	-	-	874,638
Total program expenses	<u>40,186,680</u>	<u>-</u>	<u>-</u>	<u>40,186,680</u>
Supporting services:				
General and administration	8,077,396	-	-	8,077,396
Total expenses	<u>48,264,076</u>	<u>-</u>	<u>-</u>	<u>48,264,076</u>
Change in net assets before postretirement-related changes other than net periodic benefit cost	(1,844,642)	100,332	918,455	(825,855)
Postretirement-related changes other than net periodic benefit cost	<u>(9,411,232)</u>	<u>-</u>	<u>-</u>	<u>(9,411,232)</u>
Change in net assets	(11,255,874)	100,332	918,455	(10,237,087)
Net assets, beginning of year	13,996,063	911,465	3,258,894	18,166,422
Net assets, end of year	<u>\$ 2,740,189</u>	<u>\$ 1,011,797</u>	<u>\$ 4,177,349</u>	<u>\$ 7,929,335</u>

*The accompanying notes are an integral part of this combined statement.*

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Combined Statements of Cash Flows**  
**For the years ended June 30, 2012 and 2011**

	<u>2012</u>	<u>2011</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Change in net assets	\$ (5,180,074)	\$ (10,237,087)
Adjustments to reconcile change in net assets to net cash used in operating activities		
Depreciation and amortization	589,671	557,866
Recovery on uncollectible accounts and loans receivable, net	(4,163,690)	(1,684,763)
Change in discount allowance on contributions receivable	(21,966)	22,012
Change in provision for allowance on uncollectible contributions receivable	6,536	-
Unrealized and realized depreciation (appreciation) in fair value of investments	529,618	(573,888)
Contributions restricted for endowment	(56,641)	(426,480)
Contributed services - land, building and equipment	(100,660)	-
Gain on sale of land, buildings and equipment	(228,931)	(1,042,384)
Accretion of interest on conditional asset retirement obligations	336,613	314,622
Changes in assets and liabilities:		
Decrease in accounts and loans receivable	4,617,802	1,327,051
Decrease (increase) in contributions receivable	625,416	(508,276)
Increase in crypt inventory	(200,276)	(2,831,108)
Increase in other assets	(493,754)	(220,530)
(Decrease) increase in accounts payable and accrued expenses	(216,990)	62,579
Increase (decrease) in reserves for self-insurance	1,851,621	(3,801,359)
Increase in liability for postretirement benefits	1,914,093	10,410,970
Net cash used in operating activities	<u>(191,612)</u>	<u>(8,630,775)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from sale of investments	3,086,518	10,406,779
Purchase of investments	(3,401,014)	(1,335,175)
Payments received on mortgage receivable	1,590,734	222,385
Proceeds from sale of land, buildings and equipment	350,149	706,464
Purchase of land, buildings and equipment	(763,167)	(1,797,081)
Net cash provided by investing activities	<u>863,220</u>	<u>8,203,372</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Deposits received from related parties	5,049,734	3,577,709
Repayment of deposits received from related parties	(5,266,544)	(4,036,844)
Contributions restricted for endowment	56,641	426,480
Net cash used in financing activities	<u>(160,169)</u>	<u>(32,655)</u>
 Net increase (decrease) in cash and cash equivalents	 511,439	 (460,058)
Cash and cash equivalents, beginning of year	<u>2,511,466</u>	<u>2,971,524</u>
Cash and cash equivalents, end of year	<u>\$ 3,022,905</u>	<u>\$ 2,511,466</u>
<b>SUPPLEMENTAL DATA</b>		
Mortgage receivable received from sale of land, buildings and equipment	<u>\$ -</u>	<u>\$ 419,000</u>
Assets acquired under capital lease arrangements	<u>\$ 157,211</u>	<u>\$ -</u>

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

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Notes to Combined Financial Statements**  
**June 30, 2012 and 2011**

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**1. NATURE OF THE ENTITY**

The accompanying combined financial statements reflect the financial activities of the Chancery Office of the Roman Catholic Diocese of Paterson which includes the assets, liabilities, net assets, and activities of the central business operations, the self-insurance programs, the catastrophic healthcare plan for Diocesan priests, and Calvary Cemetery, (collectively referred to as the “Chancery”). The Chancery’s accounts do not include the assets, liabilities, net assets, or activities of individual parishes, missions, schools, and social service organizations, among others.

The Chancery provides financing, investing, employee benefit programs and other services to various Diocesan affiliated organizations that include, but are not limited to Diocesan parishes, educational institutions, social service agencies, and cemeteries, which share a common mission with the Bishop of Paterson.

The Roman Catholic Diocese of Paterson (the “Diocese”) is a separately incorporated entity in the State of New Jersey. The Diocese has ultimate responsibility and oversight of all Roman Catholic Church entities in the counties of Passaic, Morris, and Sussex in Northern New Jersey. The Diocese is under the leadership of Bishop Arthur Joseph Serratelli and provides oversight to the parishes, schools, agencies, and ministries that serve the 425,000 Catholics who live in the geographic area of the Diocese. These entities may or may not be separately incorporated; however, each is distinct from the Chancery and maintains separate financial records. This oversight comes from both civil law and Canon Law declaring the authority and responsibilities of the Diocese.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation**

The accompanying combined financial statements have been prepared under accounting principles generally accepted in the United States of America (“US GAAP”). All inter-entity transactions have been eliminated in combination. The following represents the Chancery’s significant accounting policies.

**Classifications of Net Assets**

The Chancery reports its net assets and changes therein based on the existence or absence of donor-imposed restrictions as follows:

Unrestricted Net Assets consist of the following subcategories:

Undesignated Net Assets - includes all funds that are expendable, at the discretion of the Chancery, for carrying on daily operations. These funds have neither been restricted by donors nor set aside for any specific purpose.

Designated Net Assets - includes amounts set aside for specific program service needs and used at the sole discretion of the Bishop of Paterson. The operating use of these resources, however, is not externally restricted.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

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As of June 30, 2012 and 2011, the Chancery's unrestricted undesignated net assets reflected a deficit of \$24,531,049 and \$21,326,567, respectively, which is largely the result of obligations due under the priests' postretirement welfare benefit plan and provisions for loan losses related to amounts owed to the Chancery by parishes, schools and social service agencies in the Diocese.

Unrestricted designated net assets at June 30, 2012 and 2011 consisted of the following:

	<u>2012</u>	<u>2011</u>
Prepare The Way	\$ 19,976,513	\$ 20,499,214
Other designated funds	<u>2,390,201</u>	<u>3,567,542</u>
Total designated net assets	<u>\$ 22,366,714</u>	<u>\$ 24,066,756</u>

Designated net assets are set aside to address the pastoral, charitable and financial needs of parishes, schools and Diocesan ministries.

