

CHANCERY OF THE DIOCESE OF CHARLESTON  
CHARLESTON, SOUTH CAROLINA

AUDITED FINANCIAL STATEMENTS

FOR THE YEARS ENDED JUNE 30, 2008 AND 2007



## CONTENTS

	Page
Independent Auditors' Report	1
Statements of Financial Position	2
Statements of Activities	3
Statements of Changes in Unrestricted Net Assets	4
Statements of Cash Flows	5
Notes to Financial Statements	6 - 15



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## INDEPENDENT AUDITORS' REPORT

Rev. Msgr. Martin T. Laughlin  
Administrator of the Diocese of Charleston  
Charleston, South Carolina

We have audited the accompanying statement of financial position of the Chancery of the Diocese of Charleston as of June 30, 2008, and the related statements of activities, changes in unrestricted net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Chancery's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Chancery of the Diocese of Charleston as of June 30, 2007, were audited by other auditors whose report dated January 22, 2008, expressed a qualified opinion on those statements.

We conducted our audit 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 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in the notes to the financial statements, depreciation has not been recognized in the financial statements for exhaustible property and equipment. In our opinion, accounting principles generally accepted in the United States of America requires that exhaustible property and equipment be depreciated over their estimated useful lives. The effects of this departure from accounting principles generally accepted in the United States of America on the financial statements are not reasonably determinable.

In our opinion, except for the effects of not depreciating exhaustible property and equipment over their estimated useful lives, as discussed in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Chancery of the Diocese of Charleston as of June 30, 2008, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As more fully described in the note "Organization", the Chancery is not a separate legal entity, but a separate and identifiable operating unit of the Diocese of Charleston. These financial statements only contain the assets, liabilities, equity, revenue and expenses of this operating unit.

As more fully discussed in the notes, "Class Action Settlement" and "Contingencies", the Chancery is involved in certain legal and other actions which have been addressed in the accompanying financial statements as detailed in the notes.

A handwritten signature in black ink that reads "GlaserDuncan, CPAs". The signature is written in a cursive, flowing style.

January 16, 2009

STATEMENTS OF FINANCIAL POSITION  
 CHANCERY OF THE DIOCESE OF CHARLESTON

	June 30,	
	<u>2008</u>	<u>2007</u>
<b>ASSETS</b>		
Cash	\$ 14,526,855	\$ 9,270,730
Investments	36,890,060	45,275,423
Receivables from other Diocesan entities:		
Loans receivable, net	7,906,137	6,360,550
Other receivables, net	636,287	183,490
Other receivables	1,720,892	1,064,404
Cash restricted for property projects	2,245,995	-
Bonds debt service fund	653,438	643,830
Other assets	1,047,499	936,277
Property and equipment	<u>19,920,994</u>	<u>19,917,765</u>
<b>TOTAL ASSETS</b>	<u>\$ 85,548,157</u>	<u>\$ 83,652,469</u>
<b>LIABILITIES AND NET ASSETS</b>		
Liabilities:		
Accounts payable and accrued expenses	\$ 2,113,419	\$ 9,179,615
Savings deposits	14,596,618	12,216,623
Due to other Diocesan or Catholic Church entities	5,218,374	4,408,268
Interest rate swap agreement	425,577	135,194
Notes payable	10,992,235	4,688,241
Bonds payable	<u>8,090,000</u>	<u>8,825,000</u>
<b>TOTAL LIABILITIES</b>	<u>41,436,223</u>	<u>39,452,941</u>
Net Assets:		
Unrestricted:		
Designated for insurance reserve	1,580,745	1,552,610
Designated for cemeteries care	3,037,304	3,283,978
Designated for investment and endowments	10,752,428	12,208,239
Property and equipment	15,587,435	15,229,524
Operating	<u>1,338,770</u>	<u>2,180,690</u>
Total unrestricted	32,296,682	34,455,041
Temporarily restricted	8,963,671	7,540,675
Permanently restricted	<u>2,851,581</u>	<u>2,203,812</u>
<b>TOTAL NET ASSETS</b>	<u>44,111,934</u>	<u>44,199,528</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u>\$ 85,548,157</u>	<u>\$ 83,652,469</u>

See notes to financial statements.

STATEMENTS OF ACTIVITIES  
 CHANCERY OF THE DIOCESE OF CHARLESTON

	<u>YEARS ENDED JUNE 30,</u>	
	<u>2008</u>	<u>2007</u>
<b>UNRESTRICTED NET ASSETS</b>		
Total support and revenue	\$ 9,237,105	\$ 12,168,463
Net assets released from restrictions	<u>3,023,949</u>	<u>3,938,541</u>
Total support, revenue, and reclassifications	12,261,054	16,107,004
Total expenses	<u>14,129,030</u>	<u>20,520,273</u>
Decrease in unrestricted net assets before derivative adjustment	(1,867,976)	(4,413,269)
Fair value adjustment on interest rate swap agreement	<u>(290,383)</u>	<u>(18,202)</u>
Decrease in unrestricted net assets	<u>(2,158,359)</u>	<u>(4,431,471)</u>
 <b>TEMPORARILY RESTRICTED NET ASSETS</b>		
Support and revenue:		
Contributions	5,210,882	4,158,749
Investment income	117,638	144,908
Net realized gain on investment transactions	114,942	325,496
Net unrealized gain (loss) on investment transactions	<u>(348,748)</u>	<u>210,414</u>
Total support and revenue	5,094,714	4,839,567
Net assets released from restrictions	(3,023,949)	(3,938,541)
Net assets transferred from temporarily restricted classification	<u>(647,769)</u>	<u>-</u>
Increase in temporarily restricted net assets	<u>1,422,996</u>	<u>901,026</u>
 <b>PERMANENTLY RESTRICTED NET ASSETS</b>		
Net assets transferred to permanently restricted classification	<u>647,769</u>	<u>-</u>
 <b>DECREASE IN NET ASSETS</b>		
	(87,594)	(3,530,445)
NET ASSETS AT BEGINNING OF YEAR	<u>44,199,528</u>	<u>47,729,973</u>
NET ASSETS AT END OF YEAR	<u>\$ 44,111,934</u>	<u>\$ 44,199,528</u>

