

THE EPISCOPAL CHURCH IN THE
DIOCESE OF CALIFORNIA

DECEMBER 31, 2011

INDEPENDENT AUDITORS' REPORT

FINANCIAL STATEMENTS,

AND

SUPPLEMENTAL INFORMATION

The Episcopal Church in the Diocese of California

Independent Auditors' Report and Financial Statements

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Independent Auditors' Report

THE BOARD OF DIRECTORS
THE EPISCOPAL CHURCH IN THE
DIOCESE OF CALIFORNIA
San Francisco, California

We have audited the accompanying statement of financial position of **THE EPISCOPAL CHURCH IN THE DIOCESE OF CALIFORNIA (the Diocese)** as of December 31, 2011, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the Diocese's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year's summarized comparative information has been derived from the Diocese's 2010 financial statements and, in our report dated June 21, 2011, we expressed an unqualified opinion on these financial 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 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Episcopal Church in the Diocese of California as of December 31, 2011, 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.

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying changes in fund asset balance information on page 20 is presented for purposes of additional analysis and is not a required part of the Diocese's basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

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San Francisco, California
June 26, 2012

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The Episcopal Church in the Diocese of California

Statement of Financial Position

December 31, (with comparative totals for 2010)

	2011					2010 Total
	Operating	Custodial and Unexpended Income	Endowment and Trust	Deferred Gifts	Total All Funds	
Assets:						
Cash and cash equivalents	\$ 3,554,043		\$ 18,378		\$ 3,572,421	\$ 1,859,768
Receivables, net	1,782,913				1,782,913	1,764,200
Investments	174,476		15,189,222	\$ 17,111,674	32,475,372	36,018,552
Notes receivable	2,627,445				2,627,445	3,107,795
Notes receivable held for investment, net		\$ 2,300			2,300	120,424
Equity interests in real property	43,949	100,000	1,087,500		1,231,449	1,231,449
Property and equipment, net	4,198,086				4,198,086	4,239,334
Due to/from other funds	(2,487,053)	893,602	1,593,451			
Total assets	\$ 9,893,859	\$ 995,902	\$ 17,888,551	\$ 17,111,674	\$ 45,889,986	\$ 48,341,522
Liabilities and Net Assets						
Liabilities:						
Accounts payable and accrued expenses	\$ 824,958				\$ 824,958	\$ 842,604
Accounts payable, related parties			\$ 340,519		340,519	203,237
Deferred revenue	12,966				12,966	163,936
Line of credit	2,718,945				2,718,945	3,107,795
Funds held in trusts for beneficiaries				\$ 14,203,237	14,203,237	15,132,564
Total liabilities	3,556,869		340,519	14,203,237	18,100,625	19,450,136
Net Assets:						
Unrestricted	5,866,311		(1,139,855)		4,726,456	4,021,622
Unrestricted-board designated	470,679				470,679	906,310
Total unrestricted	6,336,990		(1,139,855)		5,197,135	4,927,932
Temporarily restricted		\$ 995,902	9,934,247	587,004	11,517,153	13,126,071
Permanently restricted			8,753,640	2,321,433	11,075,073	10,837,383
Total net assets	6,336,990	995,902	17,548,032	2,908,437	27,789,361	28,891,386
Total liabilities and net assets	\$ 9,893,859	\$ 995,902	\$ 17,888,551	\$ 17,111,674	\$ 45,889,986	\$ 48,341,522

The accompanying notes are an integral part of this statement.

The Episcopal Church in the Diocese of California

Statement of Activities

Years Ended December 31, 2011 (with comparative totals for 2010)