Temporarily Restricted Net Assets - net assets subject to donor-imposed stipulations that either expire with the passage of time or can be fulfilled by the actions of the Chancery pursuant to those stipulations. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets. However, when restrictions on donor-restricted contributions are met in the same accounting period, such amounts are reported as part of unrestricted net assets.

Temporarily restricted net assets at June 30, 2012 and 2011 consisted of the following:

	<u>2012</u>	<u>2011</u>
For use in the subsequent fiscal periods	\$ 641,224	\$ 957,366
For support of specific programs	<u>43,649</u>	<u>54,431</u>
Total temporarily restricted net assets	<u>\$ 684,873</u>	<u>\$ 1,011,797</u>

Permanently Restricted Net Assets - includes funds wherein donors have stipulated that the principal contributed be invested and maintained in perpetuity. Income earned from these investments is available for expenditures according to restrictions imposed by the donors. As of June 30, 2012 and 2011, permanently restricted net assets of \$4,228,723 and \$4,177,349 consisted principally of support for priestly formation and Catholic education.

**Cash and Cash Equivalents**

The Chancery considers all highly liquid investments with original maturities of three months or less from the date of purchase to be cash and cash equivalents, except for those cash equivalents which are included in the Chancery's investment portfolio which are held for long-term investment purposes.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Notes to Combined Financial Statements**  
**June 30, 2012 and 2011**

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**Investments**

Investments in equity and debt securities with readily determinable fair values are recorded at fair value determined on the basis of quoted market values. Investments in alternative investments are recorded at the Chancery's unit value in these funds as reported by the respective external investment managers. All investments are managed by outside investment advisors subject to the review, approval, and control by the Chancery. Such valuations involve assumptions and methods that are reviewed by the Chancery.

Purchases and sales of securities are reflected on a trade-date basis. Gains and losses on sales of securities are determined based on average cost and are recorded in the statement of activities in the period in which the securities are sold. Dividends and interest are recognized as earned.

Investment securities, in general, are exposed to various risks, such as interest rate, credit and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the accompanying combined financial statements.

**Fair Value Measurements**

The Chancery follows guidance that defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This standard provides a consistent definition of fair value, which focuses on an exit price between market participants in an orderly transaction. The standard also prioritizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that observable inputs be used when available.

Observable inputs are inputs that market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs reflect assumptions that market participants would use in pricing the asset or liability based on the best information available in the circumstances. The hierarchy is categorized into three levels based on the transparency of inputs as follows:

- Level 1 - Quoted prices are available in active markets for identical assets or liabilities as of the report date. A quoted price for an identical asset or liability in an active market provides the most reliable fair value measurement because it is directly observable to the market.
- Level 2 - Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the report date. The nature of these securities include investments for which quoted prices are available but traded less frequently and investments that are fair valued using other securities, the parameters of which can be directly observed. Also included in Level 2 are investments measured using a net asset value ("NAV") per share, or its equivalent, that may be redeemed at NAV at the date of the statement of financial position or in the near term, which the Chancery has determined to be within 90 days.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Notes to Combined Financial Statements**  
**June 30, 2012 and 2011**

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Level 3 - Securities that have little to no pricing observability as of the report date. These securities are measured using management's best estimate of fair value, where the inputs into the determination of fair value are not observable and require significant management judgment or estimation. Also included in Level 3 are investments measured using a NAV per share, or its equivalent, that can never be redeemed at NAV or for which redemption at NAV is uncertain due to lockup periods or other investment restrictions.

Inputs are used in applying the various valuation techniques and broadly refer to the assumptions that market participants use to make valuation decisions, including assumptions about risk. Inputs may include price information, volatility statistics, specific and broad credit data, liquidity statistics, and other factors. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. However, the determination of what constitutes "observable" requires significant judgment by the Chancery. The Chancery considers observable data to be that market data that is readily available, regularly distributed or updated, reliable and verifiable, not proprietary, and provided by independent sources that are actively involved in the relevant market. The categorization of a financial instrument within the hierarchy is based upon the pricing transparency of the instrument and does not necessarily correspond to the Chancery's perceived risk of that instrument.

**Concentration of Market and Credit Risks**

Cash, cash equivalents and investments are exposed to interest rate, market, and credit risks. The Chancery maintains its cash and cash equivalents in various bank deposit accounts that, at times, may exceed federally insured limits. To minimize risk, the Chancery's cash accounts are placed with high-credit quality financial institutions, and the Chancery's investment portfolio is diversified with several investment managers in a variety of asset classes. The Chancery regularly evaluates its depository arrangements and investments, including performance thereof.

The Chancery has loaned funds to parishes and other related entities in excess of \$1 million, and these loans are generally unsecured.

**Accounts, Loans and Contributions Receivable**

Accounts and loans receivable relate primarily to amounts due from parish assessments, employee benefits, and insurance premiums and loans to parishes, educational institutions, and other Diocesan affiliated organizations that are in financial need bearing interest at a fixed rate of 3.31% for both years ending as of June 30, 2012 and 2011. Contributions receivable relate primarily to unconditional promises to give to be received in future periods. Because of the uncertainty surrounding the collection, management provides an allowance for doubtful accounts based on consideration of the type of receivable, responsible party, the known financial condition of the respective parish or Diocesan affiliated organization, historical collection patterns and comparative aging. These allowances are maintained at a level management considers adequate to provide for subsequent adjustments and potential uncollectible accounts. These estimates are reviewed periodically and if the financial condition of the responsible party changes significantly, the Chancery will re-evaluate the recoverability of any accounts, loans and contributions receivable from that organization. The Chancery writes off any amounts that are no longer considered to be recoverable, and any payments subsequently received on such receivables are recorded as income in the period received.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

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**Land, Buildings, and Equipment**

Land, buildings, and equipment are stated at cost, or in the case of donations, at fair value on the date of the gift. Additions and improvements costing more than \$2,000 and with useful lives greater than one year are capitalized. Maintenance and repairs are expensed as incurred. Depreciation expense is calculated using the straight-line method over the following useful lives:

	<u>Years</u>
Buildings	40
Building and land improvements	10 - 20
Furniture and fixtures	10
Machinery and equipment	5

**Crypt Inventory**

Crypt inventory, which represents the cost of each unsold space, is stated at the lower of cost (computed based on the allocation of total costs incurred in the construction of the mausoleums) or market. As sales are made, inventory is reduced by the cost of the space sold.