See notes to financial statements.

STATEMENTS OF CHANGES IN UNRESTRICTED NET ASSETS  
 CHANCERY OF THE DIOCESE OF CHARLESTON

	<u>YEARS ENDED JUNE 30,</u>	
	<u>2008</u>	<u>2007</u>
Support and revenue:		
Parish assessment income	\$ 4,415,390	\$ 4,297,587
Contributions and bequests	355,237	600,356
Interest income	787,220	669,879
Investment income	1,199,674	1,297,414
Net realized gain on investment transactions	704,971	1,197,648
Net unrealized gain (loss) on investment transactions	(2,006,288)	786,602
Net loss from property and equipment transactions	(78,709)	(26,125)
Auxiliary activities	2,296,324	2,113,483
Other revenue	<u>1,563,286</u>	<u>1,231,619</u>
 Total support and revenue	 9,237,105	 12,168,463
 Net assets released from time restrictions or restrictions satisfied by payments	 <u>3,023,949</u>	 <u>3,938,541</u>
 Total unrestricted support, revenue and reclassifications	 <u>12,261,054</u>	 <u>16,107,004</u>
 Expenses:		
Program services:		
Pastoral	2,820,736	2,504,158
Church personnel development	1,419,927	1,459,805
Education	1,522,089	1,195,272
Cemeteries	361,444	358,056
Deposit and loan, including interest of \$905,675 in 2008 and \$841,980 in 2007	965,344	906,015
Auxiliary expenses	<u>1,598,862</u>	<u>1,546,397</u>
 Total program services	 <u>8,688,402</u>	 <u>7,969,703</u>
Supporting services:		
General and administration, including interest of \$286,056 in 2008 and \$200,119 in 2007	3,449,278	2,844,340
Development	<u>356,250</u>	<u>1,106,230</u>
 Total supporting services	 <u>3,805,528</u>	 <u>3,950,570</u>
 Class action settlement	 <u>1,635,100</u>	 <u>8,600,000</u>
 Total expenses	 <u>14,129,030</u>	 <u>20,520,273</u>
 Decrease in unrestricted net assets before derivative adjustment	 (1,867,976)	 (4,413,269)
 Fair value adjustment on interest rate swap agreement	 <u>(290,383)</u>	 <u>(18,202)</u>
 Decrease in unrestricted net assets	 <u>\$ (2,158,359)</u>	 <u>\$ (4,431,471)</u>

See notes to financial statements.

STATEMENTS OF CASH FLOWS  
 CHANCERY OF THE DIOCESE OF CHARLESTON

	<u>YEARS ENDED JUNE 30,</u>	
	<u>2008</u>	<u>2007</u>
Cash flows from operating activities:		
Changes in net assets	\$ (87,594)	\$ (3,530,445)
Adjustments to reconcile the changes in net assets to net cash provided (used) by operating activities:		
Contributions restricted for property projects	(2,245,995)	-
Amortization of bonds issuance costs	8,740	8,740
Donated property	-	(84,000)
Investment income - bonds debt service fund	(9,608)	(20,969)
Net (gain) loss on investment transactions	1,535,123	(2,520,160)
Net loss from property and equipment transactions	78,709	26,125
Fair value adjustment on interest rate swap agreement	290,383	18,202
Increase in receivables and other assets	(1,239,635)	(220,610)
Increase in accounts payable and accrued expenses	<u>(7,066,196)</u>	<u>7,812,727</u>
Net cash provided (used) by operating activities	<u>(8,736,073)</u>	<u>1,489,610</u>
Cash flows from investing activities:		
Increase in cash restricted for property projects	(2,245,995)	-
Proceeds from investment transactions	37,451,126	37,052,455
Purchases of investments	(30,600,886)	(39,054,116)
Increase in loans receivable	(2,737,993)	(1,378,500)
Decrease in loans receivable	1,259,132	1,272,172
Increase in other receivables	(465,801)	(87,990)
Decrease in other receivables	408,213	83,855
Decrease in other assets	1,250	-
Proceeds from dispositions of property and equipment	6,400	400
Purchases of property and equipment	<u>(88,338)</u>	<u>(138,598)</u>
Net cash provided (used) by investing activities	<u>2,987,108</u>	<u>(2,250,322)</u>
Cash flows from financing activities:		
Proceeds from contributions restricted for property projects	2,245,995	-
Increase in savings deposits	4,623,184	3,689,471
Decrease in savings deposits	(2,243,189)	(3,306,066)
Increase in payables to other Diocesan entities	4,496,565	5,569,069
Decrease in payables to other Diocesan entities	(3,686,459)	(3,183,792)
Principal payments on bonds payable	(735,000)	(735,000)
Increase in bonds debt service fund	-	(61,250)
Proceeds from borrowings (notes payable)	6,658,676	-
Principal payments on notes payable	<u>(354,682)</u>	<u>(340,341)</u>
Net cash provided by financing activities	<u>11,005,090</u>	<u>1,632,091</u>
Increase in cash	5,256,125	871,379
Cash at beginning of year	<u>9,270,730</u>	<u>8,399,351</u>
Cash at end of year	<u>\$ 14,526,855</u>	<u>\$ 9,270,730</u>