	2011					2010 Total
	Operating	Custodial and Unexpended Income	Endowment and Trust	Deferred Gifts	Total All Funds	
Support and Revenue:						
Parish and mission assessments	\$ 3,323,315				\$ 3,323,315	\$ 3,247,823
Gifts, grants and other	458,095	\$ 826,153	\$ 350,211		1,634,459	2,533,870
Change in value				\$ (203,943)	(203,943)	304,133
Investment income, net	(22,511)		(1,025,182)		(1,047,693)	1,511,821
Total support and revenue	3,758,899	826,153	(674,971)	(203,943)	3,706,138	7,597,647
Expenses:						
Episcopate	518,984				518,984	602,546
Finance	469,487				469,487	450,368
Administration	848,079				848,079	850,719
Planned giving	176,308				176,308	177,282
Congregational development	305,336				305,336	383,633
Ministry development	177,699				177,699	145,094
Youth & young adult	78,847				78,847	123,412
Multicultural ministry	319,861				319,861	402,229
Communications	211,106				211,106	245,378
Support services-outside Diocese	746,741				746,741	770,402
Other ministry	139,911				139,911	148,373
Justice, peace, and integrity	25,489				25,489	24,281
Payments to beneficiaries and other custodial fund disbursements	790,315				790,315	660,584
Total expenses	4,808,163	-	-	-	4,808,163	4,984,301
Changes in Net Assets Before						
Transfers & Reclasses	(1,049,264)	826,153	(674,971)	(203,943)	(1,102,025)	2,613,346
Interfund transfer		124,860	(124,860)			
Releases from Restrictions	1,884,581	(424,413)	(1,460,168)			
Change in Net Assets	835,317	526,600	(2,259,999)	(203,943)	(1,102,025)	2,613,346
Net Assets, beginning of year	5,501,673	469,302	19,808,031	3,112,380	28,891,386	26,278,040
Net Assets, end of year	\$ 6,336,990	\$ 995,902	\$ 17,548,032	\$ 2,908,437	\$ 27,789,361	\$ 28,891,386
Fund Balances by Classification						
Net Assets, beginning of year						
Unrestricted Net Assets	\$ 5,501,673		\$ (573,741)		\$ 4,927,932	\$ 3,343,226
Temporarily Restricted Net Assets		\$ 469,302	11,978,281	\$ 678,487	13,126,070	12,620,083
Permanently Restricted Net Assets			8,403,491	2,433,893	10,837,384	10,314,731
Net Assets, beginning of year	\$ 5,501,673	\$ 469,302	\$ 19,808,031	\$ 3,112,380	\$ 28,891,386	\$ 26,278,040
Changes in Net Assets:						
Unrestricted Net Assets	\$ 835,317		\$ (566,114)		\$ 269,203	\$ 1,584,706
Temporarily Restricted Net Assets		\$ 526,600	(2,044,034)	\$ (91,483)	(1,608,917)	505,987
Permanently Restricted Net Assets			350,149	(112,460)	237,689	522,653
Changes in Net Assets	\$ 835,317	\$ 526,600	\$ (2,259,999)	\$ (203,943)	\$ (1,102,025)	2,613,346
Net Assets, end of year						
Unrestricted Net Assets	6,336,990		(1,139,855)		\$ 5,197,135	\$ 4,927,932
Temporarily Restricted Net Assets		995,902	9,934,247	587,004	11,517,153	13,126,070
Permanently Restricted Net Assets			8,753,640	2,321,433	11,075,073	10,837,384
Net Assets, end of year	\$ 6,336,990	\$ 995,902	\$ 17,548,032	\$ 2,908,437	\$ 27,789,361	\$ 28,891,386

The accompanying notes are an integral part of this statement.

The Episcopal Church in the Diocese of California

Statement of Cash Flows

<i>Years Ended December 31, (with comparative totals for 2010)</i>	2011	2010
Cash Flows from Operating Activities:		
Changes in net assets	\$ (1,102,025)	\$ 2,613,346
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	86,707	77,660
Net realized and unrealized loss (gain) on investments	1,462,567	(1,080,849)
Donation of stock		(219,761)
Change in charitable remainder unitrusts	517,782	(576,432)
(Increase) decrease in operating assets:		
Receivables	(18,713)	46,163
Increase (decrease) in operating liabilities		
Accounts payable and accrued expenses	(17,646)	30,420
Accounts payable, related party	137,282	143,536
Deferred revenue	(150,970)	(3,533)
Net cash provided by operating activities	914,984	1,030,550
Cash Flows from Investing Activities:		
Purchases of investments	(21,424,030)	(6,334,432)
Proceeds from sale of investments	22,057,534	4,937,951
Principal payments received on notes receivable held for investments	118,124	21,438
Purchases of property and equipment	(45,459)	(5,219)
Sale of equity interest		249,661
Borrowing from Line of Credit	91,500	
Net cash provided (used) by investing activities	797,669	(1,130,601)
Net Increase (Decrease) in Cash and Cash Equivalents	1,712,653	(100,051)
Cash and Cash Equivalents, beginning of year	1,859,768	1,959,819
Cash and Cash Equivalents, end of year	\$ 3,572,421	\$ 1,859,768