**Amounts Payable to Related Parties**

Amounts received and held by the Chancery on behalf of related parties are recorded as amounts payable to related parties on the accompanying combined statement of financial position. These amounts primarily relate to deposits from parishes, schools, social service agencies and various Diocesan affiliated organizations to the Central Lending Agency program administered by the Chancery, bearing interest at a fixed rate of 1.31% for both years ending as of June 30, 2012 and 2011.

**Contributions and Other Revenue**

Contributions and unconditional promises to give are recognized as revenue in the period received. Conditional contributions and promises to give are recorded as revenue when the conditions on which they depend have been substantially met. Contributions of non-monetary assets are recorded at the estimated fair value of the assets contributed at the date of the gift. Contributions to be received after one year are recorded at the present value of their estimated future cash flows using an appropriate rate of return. Amortization of discount is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any.

Contributions are reported as increase in unrestricted net assets unless use of the related assets are limited by donor-imposed restrictions. Contributions that are permanently restricted by donors for use as endowments are invested in perpetuity. The income is used for operating purposes when expenditures satisfy the donors' restrictions and such amounts are appropriated for expenditure. Income amounts that exceed related expenditures during a fiscal period remain as temporarily restricted net assets.

Calvary sells rights to graves and crypts for which revenue is recognized upon date of sale. Other unrestricted revenues and support and gains are recorded as income when earned or realized.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Notes to Combined Financial Statements**  
**June 30, 2012 and 2011**

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**Donated Materials and Services**

The Chancery recognizes in its combined financial statements the fair value of donated materials and services. Donated materials are recorded as contributions at their estimated fair value at the date of receipt. The Chancery recognizes donated services provided by individuals possessing specialized skills which would typically need to be purchased if not provided by donation.

During fiscal 2012, the Chancery received approximately \$101,000 of contractor services for the construction of St. Paul Inside the Walls - the Catholic Center for Evangelization located in Madison, NJ. Such amounts have been included in contributions revenue and also capitalized as part of land, buildings, and equipment, net, in the accompanying combined financial statements.

**Bishop's Annual Appeal Contributions**

During September of each calendar year, a direct appeal is made to the people of the Diocese for operating support. Annual appeal contributions are recognized as unrestricted operating support in the year received.

**Program Services**

Included in operating expenses are the costs of evangelization, social ministry, pastoral, communications, educational, property and liability insurance, employee benefits and other program services provided directly by the Chancery, including subsidies given to Diocesan related organizations providing such services. These costs have been summarized on a functional basis. Accordingly, certain costs have been allocated amongst the programs and supporting services benefited.

**Special Collections**

Parishes throughout the Diocese conduct special offertory collections on designated days for the benefit of other non-Diocesan Catholic entities at the direction of the U.S. Conference of Catholic Bishops. The amounts collected by the parishes are remitted to the Chancery and then transferred to the entities for whom the collections were conducted. The parishes and the Chancery act as agents for the collections and the amounts collected are not revenues to the parishes or the Chancery. As of June 30, 2012 and 2011, special collections of approximately \$565,000 and \$566,000, respectively, have been reflected within accounts payable and accrued expenses in the accompanying combined statement of financial position.

**Use of Estimates**

The preparation of the combined financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the combined statement of financial position and the reported amounts of revenues and expenses during the reporting period. The most significant management judgments and estimates used in the preparation of the accompanying combined financial statements relate to the determination of depreciation expense, the reported fair value of certain financial instruments, the actuarial assumptions used to determine the reserves for self-insurance and liability for postretirement benefits, provision for operating accruals and the collectability of accounts, loans and contributions receivable. Actual results could differ from those estimates.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Notes to Combined Financial Statements**  
**June 30, 2012 and 2011**

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**Fair Value of Financial Instruments**

The estimated fair values of the Chancery's financial instruments have been determined by the Chancery, using appropriate market information and valuation methodologies. Considerable judgment is required to develop the estimates of fair value; thus, the estimates provided herein are not necessarily indicative of the amounts that could be realized in a current market exchange.

The carrying value of cash, cash equivalents, accounts payable and accrued expenses, and other liabilities is a reasonable estimate of their fair value due to their short-term nature. The carrying value of accounts and loans receivables has been reduced by an appropriate allowance for uncollectible accounts, based on historical collection experience and therefore approximates net realizable value. The carrying value of contributions receivable is estimated based on the present value of expected future cash flows from these receivables, and thus approximates fair value.

**Reclassifications**

Certain reclassifications were made to the 2011 financial statements in order to conform to the 2012 presentation. Such reclassifications did not change total assets, liabilities, revenues, expense or changes in net assets as reflected in the 2011 financial statements.

**Income Taxes**

The Chancery follows guidance that established criterion that an individual tax position must meet for some or all of the benefits of that position to be recognized in an entity's financial statements. This standard requires the Chancery to determine whether a tax position is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The Chancery has processes presently in place to ensure the maintenance of its tax-exempt status; to identify and report unrelated income; determine its filing and tax obligations in jurisdictions for which it has nexus; and to review other matters that may be considered tax positions. As of June 30, 2012 and 2011, management has determined that the Chancery has no uncertain tax positions that would require recognition or disclosure in the combined financial statements.

In an annually updated ruling, the Internal Revenue Service has held that agencies, instrumentalities and educational, charitable, and religious institutions operated, supervised, or controlled by or in connection with the Roman Catholic Church in the United States, its territories or possessions appearing in "The Official Catholic Directory" are exempt from federal income tax under provisions of Section 501(c)(3) of the Internal Revenue Code. The Diocese is listed in "The Official Catholic Directory" and therefore is exempt from income tax. Accordingly, the accompanying combined financial statement reflects no provision for income taxes. The tax years ending 2009, 2010 and 2011 are still open to audit for both federal and state purposes.

**Subsequent Events**

The Chancery evaluated its June 30, 2012 combined financial statements for subsequent events through November 26, 2012, the date the combined financial statements were available to be issued. The Chancery is not aware of any material subsequent events which would require recognition or disclosure in the accompanying combined financial statements.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

**3. ACCOUNTS AND LOANS RECEIVABLE, NET**

As of June 30, 2012 and 2011, accounts and loans receivable, net, consisted of the following:

	<u>2012</u>	<u>2011</u>
Parishes and schools	\$ 42,250,632	\$ 49,750,976
Social services agencies	2,175,733	2,311,953
Other	<u>859,766</u>	<u>1,138,299</u>
	45,286,131	53,201,228
Less: Allowance for doubtful accounts	<u>(31,726,121)</u>	<u>(36,231,985)</u>
Accounts and loans receivable, net	<u>\$ 13,560,010</u>	<u>\$ 16,969,243</u>

The activity for the allowance for impaired loans to parishes and schools, social service agencies and other is as follows as of June 30, 2012:

	<u>Parishes and Schools</u>	<u>Social Service Agencies</u>	<u>Other</u>	<u>Total</u>
<b>Allowance for doubtful accounts, beginning of year</b>	\$ 34,123,492	\$ 2,011,879	\$ 96,614	\$ 36,231,985
Change in allowance	(1,536,213)	-	17,300	(1,518,913)
Recoveries of amounts previously reserved	(2,555,026)	(72,451)	-	(2,627,477)
Write-offs	<u>(356,474)</u>	<u>-</u>	<u>(3,000)</u>	<u>(359,474)</u>
<b>Allowance for doubtful accounts, end of year</b>	<u>\$ 29,675,779</u>	<u>\$ 1,939,428</u>	<u>\$ 110,914</u>	<u>\$ 31,726,121</u>

At June 30, 2012 and 2011, included in accounts and loans receivables are \$44,885,893 and \$52,599,006 due from related parties, less an allowance for doubtful accounts of \$31,615,207 and \$36,135,371, respectively.

**4. CONTRIBUTIONS RECEIVABLE, NET**

Contributions receivable, net, consisted of the following unconditional promises to give at June 30, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Amounts expected to be collected in:		
Less than one year	\$ 603,844	\$ 858,747
One to five years	<u>482,025</u>	<u>852,538</u>
	1,085,869	1,711,285
Less:		
Reserve for uncollectible pledges	(217,508)	(210,972)
Discount for present value	<u>(29,005)</u>	<u>(50,971)</u>
	<u>\$ 839,356</u>	<u>\$ 1,449,342</u>

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

A discount for pledges to be received over periods longer than one year from date of contribution is provided using appropriate credit-adjusted discount rate assigned in the year the pledge originates and ranged from approximately 2.29% to 3.04% at June 30, 2012 and 2011.

During fiscal 2012, the Chancery determined that certain amounts received in prior years previously reported as unrestricted contributions should have been recorded as a liability since the Chancery was not the ultimate beneficiary of the gift instruments. As a result, the Chancery recognized approximately \$1,255,000 within general and administration expense during fiscal 2012 and recorded a corresponding liability within amounts payable to related parties. Chancery management has evaluated this adjustment and concluded that it did not have a material impact on the Chancery's fiscal 2012 combined financial statements or its previously issued combined financial statements.

**5. INVESTMENTS, AT FAIR VALUE**

As of June 30, 2012 and 2011, investments, at fair value, by fair value hierarchy, consisted of the following:

	<b>2012</b>			<b>Total</b>
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
Equities	\$ 7,690,046	\$ -	\$ -	\$ 7,690,046
Fixed income	4,307,474	-	-	4,307,474
Exchange traded funds	927,526	-	-	927,526
Money market funds	195,312	-	-	195,312
Limited partnership interests	-	-	670,594	670,594
Hedge funds	-	782,528	718,983	1,501,511
	<u>\$ 13,120,358</u>	<u>\$ 782,528</u>	<u>\$ 1,389,577</u>	<u>\$ 15,292,463</u>

  

	<b>2011</b>			<b>Total</b>
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
Equities	\$ 7,811,431	\$ -	\$ -	\$ 7,811,431
Fixed income	4,524,880	-	-	4,524,880
Exchange traded funds	948,545	-	-	948,545
Money market funds	65,075	-	-	65,075
Limited partnership interests	-	-	677,045	677,045
Hedge funds	-	750,562	730,047	1,480,609
	<u>\$ 13,349,931</u>	<u>\$ 750,562</u>	<u>\$ 1,407,092</u>	<u>\$ 15,507,585</u>

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

The following table summarizes the changes in Chancery's Level 3 investments for the years ended June 30, 2012 and 2011:

<b>Balance as of July 1, 2010</b>	\$ 4,109,445
Withdrawals	(300,000)
Net depreciation of investments	<u>(2,402,353)</u>
<b>Balance as of June 30, 2011</b>	1,407,092
Net depreciation of investments	<u>(17,515)</u>
<b>Balance as of June 30, 2012</b>	<u>\$ 1,389,577</u>

The Chancery's policy is to recognize transfers in and transfers out at the end of the reporting period.

Since hedge funds and limited partnership interests may not be readily marketable, the estimated fair value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for such investments existed, and the differences could be material. The values assigned to these holdings do not necessarily represent amounts which might ultimately be realized upon sale or other disposition since such amounts depend on future circumstances and cannot reasonably be determined until the actual liquidation occurs.

The Chancery uses NAV per share, or its equivalent, to determine the fair value of all the underlying investments which: (a) do not have a readily determinable fair value and (b) prepare its financial statements consistent with the measurement principles of an investment company or have the attributes of an investment company. The following table lists such investments by major category:

2012								
Type	Strategy	NAV In funds	# of Funds	Remaining Life	\$ Amount Of Unfunded Commitments	Redemption Terms	Redemption Restrictions	Redemption Restrictions In Place At Year End
Hedge fund	Invests primarily in illiquid portfolio funds that offer the potential for higher long-term returns	\$ 718,983	1	Subject to the determination of the respective fund manager	N/A	Semi-annually as of June 30 or December 31 upon 30 days notice	Redemption may not be requested prior to the 12th month-end after a subscription dealing day	N/A
Hedge fund	Seeks long-term capital appreciation thru investments in US fixed income instruments and non-US sovereign debt securities	\$ 782,528	1	Subject to the determination of the respective fund manager	N/A	Daily upon 10 days notice	N/A	N/A

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

2011

Type	Strategy	NAV In funds	# of Funds	Remaining Life	\$ Amount Of Unfunded Commitments	Redemption Terms	Redemption Restrictions	Redemption Restrictions In Place At Year End
Hedge fund	Invests primarily in illiquid portfolio funds that offer the potential for higher long-term returns	\$ 730,047	1	Subject to the determination of the respective fund manager	N/A	Semi-annually as of June 30 or December 31 upon 30 days notice	Redemption may not be requested prior to the 12th month-end after a subscription dealing day	N/A
Hedge fund	Seeks long-term capital appreciation thru investments in US fixed income instruments and non-US sovereign debt securities	\$ 750,562	1	Subject to the determination of the respective fund manager	N/A	Daily upon 10 days notice	N/A	N/A

The components of investment return for the year ended June 30, 2012 and 2011, follow:

	<u>2012</u>	<u>2011</u>
Dividends and interest*	\$ 508,497	\$ 405,325
Net realized gains (losses)	54,496	(254,076)
Net unrealized (depreciation) appreciation	<u>(584,114)</u>	<u>827,964</u>
Total investment (loss) return	<u>\$ (21,121)</u>	<u>\$ 979,213</u>

\* This amount excludes interest income of approximately \$555,000 and \$816,000 earned by the Chancery on accounts and loans receivable and mortgage receivable in fiscal years 2012 and 2011, respectively.