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS  
CHANCERY OF THE DIOCESE OF CHARLESTON

ORGANIZATION

The Diocese of Charleston (the "Diocese"), a unit of the Roman Catholic Church, is a non-profit corporation organized under the laws of the State of South Carolina under the name of Bishop of Charleston. There are no shareholders, directors or officers in the corporation. There is only the holder of the office of Bishop. The Diocese holds title to all assets and is liable for all indebtedness of its operating entities.

The Diocese consists of various distinct operating entities administered through the Diocesan structure. Each entity maintains its own separate accounts and carries on specific services and programs. The various entities can be categorized as follows: the Chancery, which includes various diocesan level programs or activities (pastoral, church personnel development, educational support and the Diocesan educational offices for Catholic Youth Ministry, Religious Education, and the Catholic Schools Office, Diocesan cemeteries, cooperative investment and lending program, and auxiliary services involving certain insurance activities and the Diocesan newspaper, The Miscellany) and diocesan level administrative support offices; Parishes and Missions; Diocesan Educational Entities; Catholic Charities; and others. The accompanying financial statements include only the programs and administrative support offices of the Chancery of the Diocese of Charleston.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Chancery have been prepared on the accrual basis of accounting and, accordingly, reflect all significant receivables, payables and other liabilities.

The Chancery's financial statement presentation follows the recommendations of the Financial Accounting Standards Board in its Statement of Financial Accounting Standards (SFAS) No.117, "Financial Statements of Not-for-Profit Organizations". Under SFAS No. 117, the Chancery is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Receivables are stated at amounts the Chancery expects to collect (unpaid principal balances less estimated allowances for doubtful accounts) based on the Chancery's assessment of the financial stability of the respective debtors. Receivables determined by the Chancery to not be collectible are charged off against the respective allowances.

Investments in equity securities with readily determinable fair values and all debt securities are stated at their fair values.

Purchases of property and equipment having a unit cost of \$5,000 or more are capitalized at cost. Donated property and equipment are capitalized at their estimated fair value at the date of donation. However, historical costs are not available for certain assets acquired before 1972. For these assets, insured or appraised values have been used. No provision is made for depreciation of exhaustible property and equipment.

The Chancery uses an interest rate swap agreement to manage its exposure to interest rate changes with respect to its bonds payable. The interest rate swap agreement is a derivative instrument and, as required by SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended, has been reported in the accompanying financial statements at fair value.

Costs incurred in connection with the issuance of bonds are being amortized over the term of the bonds.

Parish assessment income is recorded as revenue in the year the parishes are assessed. Such revenue is calculated and assessed based upon an approved percentage of each parish's adjusted income for the preceding year.

Contributions are considered to be unrestricted unless specifically restricted by the donors. Contributions that are restricted by the donors are reported as increases in the temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statements of Activities and of Changes in Unrestricted Net Assets as net assets released from restrictions.

Investment income consists of the interest income, dividend income and the realized gains/losses within mutual funds from assets classified as investments in the accompanying financial statements. Interest income consists of the interest earned on assets, other than investments.



NOTES TO FINANCIAL STATEMENTS  
 CHANCERY OF THE DIOCESE OF CHARLESTON

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

The Diocese is exempt from federal and state income taxes under certain provisions of the Internal Revenue Code and the South Carolina Code of Laws; therefore, no provisions for income taxes have been included in these financial statements.

The costs of providing various programs and other activities have been summarized on a functional basis in the Statements of Changes in Unrestricted Net Assets. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

For purposes of the Statements of Cash Flows, the Chancery considers all highly liquid temporary cash investments with a maturity of three months or less when purchased to be cash equivalents, except for the cash investments in the funds managed by investment companies and cash held by the bond trustee.

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

RECLASSIFICATIONS

Certain amounts in the 2007 financial statements have been reclassified to conform with the presentation in the 2008 financial statements.

CASH

Cash consists of interest-bearing checking accounts, savings accounts, money-market accounts, and certificates of deposit with a maturity of three months or less when purchased.