The accompanying notes are an integral part of this statement.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Note 1 - Summary of Significant Accounting Policies:

a. Organization

The Episcopal Church in the Diocese of California (the Diocese) is a nonprofit entity that administratively supports Episcopal parishes and other ancillary institutions throughout the San Francisco Bay Area in the State of California. The Diocese is governed by the Executive Council which is the legal board of directors of the Diocesan Corporation.

b. Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting and, accordingly, reflect all significant receivables, payables, and other liabilities, including deferred revenue. The principles of “fund accounting” are utilized in order to provide a more detailed accountability for the funds entrusted to the Diocese.

c. Basis of Presentation

Financial statement presentation follows the recommendations of the Accounting Standards Codification (ASC) 958, *Not-for-Profit Entities*. Under ASC 958, the Diocese is required to report information regarding its financial position and activities according to three classes of net assets:

Unrestricted Net Assets. The portion of net assets that is neither temporarily restricted nor permanently restricted by donor-imposed stipulations.

Temporarily Restricted Net Assets. The portion of net assets whose use by the organization is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the Diocese.

Permanently Restricted Net Assets. The portion of net assets whose use by the organization is limited by donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of the Diocese.

d. Cash and Cash Equivalents

For purposes of the Statement of Cash Flows, cash and cash equivalents include time deposits and all highly liquid debt instruments with original maturities of three months or less.

e. Receivables

Receivables consist of amounts due to the Diocese from parishes that are within the Diocese of California and represent assessments, reimbursable expenses, and other receivables. The Diocese records bad debts using the allowance method.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

f. Fair Value Measurements

The Diocese classifies its financial assets and liabilities measured at fair value on a recurring basis based on a fair value hierarchy with three levels of inputs. Level 1 values are based on unadjusted quoted prices in active markets for identical securities. Level 2 values are based on significant observable market inputs, such as quoted prices for similar securities and quoted prices in inactive markets. Level 3 values are based on significant unobservable inputs that reflect the Diocese's determination of assumptions that market participants might reasonably use in valuing the securities. The valuation levels are not necessarily an indication of the risk or liquidity associated with the assets and liabilities measured at fair value.

The fair value of investment securities is the market value based on quoted market prices, when available, or market prices provided by recognized broker dealers. If listed prices or quotes are not available, fair value is based upon externally developed models that use unobservable inputs due to limited market activity of the instrument.

g. Notes Receivable Held for Investment

Notes receivable held for investment consists of notes to several churches. The notes bear interest at rates ranging from 0% - 4% and are due through 2016. The notes are secured by property or unsecured and are recorded net of an allowance related to interest accruals.

h. Equity Interest in Real Property

Equity interest in real property consists of property owned by the Diocese, and amounts funded by the Diocese for the purchase of property by related parties. The Diocese has an equity interest in the property for the amount of the purchase price funded by the Diocese. This interest is recorded at cost.

i. Property and Equipment

Purchased property and equipment is recorded at cost. Donated property is valued at fair value at time of donation. Depreciation is provided on a straight-line basis over the estimated useful lives (five to thirty years) of the related assets. Maintenance and repairs are charged to expense as incurred. Significant betterments and renewals are capitalized. The Diocese has elected not to depreciate its real property and has determined that the effect on the financial statements is not material as of December 31, 2011.

j. Deferred Revenue

Deferred revenue consists of assessments, payroll, and benefits received from parishes in advance of the period to which they relate.

k. Recognition of Support and Revenue

Current year parish and mission assessments have been prepared on the accrual basis of accounting.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Gifts and grants are recognized when the donor makes an unconditional promise to give to the Diocese. Donor-restricted gifts and grants are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets.