Investment management fees approximated \$20,000 in fiscal years 2012 and 2011, and were expensed on the accompanying combined statement of activities.

## 6. MORTGAGE RECEIVABLES

In October 2002, the Chancery extended a \$8,000,000 mortgage note to Martin De Porres Village, Inc., a related party of the Diocese, to operate a low-income housing project for senior citizens, families, and disabled individuals, among others. The mortgage bears interest at a fixed rate of 7.00% per annum. Principal and interest are payable monthly over a twenty-five (25) year period and the mortgage is secured by the assignment of leases covering the property. As of June 30, 2012 and 2011, the outstanding mortgage receivable was \$5,090,540 and \$6,672,672, respectively.

In June 2011, the Chancery sold property located in Clifton, New Jersey to Zion Church of God, Inc. ("Zion"), an unrelated third party, for \$619,000. In connection with the sale, the Chancery extended a \$419,000 mortgage note to Zion. The mortgage bears interest at a fixed rate of 5.75% per annum and is secured by the property. Principal and interest commenced in August 2011 and are payable monthly over a twenty (20) year period. As of June 30, 2012 and 2011, the outstanding mortgage receivable was \$410,398 and \$419,000, respectively.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

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**7. CRYPT INVENTORY**

As of June 30, 2012 and 2011, crypt inventory, consisted of the following:

	<u>2012</u>	<u>2011</u>
Mausoleum Unit I	\$ 126,409	\$ 126,838
Mausoleum Unit II	122,263	124,865
Mausoleum Unit III	1,045,299	1,088,124
Mausoleum Unit IV	<u>10,847,066</u>	<u>10,600,934</u>
Crypt inventory	<u>\$ 12,141,037</u>	<u>\$ 11,940,761</u>

**8. LAND, BUILDINGS AND EQUIPMENT, NET**

The principal properties owned by the Chancery reflected in the accompanying combined statement of financial position include Nazareth Village Priests' Retirement Home, Pope John Paul II Elementary School, and the following high schools: DePaul Catholic, Morris Catholic, Paterson Catholic, Pope John XXIII, Neumann Preparatory, and Bayley-Ellard.

Land, buildings and equipment, net, consisted of the following as of June 30, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Buildings and improvements	\$ 26,844,332	\$ 26,687,658
Machinery, equipment and furniture	<u>1,335,187</u>	<u>1,083,224</u>
	28,179,519	27,770,882
Less: Accumulated depreciation and amortization	<u>(15,749,803)</u>	<u>(15,267,431)</u>
	12,429,716	12,503,451
Land	2,895,015	2,961,015
Undeveloped land	2,027,211	2,027,211
Construction in progress	<u>449,884</u>	<u>-</u>
Land, buildings and equipment, net	<u>\$ 17,801,826</u>	<u>\$ 17,491,677</u>

At June 30, 2012 and 2011, included in buildings and improvements are capitalized conditional asset retirement obligations at a cost of approximately \$423,000 that were fully depreciated. At June 30, 2012, included in machinery, equipment and furniture are assets acquired under capital lease arrangements at a cost of approximately \$157,000 with accumulated amortization of approximately \$15,000.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

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**9. DEBT OBLIGATIONS**

The Chancery has entered into various credit facility agreements with certain lending institutions on behalf of DePaul Catholic (“DePaul”), Morris Catholic (“Morris”), and Pope John XXIII (“PJ XXIII”) high schools. Accordingly, as of June 30, 2012 and 2011, the Chancery has recorded a receivable of \$3,936,827 and \$7,038,040, respectively, due from DePaul, Morris, and PJ XXIII corresponding to the debt obligations. These receivables are included within accounts and loans receivable in the accompanying combined statement of financial position. Repayments on these credit facilities are made by DePaul and PJ XXIII and paid directly to the respective lender.

Such debt obligations consisted of the following at June 30, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Valley National Bank - field loan (a)	\$ 25,000	\$ 75,409
Valley National Bank - term loan (b)	-	2,127,114
Valley National Bank - term loan (c)	-	342,009
Lakeland Bank - term loan (d)	565,551	855,913
Lakeland Bank - term loan (e)	762,350	852,134
Wells Fargo Bank - term loan (f)	<u>2,583,926</u>	<u>2,785,461</u>
	<u>\$ 3,936,827</u>	<u>\$ 7,038,040</u>

**Valley National Bank - Field Loan (a)**

On December 9, 2002, the Chancery entered into a unsecured loan agreement with Valley National Bank on behalf of DePaul for the purpose of renovating one of its athletic fields. The amount of this loan was \$500,000 with payments for a period of 120 months. Principal is payable quarterly and interest is payable monthly commencing on January 1, 2003 and the first day of each month through maturity on December 1, 2012. As of June 30, 2012 and 2011, the rate of this loan was 4.75%.

**Valley National Bank - Term Loan (b)**

On February 23, 2005, the Chancery entered into a line of credit agreement with Valley National Bank on behalf of DePaul for the purpose of constructing an addition to and renovating existing buildings at the high school. Effective August 1, 2006 the line of credit was converted to an unsecured term loan. The amount of this loan was \$3,500,000 with payments for a period of 120 months. Principal and interest were payable monthly commencing on September 1, 2006 and the first day of each month through maturity on August 1, 2016.

On November 22, 2011, this loan was refinanced and restructured with Valley National Bank to lower the fixed interest rate. In addition, the loan was modified to have DePaul service as the primary obligor with the Chancery serving only as a guarantor. The result of this transaction reduced the Chancery’s accounts and loans receivable and debt obligations as of June 30, 2012.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Notes to Combined Financial Statements**  
**June 30, 2012 and 2011**

---

**Valley National Bank - Term Loan (c)**

On August 11, 2003, the Chancery entered into a line of credit agreement with Valley National Bank on behalf of Morris for the purpose of installing a synthetic turf system at the high school. Effective August 1, 2006, the line of credit was converted to an unsecured term loan. The amount of this loan was \$800,000 with payments for a period of 180 months. Principal and interest were payable monthly commencing on November 1, 2003 and the first day of each month through maturity on October 1, 2018.

On August 1, 2011, this loan was refinanced and restructured with Lakeland Bank to include additional principal which were used to repay a loan between Morris and the Chancery. In addition, the loan was modified to have Morris service as the primary obligor with the Chancery serving only as a guarantor. The result of this transaction reduced the Chancery's accounts and loans receivable and debt obligations as of June 30, 2012.