INVESTMENTS

Investments at June 30, 2008 consist of the following:

	<u>Cost</u>	<u>Fair Value</u>
Certificates of deposit (with maturity greater than three months when purchased) with banks	\$ 9,121,143	\$ 9,121,143
Cash investments with investment companies	1,073,994	1,073,994
Mutual funds	3,904,593	4,186,220
Mortgage and asset backed securities	670,423	677,115
Corporate and government debt securities	11,532,255	11,655,443
Equity securities	<u>10,244,642</u>	<u>10,176,145</u>
	<u>\$ 36,547,050</u>	<u>\$ 36,890,060</u>

Investments at June 30, 2007 consist of the following:

	<u>Cost</u>	<u>Fair Value</u>
Certificates of deposit (with maturity greater than three months when purchased) with banks	\$ 10,925,877	\$ 10,925,877
Cash investments with investment companies	5,602,619	5,602,619
Mutual funds	4,584,334	5,299,273
Mortgage and asset backed securities	697,937	696,081
Corporate and government debt securities	10,636,530	10,744,839
Equity securities	<u>9,976,742</u>	<u>12,006,734</u>
	<u>\$ 42,424,039</u>	<u>\$ 45,275,423</u>

NOTES TO FINANCIAL STATEMENTS  
 CHANCERY OF THE DIOCESE OF CHARLESTON

INVESTMENTS-Continued

Certain of the Chancery's investments are maintained in funds managed by investment companies. Other Diocesan entities (e.g. - parishes, schools, etc.) also participate in these investment funds. Investment income and realized and unrealized gains and losses are allocated monthly to the respective Chancery and other Diocesan entity accounts maintained for these pooled investments. Only the Chancery's share of these pooled investments is reflected in the accompanying financial statements. A recap of these pooled investments follows:

	<u>2008</u>	<u>2007</u>
Chancery	\$ 21,761,657	\$ 23,671,941
Other Diocesan entities	<u>8,500,012</u>	<u>14,720,463</u>
	<u>\$ 30,261,669</u>	<u>\$ 38,392,404</u>

The Chancery's share of these pooled investments has been allocated to the respective classifications of investments as of June 30, 2008 and 2007 detailed previously in this note.

At June 30, 2008, certificates of deposits totaling approximately \$297,000 were pledged as collateral with respect to certain letters of credit; and certain pooled investment accounts with fair values totaling approximately \$12,926,000 were pledged as collateral with respect to Note 5 (see the note, "Notes Payable"). These pooled investment accounts are subject to the terms of a pledge agreement and to certain account control agreements with Bank of America.

Subsequent to June 30, 2008, the fair values of the pooled investments declined by approximately 16% as of December 31, 2008.

RECEIVABLES FROM OTHER DIOCESAN ENTITIES

Loans receivable consist of the loans made under the lending program of the Chancery. The loans are primarily due from parishes and schools in varying amounts through 2025 and bear interest at varying rates. The loans are stated at their unpaid balances less estimated allowances for doubtful accounts of approximately \$735,000 and \$802,000 at June 30, 2008 and 2007, respectively.

The Diocese obtains blanket property, liability and health insurance for the Chancery and certain other Diocesan entities. The Chancery pays the premiums and bills the Diocesan entities for their portion of the premiums. In addition, the Chancery bills parishes for their annual parish assessments. Receivables related to these billings principally comprise the other receivables from other Diocesan entities. These receivables are stated at their unpaid balances less estimated allowances for doubtful accounts of approximately \$44,000 and \$23,000 at June 30, 2008 and 2007, respectively.

OTHER RECEIVABLES

	<u>2008</u>	<u>2007</u>
Mortgage note receivable, secured by property in Charleston, South Carolina, due in monthly installments totaling \$7,871, including interest at 5.75%, with a final payment of all unpaid note principal and interest due in July 2015	\$ 552,424	\$ 613,208
Insurance claim receivables, principally related to the class action settlement (see Note, "Class Action Settlement" for a further discussion of same)	916,166	-
Accrued interest on investments and receivables, payments due within 12 months	158,903	310,048
Other, net of allowances for doubtful accounts of approximately \$95,000 and \$58,000 at June 30, 2008 and 2007, respectively, principally related to the sale of cemetery lots and crypts, payments generally due in monthly installments over periods up to 5 years	<u>93,399</u>	<u>141,148</u>
	<u>\$ 1,720,892</u>	<u>\$ 1,064,404</u>

NOTES TO FINANCIAL STATEMENTS  
 CHANCERY OF THE DIOCESE OF CHARLESTON

CASH RESTRICTED FOR PROPERTY PROJECTS AND STATEMENT OF CASH FLOWS

In 2008, the Chancery received contributions totaling \$2,245,995 restricted for property projects, including \$2,226,595 for the Diocesan Retreat and Conference Center (which is part of the Our Heritage Our Hope Campaign). The restricted contributions are deemed to be financing activities in the accompanying 2008 statement of cash flows since they are donor-restricted for a long-term purpose.

BONDS DEBT SERVICE FUND

In conjunction with the issuance of certain bonds (see the note, "Bonds Payable", for a further discussion of same), a bonds debt retirement fund, consisting of an interest reserve account and a redemption account, was established in the custody of the bonds' trustee. Monthly interest payments are made to the interest reserve account by the Chancery and disbursed by the trustee to the bondholders on the first day of the month. Additionally, monthly principal payments are made to the redemption account by the Chancery to fund the bonds to be redeemed annually by the trustee on September 1. The bond debt service balances at June 30, 2008 and 2007 consist of the monthly principal redemption payments made by the Chancery, plus the accumulated interest earned on same.

PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	<u>2008</u>	<u>2007</u>
Land	\$ 9,277,275	\$ 9,277,275
Buildings and equipment	10,643,719	10,640,490
	<u>\$ 19,920,994</u>	<u>\$ 19,917,765</u>

As more fully discussed in the following note, "Notes Payable", the Chancery purchased certain property in Horry County for approximately \$2,004,000 subsequent to June 30, 2008.

NOTES PAYABLE

Notes payable consist of the following:

	<u>2008</u>	<u>2007</u>
Note 1	\$ 884,095	\$ 934,002
Note 2	791,147	840,408
Note 3	1,782,468	1,982,982
Note 4	875,849	930,849
Note 5	6,658,676	-
	<u>\$ 10,992,235</u>	<u>\$ 4,688,241</u>

Note 1 is unsecured and is payable in monthly installments of \$7,633, including interest at 4.5%, with a final payment of all unpaid principal and interest due in February 2011.

Note 2 is unsecured and is payable in monthly installments of \$7,397, including interest at 4.75%, with a final payment of all unpaid principal and interest due in January 2012.

Note 3 is unsecured and is payable in monthly installments of \$25,045, including interest at 5.2%, with a final payment of all unpaid principal and interest due in July 2015.

Note 4 is unsecured and is payable in monthly principal installments of \$4,583, plus interest at the LIBOR daily floating rate plus .85%, with a final payment of all unpaid principal and interest due in October 2012.

NOTES TO FINANCIAL STATEMENTS  
CHANCERY OF THE DIOCESE OF CHARLESTON

NOTES PAYABLE-Continued

Note 5 is collateralized by certain pooled investment accounts having fair values totaling approximately \$12,926,000 at June 30, 2008 (see the note, "Investments", for a further discussion of same), interest only is payable monthly at the Libor daily floating rate plus .5%, loan principal and accumulated interest was originally due in full in July 2008. Subsequent to June 30, 2008, the note was renewed under principally the same terms with the loan principal and accumulated interest due in full in July 2009. However, the required minimum collateral value was reduced to \$7,750,000.

In conjunction with the funding of the class action settlement pool of \$7,000,000 (see the note, "Class Action Settlement" for a further discussion of same), the Chancery obtained a letter of credit and a line of credit with Bank of America for \$7,000,000 each. In July 2007, Note 5 was funded under the line of credit. The letter of credit and line of credit both expired in July 2008 with no additional funding being provided.

The scheduled future maturities of the notes payable at June 30, 2008 are as follows: 2009 - \$370,485; 2010 - \$7,045,596; 2011 - \$1,123,853; 2012 - \$930,711; 2013 - \$916,895 and thereafter - \$604,695.

Subsequent to June 30, 2008, the Chancery purchased certain property in Horry County, consisting of approximately 26 acres of land and certain buildings and improvements thereon, for approximately \$2,004,000. The purchase was principally funded by a note payable for \$2,000,000 with the following terms: monthly principal payments of \$11,111, plus interest at the bank's prime rate, beginning in December 2008, with a final payment of all unpaid principal and interest due in November 2011.

BONDS PAYABLE

On September 1, 1998, tax-exempt bonds in the aggregate principal amount of \$12,500,000 were issued on behalf of the Diocese through the South Carolina Jobs - Economic Development Authority to finance the acquisition, construction, equipping and furnishing of certain educational facilities in the Diocese. As more fully discussed in the note, "Organization", the Diocese consists of various distinct operating entities, including the Chancery. The bonds payable are included in the financial statements of the Chancery, as part of its cooperative investment and lending program. However, the construction projects funded by the bonds involve certain other diocesan educational entities. As such, these construction projects are included as property and equipment on these other diocesan entities' records. Accordingly, the Chancery's financial statements reflect assets, consisting of notes receivable from other diocesan entities, relative to the use of the bond proceeds.

The bonds bear interest at the "weekly rate", as defined in the bond document. Under the weekly rate, interest is payable monthly, in arrears, on the first day of each month. Beginning in October 2001, monthly principal payments to the bond fund held by the trustee were also required. Principal payments to the bondholders are payable on September 1 of each of the following years: 2009 through 2017 - \$735,000; 2018 - \$740,000.

In conjunction with the issuance of the bonds, the Diocese entered into a letter of credit agreement with Bank of America to secure the principal balance of the outstanding bonds plus an interest component thereof. The letter of credit, as amended in August 2003, expired on September 15, 2008. In July 2008, the letter of credit was amended to extend the stated expiration date to September 14, 2010.

The bonds, including the various related agreements, provide for certain covenants including (1) the maintenance of unencumbered liquid assets of 25% of the aggregate borrowing availability; and (2) certain limitations on encumbrances of diocesan property, transfers of diocesan property outside the ordinary course of business, and additional indebtedness.

INTEREST RATE SWAP AGREEMENT

In February 2001, the Diocese entered into an interest rate swap agreement with Bank of America having a stated fixed interest rate of 3.96% on the outstanding bonds payable for the period from February 15, 2001 through September 1, 2018. Interest expense on the bonds under the bond document and interest rate swap agreement is included as part of the deposit and loan interest expense in the accompanying Statements of Changes in Unrestricted Net Assets.