**Lakeland Bank - Term Loan (d)**

On August 18, 1999, the Chancery entered into a term loan agreement with Lakeland Bank on behalf of PJ XXIII for the purpose of constructing additional classroom space at the high school. The amount of this loan was \$1,800,000 with payments for a period of 240 months. Principal and interest are payable monthly commencing on September 1, 1999 and the first day of each month through maturity on September 1, 2019. Lakeland Bank has been granted a security interest in the land and buildings at 28 Andover Rd., Sparta N.J. which is the physical location of PJ XXIII. As of June 30, 2012 and 2011, the rate of this loan was 4.52%.

**Lakeland Bank - Term Loan (e)**

On April 27, 2001, the Chancery entered into a term loan agreement with Lakeland Bank on behalf of PJ XXIII for the purpose of constructing a new gymnasium at the school. The amount of this loan was \$1,500,000 with payments for a period of 240 months. Principal and interest are payable monthly commencing on September 1, 1999 and the first day of each month through maturity on April 27, 2022. Lakeland Bank has been granted a security interest in the land and buildings at 28 Andover Rd., Sparta N.J. which is the physical location of PJ XXIII. As of June 30, 2012 and 2011, the rate of this loan was 6.15%.

**Wells Fargo Bank – Term Loan (f)**

In May 2012, the Chancery amended its existing \$4,000,000 line of credit facility agreement with Wells Fargo Bank on behalf of PJ XXIII to an unsecured term loan agreement. The total amount of the loan is approximately \$2,630,000 and matures on May 31, 2013. The loan bears interest at 1 month LIBOR plus 1.0% (1.25% at June 30, 2012). Outstanding borrowings on the previous line of credit facility bore interest at 1 month LIBOR plus 1.0% (1.18% at June 30, 2011).

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

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At June 30, 2012, aggregate principal payments due over each of the next five fiscal years and thereafter follow:

<b>Year Ending June 30,</b>	
2013	\$ 2,774,308
2014	174,283
2015	183,672
2016	193,579
2017	204,037
Thereafter	406,948
	<u>\$ 3,936,827</u>

Interest expense on long-term debt for the years ended June 30, 2012 and 2011 totaled approximately \$152,000 and \$324,000, respectively.

**Capital Lease Obligation**

At June 30, 2012, future minimum lease payments due under the Chancery's capital lease obligation follow:

<b>Year Ending June 30,</b>	
2013	\$ 37,320
2014	37,320
2015	37,320
2016	37,320
2017	21,770
Total minimum lease payments	<u>171,050</u>
Less: amount representing interest	<u>(24,958)</u>
Present value of minimum lease payments	<u>\$ 146,092</u>

**10. CONDITIONAL ASSET RETIREMENT OBLIGATIONS**

The Chancery is required to recognize a conditional asset retirement obligation ("CARO") related to the cost associated with the eventual remediation and abatement of asbestos located within the construct of certain buildings. The total CARO liability at June 30, 2012 and 2011 totaled \$5,152,243 and \$4,815,630, respectively. For the years ended June 30, 2012 and 2011, the accretion of interest related to these obligations totaled \$336,613 and \$314,622, respectively.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

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**11. SELF-INSURANCE PROGRAMS**

The Chancery participates and maintains self-insurance programs for medical, pharmacy, general liability, property damage, automobile damage, unemployment compensation, workers' compensation and long-term disability. The participants of these programs also include the parishes, institutions and agencies owned by or related to the Diocese. Premiums charged to the various, non-Chancery, participating organizations and payments made on insurance claims are reported as revenues and expenses, respectively, within the employee benefits and property and liability insurance programs in the accompanying combined statement of activities. Insurance program costs for Chancery departments are reflected in the accompanying combined statement of activities within their respective functional classification.

For the July 1, 2010 to June 30, 2011 policy period, the Chancery was not fully self-insured relating to its property and liability insurance program, retaining only the automobile damage exposure. Effective July 1, 2011, the Chancery elected to resume self-insurance on its entire property and liability insurance program.

**Employee Benefits**

Employees of the participating organizations are provided health benefits under the self-insured program which is administered by a third party claims administrator. As of June 30, 2012 and 2011, the Chancery had deposited approximately \$553,000 and \$526,000, respectively, with the claims administrator as a good faith deposit against these payments. These deposits are included as other assets in the accompanying combined statement of financial position.

**Property and Liability Insurance**

Under this program, the Chancery is liable for the first \$250,000 of a property damage claim, as well as the first \$250,000 of a general liability or auto claim, with additional coverage in excess of the above amounts purchased through outside insurance agencies. Self-insurance reserves have been developed based on an actuarial model based on historical claims and industry experience.

As of June 30, 2012 and 2011, the actuarially determined liabilities for employee benefits and property and liability insurance consisted of the following:

	<b>2012</b>		
	<b>Case Reserve</b>	<b>Incurred But Not Reported</b>	<b>Total</b>
Employee medical and pharmacy plan	\$ -	\$ 1,945,659	\$ 1,945,659
General liability, automobile, workers' compensation and property coverage	<u>1,890,194</u>	<u>2,290,104</u>	<u>4,180,298</u>
Total liability for self-insurance claims	<u>\$ 1,890,194</u>	<u>\$ 4,235,763</u>	<u>\$ 6,125,957</u>

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

	2011		
	Case Reserve	Incurred But Not Reported	Total
Employee medical and pharmacy plan	\$ -	\$ 1,554,323	\$ 1,554,323
General liability, automobile, workers' compensation and property coverage	<u>1,257,985</u>	<u>1,268,586</u>	<u>2,526,571</u>
Total liability for self-insurance claims	<u>\$ 1,257,985</u>	<u>\$ 2,822,909</u>	<u>\$ 4,080,894</u>

Additionally, the Chancery has recorded a liability for unemployment benefits and long-term disability of \$374,112 and \$567,554 as of June 30, 2012 and 2011, respectively.

**12. POSTRETIREMENT BENEFITS**

**Lay Pension Plan**

The Chancery participates in a noncontributory defined benefit pension plan which covers substantially all full-time lay employees. Under this plan the employer contributions are made by the Chancery, Diocesan High Schools and other Diocesan organizations and parishes, which employ covered plan members. Upon retirement, participants will receive 1) a pension of 1.25% of their average earnings for the highest three years in the plan, multiplied by their years of participation in the plan, 2) enrollment in the American Association of Retired Persons' Medicare Supplement Health Insurance program and 3) certain specified death benefits. Contributions to the lay pension plan by the Chancery for the years ended June 30, 2012 and 2011 totaled approximately \$361,000 and \$324,000, respectively.