NOTES TO FINANCIAL STATEMENTS  
CHANCERY OF THE DIOCESE OF CHARLESTON

INTEREST RATE SWAP AGREEMENT-Continued

The Chancery uses the interest rate swap agreement to manage its exposure to interest rate changes with respect to its bonds payable. It is not intended for speculative purposes. The interest rate swap is a derivative instrument. Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended, requires that all derivative instruments be reported at fair value. At June 30, 2008 and 2007, the fair values of the swap agreement were (\$425,577) and (\$135,194), respectively, and are reflected in the accompanying Statements of Financial Position as liabilities. The changes in the fair value of the swap agreement for 2008 and 2007 are reflected in the Statements of Activities and Changes in Unrestricted Net Assets as decreases in unrestricted net assets of \$290,383 and \$18,202, respectively, and identified as "fair value adjustment on interest rate swap agreement".

This interest rate swap agreement requires the Diocese and, effectively, the Chancery to maintain unrestricted cash and equivalents, government backed securities, and equities in an amount not less than \$1,000,000.

INVESTMENT EXPENSES

Expenses relating to investment income, including custodial fees and investment advisory fees, approximated \$128,400 and \$117,200 for 2008 and 2007, respectively, and have been netted against investment income in the accompanying Statements of Activities and Changes in Unrestricted Net Assets.

RETIREMENT PLAN

The Diocese has a contributory retirement plan covering substantially all lay Diocesan employees, including Chancery employees. After one year of service, the employer contributes 5% of the employee's monthly pay for a participating employee contributing a minimum of 3% of monthly pay. The contributions are limited to the maximum annual amounts allowed by the Internal Revenue Service. In 2008 and 2007, the Chancery made contributions to the lay retirement plan for its employees approximating \$81,000 and \$74,500, respectively.

In addition, the Diocese maintains the Diocesan Priests' Retirement Plan (the "Plan") for the benefit of all eligible priests, as defined in the Plan provisions, working in the Diocese. The Plan is a defined benefit plan providing benefits to eligible participants in accordance with the Plan provisions. Effective January 1, 2007, the Plan was amended to (a) conform to Section 401(a) of the Internal Revenue Code; (b) allow foreign priests to be eligible to participate in the Plan; (c) reduce the vesting period; (d) reduce the required number of years for normal retirement benefits; and (e) provide for the proration of normal retirement benefits for years less than 20. The funding of the Plan is provided by the respective Diocesan entities (Chancery, parishes and missions, and other Diocesan entities) which are served by the eligible priests of the Diocese. For 2008 and 2007, the funding established for the Plan was \$500 per month for each active eligible priest. In 2008 and 2007, the Chancery made contributions to the Plan approximating \$74,500 and \$46,000, respectively, for the eligible priests assigned to the Chancery. The Chancery recognizes pension expense based upon the funding established for the Plan.

Statements of Financial Standards (SFAS) No. 132, as amended by SFAS 158, require certain reporting and disclosures with respect to defined benefit plans such as the Diocesan Priests' Retirement Plan. The Plan involves the Diocese as a whole which consists of various distinct operating entities, including the Chancery. It is not practical to separate such reporting and disclosures for the Chancery or the other Diocesan operating entities participating in the Plan. For purposes of the Chancery's financial statements, the Plan is considered a multiemployer pension plan and the reporting and disclosures limited to the information provided in the preceding paragraph. The Diocese did obtain an actuarial valuation of the Plan as of June 30, 2008 which reported that the present value of the accumulated plan benefits exceeded the Plan's assets by approximately \$1,085,000 as of that date. The underfunding of the Plan as of June 30, 2008 was significantly affected by the decline in the market value of the Plan's investments as of that date. Based on the current funding of \$500 per month for each eligible priest, contributions to the Plan for the year ending June 30, 2009, are estimated at approximately \$500,000 and exceed the estimated benefit payments of approximately \$406,000 for this fiscal year. Funding of \$1,000,000 to the Plan is one of the case elements of the Our Heritage Our Hope Campaign and the Plan anticipates receiving such funding within the next two years. Effectively, the Chancery is a guarantor of the Plan's obligations.

NOTES TO FINANCIAL STATEMENTS  
 CHANCERY OF THE DIOCESE OF CHARLESTON

STATEMENTS OF CASH FLOWS SUPPLEMENT

Interest expense paid during 2008 and 2007 totaled \$1,168,810 and \$1,043,596, respectively.

The following non-cash investing activity occurred during 2008 and 2007:

- a. Donated property having an estimated fair value of \$84,000 was received in 2007.

LIMITATIONS ON UNRESTRICTED NET ASSETS

The Administrator has chosen to place the following limitations on unrestricted net assets:

	<u>2008</u>	<u>2007</u>
Designated for a reserve to fund the deductible/self insured retention provided in the property insurance program for the Diocese	\$ 1,580,745	\$ 1,552,610
Designated for the perpetual care of the St. Lawrence and Holy Cross cemeteries	3,037,304	3,283,978
Designated for long-term investments and certain endowments	<u>10,752,428</u>	<u>12,208,239</u>
	<u>\$ 15,370,477</u>	<u>\$ 17,044,827</u>

RESTRICTIONS ON NET ASSETS

Temporarily restricted net assets consist of the following:

	<u>2008</u>	<u>2007</u>
Net assets, subject to time restrictions which expire in the subsequent fiscal year, available to support the subsequent year's activities	\$ 1,560,933	\$ 1,303,678
Net assets, subject to purpose restrictions, available to support the subsequent year's activities to the extent the respective purposes are accomplished	<u>7,402,738</u>	<u>6,236,997</u>
	<u>\$ 8,963,671</u>	<u>\$ 7,540,675</u>

The temporarily restricted net assets subject to purpose restrictions include \$2,245,995 for long term purposes, principally the Diocesan Conference and Retreat Center.

Permanently restricted net assets consist of endowment fund assets to be held indefinitely. The income from the assets is subject to purpose restrictions and can be used to support the Chancery's activities to the extent the respective purposes are accomplished. In 2008, the personal representative for an estate which had bequeathed \$647,769 to the Diocese prior to 2007 clarified that such funds were permanently restricted. These assets were originally classified as temporarily restricted. Accordingly, such assets are reported as net assets transferred to a permanently restricted classification in the accompanying 2008 statement of activities.

RELATED PARTY TRANSACTIONS

The Chancery has entered into an agreement to lease certain land in Mt. Pleasant, South Carolina to East Cooper Community Outreach (ECCO), a non-profit organization associated with a Diocesan parish. The land lease is for a period of 50 years, ending in 2052, at \$1 per year, with ECCO being responsible for all costs relative to the property and the operation of an ecumenical outreach center thereon.

NOTES TO FINANCIAL STATEMENTS  
CHANCERY OF THE DIOCESE OF CHARLESTON

CONCENTRATION OF CREDIT RISK

The Chancery maintains cash balances with various financial institutions that exceed the federally insured limit of \$100,000 (which was changed to \$250,000 in October 2008) per financial institution. Statement of Financial Accounting Standards No. 105 identifies such as a concentration of credit risk requiring disclosure. The Chancery's management believes such risk is reduced by maintaining its deposits in high quality financial institutions. At June 30, 2008 and 2007, the Chancery's uninsured cash balances, including those cash accounts classified as investments, totaled approximately \$26,300,000 and \$20,300,000, respectively.

CLASS ACTION SETTLEMENT

In June 2006, the Diocese entered into an agreement to pay four claimants \$460,000 in settlement of allegations of sexual abuse by certain church personnel of the Diocese and to pursue the formation of a "class" of potential claimants in order to reach out to a broad group (those born before August 30, 1980) of victims of sexual abuse by church personnel of the Diocese. The final settlement agreement was entered into on January 12, 2007 and on July 30, 2007, the proposed class action settlement of \$12,000,000 ("class settlement") was approved by a circuit court. The class settlement provided for the following: (1) two pools of funds (\$5,000,000 and \$7,000,000) were to be established and funded by the Diocese; (2) awards ranging from \$10,000 to \$200,000 depending on the type of abuse were established; (3) claimants had until December 6, 2007 to elect to participate in the class action or to opt out; and (4) a neutral arbitrator was appointed to review and validate each claim.

On August 31, 2007, the court entered an order approving a supplemental settlement agreement with eleven victims whose objections were overruled by the original court order. Under this court order ("supplemental settlement"), these eleven victims are to receive a total of \$1,375,000 which was to be paid (1) from the surplus funds, if any, of the class settlement total of \$12,000,000; or (2) if sufficient funds were not available from surplus class settlement funds, then the Diocese was obligated to pay the supplemental settlement amount of \$1,375,000. Additionally, class counsel for the class settlement was required to pay \$100,000 of the supplemental settlement.

During the year ended June 30, 2007, the Chancery remitted \$460,000 to class counsel. The Chancery's reasonable estimate of the remaining liability at June 30, 2007 ranged from \$7,016,000 to \$10,949,000; and its best estimate within this range was \$8,600,000. Accordingly, \$8,600,000 was accrued at June 30, 2007. During 2008, (1) claims and non-claimant costs totaling \$9,850,100 relative to the class settlement were approved and paid from the two pools of funds and the unexpended balance of the funds was returned to the Chancery; (2) the class counsel for the class settlement put \$100,000 on deposit with the Chancery's attorney to be held in escrow for the supplemental settlement; and (3) insurance claims totaling \$890,000 were filed by the Chancery, recorded as part of other receivables at June 30, 2008, and collected by the Chancery subsequent to year end. At June 30, 2008, the supplemental settlement of \$1,375,000 was unpaid and is accrued as part of the Chancery's accounts payable and accrued expenses. The class settlement payments in 2008 and the unpaid supplemental settlement, net of the payment received in 2008 of \$100,000 from the class counsel for the class settlement and the insurance claim settlements of \$890,000, exceeded the class action liability accrued at June 30, 2007 by \$1,635,100 and is reported as the class action settlement expense in the 2008 statement of changes in unrestricted net assets.

In March 2008, prior to the court ordered settlement of \$1,375,000 being paid by the Chancery, the claimants' attorney for the supplemental settlement filed a civil complaint against the Diocese seeking additional damages of costs and interest in addition to special damages for a twelfth claimant not a party to the supplemental settlement. The Diocese has filed certain motions in response to these new legal actions and, upon advice from its counsel, payment of the court ordered settlement of \$1,375,000 was suspended until these new legal actions are addressed by the courts. Counsel for the Diocese has advised: (1) that the new legal actions are without merit; (2) that the Diocese intends to contest them vigorously; and (3) that the ultimate outcome of these new legal actions cannot presently be determined. Accordingly, the liability accrued by the Chancery at June 30, 2008 is the August 2007 court ordered settlement amount of \$1,375,000 and no provision for any additional liability that may result from these new legal actions has been made in the accompanying financial statements.