**Priests' Pension Plan**

The Chancery also participates in a noncontributory priests' pension plan covering all priests. Upon retirement each priest will receive a pension of \$3,150 per month. Effective July 1, 2010, the priests' pension plan no longer pays for normal medical, dental and automobile insurance benefits for retired priests. Such costs have been assumed by the priests' postretirement welfare benefit plan which is administered by the Chancery. Annual contribution rates for the year ended June 30, 2012 and 2011 were \$18,100 a year per priest. Contributions to the priests' pension plan by the Chancery for the years ended June 30, 2012 and 2011 totaled approximately \$442,000 and \$597,000, respectively.

The Lay and Priest pension plans are considered church plans and are therefore exempt from the provisions of the Employee Retirement Income Security Act of 1974 ("ERISA"), as amended. Due to the nature of these plans, it is not practicable to determine the extent to which the assets of the plans cover the actuarially computed value of vested benefits for the Chancery as a standalone operation. As such, the actuarial present value of accumulated plan benefits and the fair value of plan assets have not been recorded in the accompanying combined statement of financial position. In addition, because the plans are considered multiemployer plans, they are only subject to certain minimum reporting requirements.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

As of July 1, 2012 and 2011, the following is a summary of the accumulated Plan benefits covering all participants (unaudited):

	<b>2012</b>	
	<u>Lay</u>	<u>Priest</u>
Vested benefits:		
Participants currently receiving payments	\$ 63,130,835	\$ 19,191,513
Other participants	<u>47,902,099</u>	<u>8,514,299</u>
	111,032,934	27,705,812
Non-vested benefits	<u>1,853,343</u>	<u>334,468</u>
Total actuarial present value of accumulated plan benefits	<u>\$ 112,886,277</u>	<u>\$ 28,040,280</u>
Fair value of plan assets	<u>\$ 89,822,176</u>	<u>\$ 14,115,180</u>
Funded status	<u>\$ (23,064,101)</u>	<u>\$ (13,925,100)</u>
	<b>2011</b>	
	<u>Lay</u>	<u>Priest</u>
Vested benefits:		
Participants currently receiving payments	\$ 61,528,580	\$ 16,288,557
Other participants	<u>43,403,032</u>	<u>9,782,385</u>
	104,931,612	26,070,942
Non-vested benefits	<u>2,134,769</u>	<u>247,472</u>
Total actuarial present value of accumulated plan benefits	<u>\$ 107,066,381</u>	<u>\$ 26,318,414</u>
Fair value of plan assets	<u>\$ 91,904,044</u>	<u>\$ 14,573,995</u>
Funded status	<u>\$ (15,162,337)</u>	<u>\$ (11,744,419)</u>

**Priests' Postretirement Welfare Benefit Plan**

The Chancery administers and participates in a postretirement welfare benefit plan covering all Diocesan priests. Effective July 1, 2010, the priests' postretirement welfare benefit plan pays for normal medical, dental and automobile insurance benefits for retired priests. The Chancery contributes 100% of dental and automobile benefits and all medical benefits in excess of the priest's annual contribution of \$2,721 toward their medical benefits. Prior to July 1, 2010, these costs were paid by the priests' pension plan.

This plan also provides long-term catastrophic healthcare. This coverage is self-funded by premiums charged to the various parishes and Diocesan organizations which employ Diocesan priests. For the years ended June 30, 2012 and 2011, approximately \$439,875 and \$458,000, respectively, was billed and included as employee benefits program revenue in the accompanying combined statement of

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

---

activities. Upon admission into a long-term healthcare facility, the Chancery contributes approximately 75% of the cost for long term healthcare with the priest responsible for the remaining balance.

The accumulated benefit obligation recognized in the accompanying combined statement of financial position at June 30, 2012 and 2011, is as follows:

	<u>2012</u>	<u>2011</u>
Accumulated benefit obligation, beginning of fiscal year	\$ 19,440,983	\$ 9,080,750
Interest cost	1,052,479	796,218
Service cost	278,486	109,735
Benefits paid	(610,008)	(786,476)
Actuarial loss	1,161,719	4,451,583
Transfer from pension plan	-	5,789,173
Accumulated benefit obligation, end of fiscal year	<u>\$ 21,323,659</u>	<u>\$ 19,440,983</u>
Funded status of plan at fiscal year end	<u>\$ (21,323,659)</u>	<u>\$ (19,440,983)</u>
Amounts not yet reflected in net periodic benefit cost and included in unrestricted net assets:		
Unrecognized prior service cost	\$ 1,817,653	\$ 2,172,592
Unrecognized actuarial loss	14,683,331	14,205,862
	<u>\$ 16,500,984</u>	<u>\$ 16,378,454</u>

The weighted average rates used to determine the accumulated benefit obligation as of June 30, 2012 and 2011, were:

	<u>2012</u>	<u>2011</u>
Discount rate	3.96%	5.50%
Health-care cost trend rate assumed for next year	8.50%	9.00%
Ultimate health-care cost trend rate	5.00%	5.00%
Year ultimate health-care cost trend rate is achieved	2018	2018

Components of net periodic benefit cost in the combined statement of activities consisted of the following:

	<u>2012</u>	<u>2011</u>
Service cost	\$ 278,486	\$ 109,735
Interest cost	1,052,479	796,218
Amortization of actuarial loss	684,250	474,585
Amortization of prior service cost	354,939	354,939
Net periodic benefit cost	<u>\$ 2,370,154</u>	<u>\$ 1,735,477</u>

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

---

The weighted-average rates used to determine net periodic benefit cost for the years ended June 30, 2012 and 2011, were:

	<u>2012</u>	<u>2011</u>
Discount rate	5.50%	6.25%
Health-care cost trend rate assumed for next year	8.50%	9.00%
Ultimate health-care cost trend rate	5.00%	5.00%

Other changes in the accumulated benefit obligation recognized in unrestricted net assets were as follows:

	<u>2012</u>	<u>2011</u>
Net actuarial loss arising during measurement period	\$ 1,161,719	\$ 4,451,583
Amortization of actuarial loss	(684,250)	(474,585)
Amortization of prior service cost	(354,939)	(354,939)
Transfer from pension plan	-	5,789,173
Postretirement-related changes other than net periodic benefit cost	<u>\$ 122,530</u>	<u>\$ 9,411,232</u>

For the years ended June 30, 2012, the effect of a 1% change in the health care cost trend rate was as follows:

	<u>1% Increase</u>	<u>1% Decrease</u>
Effect on net periodic benefit cost	\$ 309,264	\$ (243,659)
Effect on accumulated benefit obligation	7,752,725	(36,440)

The estimated prior service cost and actuarial loss that will be amortized into net periodic benefit cost during fiscal 2012 are \$0 and \$722,982, respectively.

Plan benefits expected to be paid in the following fiscal years are as follows:

2013	\$ 531,917
2014	605,160
2015	674,780
2016	636,911
2017	670,335
2018 - 2022	4,301,129

Because the plan is unfunded, the future benefit payments also represent the expected contributions to the plan for that year.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

---

**Other**

The Chancery also provided postretirement benefits to certain priests and lay employees outside of the plans noted above. As of June 30, 2012 and 2011, the Chancery has recorded a liability of \$2,476,761 and \$2,445,344, respectively, for those benefits, and is included within liability for postretirement benefits in the accompanying combined statement of financial position.

**13. ENDOWMENT**

The Chancery's donor-restricted (gifted) endowment consists of three donor-restricted endowment funds established principally for the support of priestly formation and Catholic education, and it excludes permanently restricted contributions receivable. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

**Interpretation of Relevant Law**

The Chancery has interpreted the New Jersey Uniform Prudent Management of Institutional Funds Act ("UPMIFA") as requiring the preservation of the fair value of the original gift as of the gift date of the respective donor-restricted endowment fund 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 of income to the permanent endowment made in accordance with the direction of the applicable donor gift instrument. Therefore, permanently restricted endowment net assets represent the original corpus of gifts given to the Chancery for which the gift instruments stipulate that the principal be invested in perpetuity and only income be used for donor intended purposes, if any.

Net appreciation earned on the corpus of permanently restricted endowment net assets, under New Jersey UPMIFA, is spendable, and, accordingly, the Chancery classifies the appreciation as temporarily restricted net assets, pending appropriation for expenditure by the Bishop of Paterson.

The Chancery's endowment was \$3,978,371 and \$3,612,430 at June 30, 2012 and 2011 and consisted of the following net asset classes:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
<b>2012</b>				
Donor restricted endowment funds	\$ (95,869)	\$ 43,648	\$ 4,030,592	\$ 3,978,371
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
<b>2011</b>				
Donor restricted endowment funds	\$ (127,375)	\$ 54,431	\$ 3,685,374	\$ 3,612,430

Excluded from permanently restricted net assets in the table above at June 30, 2012 and 2011 is \$198,131 and \$491,975, respectively, of contributions receivable.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
Notes to Combined Financial Statements  
June 30, 2012 and 2011

The Chancery's individual endowment funds are managed separately for investment purposes. The investment portfolio is managed to achieve a prudent long-term total return. The Chancery 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 Chancery targets a diversified asset allocation that places an equal emphasis on equity-based and fixed income investments to achieve its long-term return objectives within prudent risk constraints.

The following tables summarize the Chancery's total return on endowment investments and the changes in endowment net assets for the year ended June 30, 2012 and 2011:

2012	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Endowment net assets, beginning of year</b>	\$ (127,375)	\$ 54,431	\$ 3,685,374	\$ 3,612,430
Dividends and interest on endowment investments	93,885	10,250	-	104,135
Net realized and unrealized appreciation in fair value of endowment investments	(62,379)	(6,810)	-	(69,189)
New gifts and pledges	-	-	345,218	345,218
Endowment return used for operations	-	(14,223)	-	(14,223)
<b>Endowment net assets, end of year</b>	<u>\$ (95,869)</u>	<u>\$ 43,648</u>	<u>\$ 4,030,592</u>	<u>\$ 3,978,371</u>

  

2011	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Endowment net assets, beginning of year</b>	\$ (237,089)	\$ 48,387	\$ 3,158,894	\$ 2,970,192
Dividends and interest on endowment investments	77,049	10,276	-	87,325
Net realized and unrealized appreciation in fair value of endowment investments	44,205	5,896	-	50,101
New gifts and pledges	-	-	526,480	526,480
Endowment return used for operations	(11,540)	(10,128)	-	(21,668)
<b>Endowment net assets, end of year</b>	<u>\$ (127,375)</u>	<u>\$ 54,431</u>	<u>\$ 3,685,374</u>	<u>\$ 3,612,430</u>

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level the Chancery is required to maintain as a fund of permanent duration. Deficiencies of this nature generally resulted from unfavorable market fluctuations or prudent appropriations by the Bishop that reduced the fair value of individual endowment funds below historical dollar value, as permitted by the State of New Jersey UPMIFA. In accordance with US GAAP, such amounts, which total \$95,869 and \$127,375 at June 30, 2012 and 2011, respectively, have been charged to unrestricted net assets. Subsequent investment earnings on such funds which restore the fair value of individual endowment funds back to their original corpus value are reported in unrestricted net assets, with earnings in excess of this amount reported in temporarily restricted net assets.

**CHANCERY OFFICE OF THE ROMAN CATHOLIC  
DIOCESE OF PATERSON AND AFFILIATE**  
**Notes to Combined Financial Statements**  
**June 30, 2012 and 2011**

---

**14. GUARANTEES**

The Chancery has guaranteed the repayment of certain loans obtained directly by parishes and social service agencies related to the Diocese. At June 30, 2012 and 2011, outstanding amounts due to lenders approximated \$9,164,000 and \$5,840,000, respectively. Should the Diocesan related organizations default on the loans, the Chancery would become liable for all remaining payments due to the lender. Management is currently not aware of any defaults or circumstances that would require the Chancery to perform under such guarantees and as such, no loss provision has been recognized as of June 30, 2012 and 2011.

**15. COMMITMENTS AND CONTINGENCIES**

The Chancery, in the ordinary course of business, is a party to various litigation involving contract and conduct related claims, and other miscellaneous causes of action arising from Diocesan activities. While it is not feasible to predict the ultimate outcomes of such matters, management of the Chancery is not aware of any claims or contingencies, which are not covered by insurance that would have a material adverse effect on the Chancery's combined financial position, changes in net assets and cash flows.

Various school, parish and mission properties are not included in the property accounts, nor are the operations of these entities reflected in the accompanying combined financial statements. In the event that any of the entities fiscally responsible to the Chancery, are unable to fulfill their operating commitment, any liens or claims against these properties and/or deficits from their operations, if any, would become a liability to the Chancery. Management is currently not aware of any events that would require the Chancery to accrue for such financial commitments as of June 30, 2012 and 2011.

The Chancery has entered into various non-cancellable operating leases primarily for office equipment.

Future minimum lease payments due under these arrangements are as follows:

**Year Ending June 30:**

2013	\$ 20,738
2014	8,296
2015	4,150
2016	3,935
2017	1,579
	<u>\$ 38,698</u>

Rent expense for the years ended June 30, 2012 and 2011 totaled approximately \$59,000 and \$78,000, respectively.