In December 2008, a complaint and petition on behalf of a claimant, who was part of the class settlement, was filed with the South Carolina State Supreme Court alleging that certain persons were negligent in the handling of the class action lawsuit. In conjunction with this complaint and petition, the Diocese was named as a defendant and was alleged to have colluded in obtaining court approval of the class action settlement. Counsel for the Diocese has advised that there are significant uncertainties with respect to this legal action and that the ultimate outcome cannot presently be determined. Accordingly, no provision for any liability that may result from this matter has been made in the accompanying financial statements.

NOTES TO FINANCIAL STATEMENTS  
CHANCERY OF THE DIOCESE OF CHARLESTON

CONTINGENCIES

Various legal and other actions, other than those identified in the preceding note, "Class Action Settlement", are pending against the Diocese and, effectively, the Chancery which involve claims for damages, as well as other types of relief, relative to the actions of certain personnel of the Diocese of Charleston. Counsel for the Diocese has advised that there are significant uncertainties with respect to these legal and other actions; and that the ultimate outcome from such legal and other actions pending against the Diocese cannot presently be determined. Accordingly, no provision for any liability that may result from these matters has been made in the accompanying financial statements.

The Diocese had a line of credit in the amount of \$15,000,000 with Bank of America with an availability period from February 26, 2007 to June 28, 2008 for the construction of new facilities and for additions or renovations to existing facilities in the Diocese. Any loans funded under the line of credit were to be unsecured and have the following terms: interest only payable directly by the Chancery to Bank of America on a monthly basis at the BBA LIBOR Daily Floating Rate, plus .73%; the principal balances of any loans funded were due in full on June 28, 2008. Additionally, the line of credit agreement included a covenant which required the Diocese, and, effectively, the Chancery to maintain unrestricted cash and equivalents, government backed securities, and equities at a minimum of fifty percent of "Aggregate Borrowing Availability", as defined in the loan agreement. There were no loans funded under this line of credit and such expired on June 28, 2008.

Bank of America has made loans to the Diocese under certain line of credit agreements which have been used by Diocesan parishes and missions in connection with the construction of new facilities and for additions or renovations to existing facilities. The monthly debt service payments on these notes are made by the respective parishes and missions directly to Bank of America. The balances on these notes totaled \$18,192,510 and \$21,591,562 at June 30, 2008 and 2007, respectively. Such debt is not reflected in the accompanying financial statements of the Chancery. Effectively, the Chancery is a guarantor of such debt.

As more fully discussed in the note, "Retirement Plan", the Diocese obtained an actuarial valuation of the Diocesan Priests' Retirement Plan (the "Plan") which reported that the Plan's liabilities at June 30, 2008 exceeded its assets by approximately \$1,085,000. Effectively, the Chancery is a guarantor of the Plan's obligations.

The Diocese obtains blanket property and liability insurance coverage for the Chancery and certain other Diocesan entities. The Chancery pays the premiums and bills the Diocesan entities for their portion of the premiums. Under the Diocese's property and liability insurance coverage, the self insured retention of the Chancery has an annual aggregate ("stop loss") of \$750,000.

In connection with a school building project for a parish in Beaufort County, the County required the following letters of credit: (1) \$134,168 for landscape survival covering a two year period ending November 2009; and (2) \$158,650 for a frontage road covering a three year period ending November 2010. The Chancery, on behalf of the parish, obtained these letters of credit from Bank of America and purchased certificates of deposits with Bank of America, originally in the same amounts as the letters of credit, which collateralize same.



NOTES TO FINANCIAL STATEMENTS  
 CHANCERY OF THE DIOCESE OF CHARLESTON

OUR HERITAGE, OUR HOPE CAMPAIGN

The Diocese of Charleston conducted Our Heritage, Our Hope, a diocesan capital fund raising campaign (“Campaign”), during the period from September 2005 through December 2006. The Campaign had a goal to raise \$32,000,000 for the benefit of numerous Diocesan entities, including approximately 33% for the benefit of the Chancery. In conjunction with the Campaign, intentions to give (“faith promises”) were obtained. However, such intentions to give are not intended to be legally binding. As such they do not represent promises to give and are not recognized as revenues when obtained. In conjunction with the Campaign, the Chancery agreed to absorb all of the fund raising costs from its share of the Campaign contributions. The following is a summary of the cumulative cash activities of the Campaign through June 30, 2008:

		<u>Through June 30, 2008</u>
Contributions received by the development office of the Chancery		<u>\$ 14,312,589</u>
Allocation of contributions received		
Temporarily restricted contributions to the Chancery for:		
Fund raising costs	\$ 2,413,435	
Bishop's Stewardship Appeal for 2006	1,866,422	
Diocesan retreat and conference center	2,226,595	
Other Campaign case elements	<u>29,754</u>	\$ 6,536,206
Contributions for non-Chancery Campaign case elements:		
Local parish support:		
Disbursed to the parishes	3,585,445	
Liability at June 30, 2008 to be subsequently disbursed	<u>621,035</u>	4,206,480
Cathedral restoration:		
Disbursed to the Cathedral parish	120,750	
Liability at June 30, 2008 to be subsequently disbursed	<u>3,379,250</u>	3,500,000
Other non-Chancery Campaign case elements		<u>69,903</u>
Total		<u>\$ 14,312,589</u>