Investment income is recognized as revenue when earned. Investment income earned on permanently restricted net assets is recorded as an increase or decrease in temporarily restricted net assets unless specifically restricted as permanent by the donor.

l. Income Taxes

The Diocese is a tax exempt organization under the provision of the Internal Revenue Code, Section 501(c)(3), and the related state provisions. Accordingly, no provision for income taxes has been reflected in these financial statements.

The Diocese follows the guidelines of the Financial Accounting Standards Board (FASB) ASC Topic 740 for accounting for uncertainty in income taxes. As of December 31, 2011, management evaluated the Diocese's tax positions and concluded that the Diocese had maintained its tax exempt status and has taken no uncertain tax positions that require adjustment to the financial statements. Therefore, no provision or liability for income taxes has been included in the financial statements.

m. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

n. Subsequent Events

The Diocese has reviewed the changes in net assets for the period of time from December 31, 2011 through June 26, 2012, the date the financial statements are available to be issued, and have determined that no adjustments are necessary to the amounts reported in the accompanying financial statements nor subsequent events have occurred, the nature of which would require disclosure, except as disclosed in Note 9.

o. Comparative Financial Information

The financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with GAAP. Accordingly, such information should be read in conjunction with the Diocese's financial statements for the year ended December 31, 2010, from which the summarized information was derived.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Note 2 - Description of Funds:

a. Operating Fund

This fund is used to account for all expenditures related to unrestricted support and revenue. The Board of Directors of the Diocese has set aside certain donor unrestricted funds for certain designated uses. These funds are included in the operating fund as board designated.

b. Custodial and Unexpended Income Fund

This fund is used to account for gifts and grants designated for specific projects or programs by donors. The fund balance is classified as temporarily restricted on the statement of financial position.

c. Endowment and Trust Fund

This fund is used to account for assets contributed by donors that are subject to various restrictions, both temporary and permanent. The Diocese is responsible to assure that distributions be made in accordance with the provisions of each trust. When the market value of permanently restricted funds fall below the historical value, the deficiency is reflected as unrestricted net assets. At the end of 2011, this deficiency increased to \$1,139,855. The permanently restricted net assets represent the historic value of additions to the endowment, and the temporarily restricted net assets represent appreciation of the endowment and the trust fund balances.

d. Deferred Gifts Fund

This fund is used to account for funds held in trust and administered by the Diocese, the income of which is payable to individual beneficiaries. Income earned but not paid to beneficiaries is treated as a liability, which is included with "Funds Held in Trust for Beneficiaries". Upon the expiration of the income beneficiaries' interest, the principal will be distributed in accordance with the conditions prescribed by the Charitable Remainder Unitrust agreements. Any principal that will ultimately be distributed to third party beneficiaries has been recorded as a liability, "Funds Held in Trust for Beneficiaries." The remainder is distributable to the Diocese and is stated at the estimated present value, which is calculated based on the actuarial life expectancy of the donor or designees. The discount rate used, ranging between 5% and 6.5%, approximates the 30 year U.S. Treasury Bond rate in the year of origination. The fund balances are a combination of permanently restricted net assets and temporarily restricted net assets on the statement of financial position.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Note 3 - Receivables:

Receivables consist of the following at December 31, 2011 and 2010:

	2011	2010
Assessments	\$ 151,024	\$ 267,459
Reimbursable expenses from related entities, net of allowance	1,195,763	1,187,786
Other receivables	436,126	308,955
	<hr/>	<hr/>
	\$ 1,782,913	\$ 1,764,200

Note 4 - Investments:

The fair value of investments at December 31, 2011 and 2010 is as follows:

	2011	2010
Corporate stocks		\$ 6,147,090
Mutual funds	\$ 15,363,698	11,312,679
Charitable trusts	17,111,674	18,558,783
	<hr/>	<hr/>
	\$ 32,475,372	\$ 36,018,552

Investment income for the years ended December 31, 2011 and 2010 consists of the following:

Interest and dividends, net of management fees of \$141,355 and \$57,410, respectively	\$ 402,155	\$ 436,856
Realized gains and losses	(360,532)	366,858
Unrealized gains and losses	(1,089,316)	708,107
	<hr/>	<hr/>
	\$ (1,047,693)	\$ 1,511,821

Investment income is included in:

Unrestricted net assets	\$ (588,623)	\$ 30,156
Temporarily restricted net assets	(459,070)	1,481,665
	<hr/>	<hr/>
	\$ (1,047,693)	\$ 1,511,821

The Episcopal Church in the Diocese of California

Notes to Financial Statements

The table below presents the balances of assets measured at fair value at December 31, 2011 on a recurring basis:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>
Investments:			
Mutual Funds:			
Intermediate Duration			
Institutional	\$ 15,189,222	\$ 15,189,222	
Emerging Markets Fund	174,476	174,476	
Charitable Trusts:			
Cash & Equivalents	409,948		\$ 409,948
Domestic REIT	1,422,811		1,422,811
Emerging Markets Stocks	231,363		231,363
High Quality Bond Funds	2,353,263		2,353,263
High Quality Bonds	217,372		217,372
High Yield Bond Funds	374,166		374,166
Int'l Bond Funds	838,738		838,738
Int'l REIT	750,432		750,432
Int'l Stocks	2,042,096		2,042,096
Int'l Small Co. Stocks	324,259		324,259
Investm't Grade Bond			
Funds	1,798,617		1,798,617
Large Co. Stocks	5,127,340		5,127,340
Small Co. Stocks	1,221,269		1,221,269
Total assets measured at fair value	\$ 32,475,372	\$ 15,363,698	\$ 17,111,674

There are no investments measured at level 3.

Financial Investments not Measured at Fair Value

Some of the Diocese's financial instruments are not measured at fair value on a recurring basis but nevertheless are recorded at amounts that approximate fair value due to their liquid or short-term nature. Such assets and liabilities include: Cash and cash equivalents, receivables, other investments, notes receivable, equity interest in real property, payables, deferred revenue and line of credit.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Note 5 - Charitable Remainder Unitrusts:

The Diocese is the trustee for various charitable remainder unitrusts, which have been invested. These investments represent gifts received subject to certain restrictions on the distribution of income and the assets of the unitrust. The unitrust agreements specify the beneficiaries of the income and the assets.

The charitable remainder unitrust agreements provide for annuity payments to donors of 5% to 10%. The Diocese records this investment at fair market value. The estimated liability is based upon the annuity payments and donor life expectancy using a discount rate of 5% to 6.5% (as of gift receipt date) and is classified as funds held in trust for beneficiary.

The investments in charitable remainder unitrusts consist of the following at December 31, 2011 and 2010:

	2011	2010
Funds	\$ 17,111,674	\$ 18,558,783
Less funds held in trust for beneficiaries	(14,203,237)	(15,132,564)
Less accounts payable to related party		(313,839)
	<hr/>	<hr/>
	\$ 2,908,437	\$ 3,112,380

The contribution revenue and changes in value of charitable remainder trusts recognized under such agreements for the year ended December 31, 2011 and 2010 are the following:

	2011	2010
Contributions		\$ 3,201
Change in value	\$ (203,943)	304,133
Interfund transfer		(292,991)
	<hr/>	<hr/>
Net change in unitrusts	\$ (203,943)	\$ 14,343

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Note 6 - Notes Receivable Held for Investment:

Notes receivable held for investment consists of the following at December 31, 2011 and 2010:

	2011	2010
Note receivable from Episcopal Church of the Redeemer and Redeemer Pre-School; bearing interest at 4%; principal and interest due through August 2014; secured by Episcopal Bishop of California property.		\$ 89,674
Note Receivable from St. James Episcopal Church, Oakland; bearing interest at 0% and due in 2016.	\$ 2,300	30,750
	<u>\$ 2,300</u>	<u>\$ 120,424</u>

Note 7 - Equity Interests in Real Property:

Equity interests in real property, which are recorded at cost, consist of the following at December 31, 2011 and 2010:

	2011	2010
24% equity interest in real property owned by Bayani Rico	\$ 43,949	\$ 43,949
31% equity interest in real property owned by the Culmers	160,000	160,000
22% equity interest in real property owned by the Mission Clergy Person, Sue Thompson	100,000	100,000
50% equity interest in real property owned by the former Bishop	927,500	927,500
	<u>\$ 1,231,449</u>	<u>\$ 1,231,449</u>

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Note 8 - Property and Equipment:

At December 31, 2011 and 2010, property and equipment consisted of the following:

	2011	2010
Diocesan House	\$ 1,047,630	\$ 1,027,752
S. F. Campus Center partial interest	30,000	30,000
Computers/server	112,303	99,667
Other furniture and equipment	82,240	79,039
Automobile	27,108	27,108
Hearst Street, Berkeley	649,669	649,669
Bishop's Residence	1,112,605	1,112,605
Bishop's Residence Improvements	72,707	72,707
Construction in Progress	9,744	
	<hr/>	<hr/>
	3,144,006	3,098,547
Less accumulated depreciation	(762,133)	(675,426)
	<hr/>	<hr/>
	2,381,873	2,423,121
Land	1,816,213	1,816,213
	<hr/>	<hr/>
	\$ 4,198,086	\$ 4,239,334

Depreciation expense for the years ended December 31, 2011 and 2010 was \$86,707 and \$77,660, respectively.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Note 9 - Line of Credit:

The Diocese has an unsecured line of credit agreement with Union Bank of California under which the Diocese may borrow up to \$9,500,000; bearing interest at the prime rate (3.25%); interest payable monthly; principal due on October 2, 2012.

Total principal payments due to Union Bank on the line of credit are \$2,718,945 at December 31, 2011. This debt is incurred by the Diocese on behalf of various parishes and missions as follows:

<i>December 31, 2011</i>	Line of Credit and Other Notes Payable	Corresponding Receivable
Parishes:		
Lafayette, St. Anselm's	\$ 43,615	\$ 43,615
Orinda, St. Stephens	621,000	621,000
Pleasanton, St. Clare's	587,813	587,813
San Francisco, St. Aidan's	33,000	33,000
San Leandro, All Saints'	33,437	33,437
Pleasant Hill, Resurrection	28,466	28,466
Danville, St. Timothy's	557,913	557,913
Concord, St. Michael and All Angels	59,500	59,500
Total parishes	1,964,744	1,964,744
Other Properties:		
Berkeley Emergency Food and Housing	132,194	132,194
Bishop's Ranch	51,375	51,375
Episcopal Community Services	400,000	400,000
Episcopal Diocese	91,500	
St. Dorothy's Rest	79,132	79,132
Total other properties	754,201	662,701
Total	\$ 2,718,945	\$ 2,627,445

In May 2012, St. Dorothy's drew down approximately \$800,000 of the line of credit to close a land purchase transaction. The line of credit is under the same line of credit agreement with Union Bank of California above.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Note 10 - Endowment Funds:

The Diocese's endowments consist of 102 individual funds, established to fund general operations of the Diocese or specific congregations and programs in the Diocese. Its endowment includes donor-restricted endowment funds and funds designated by the Executive Council to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the Executive Council to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

In 2008, the Diocese implemented ASC 958-205 *Reporting Endowment Funds* which was effective for fiscal years ending after December 15, 2008. The state of California adopted a version of the Uniform Prudent Management of Institutional Funds Act as its State Prudent Management of Institutional Funds Act (SPMIFA) which is applicable to funds established on or after January 1, 2009 and funds established prior to January 1, 2009 only with respect to actions taken after January 1, 2009.

SPMIFA moves away from the concept of corpus with its "historical dollar value" in an endowment. Charities are encouraged to develop spending policies that are responsive to short term fluctuations in the value of the fund, preserve the value of the fund for future use, and honor the charitable purpose of the fund. The Diocese will continue to balance the endurance of its funds and the needs of the community in its spending policy and practices.

Interpretation of Relevant Law

The Diocese considers the fair value of its endowment funds to be the value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary.

The Diocese classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by SPMIFA.

In accordance with SPMIFA, the organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) The duration and preservation of the fund, (2) The purposes of the organization and the donor-restricted endowment fund, (3) General economic conditions, (4) The possible effect of inflation and deflation, (5) The expected total return from income and the appreciation of investments, (6) Other resources of the organization, (7) The investment policies of the organization.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or SPMIFA requires the Diocese to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were \$1,139,855 and \$573,741 as of December 31, 2011 and 2010, respectively.

Return Objectives and Risk Parameters

The Diocese has adopted investment and spending policies for endowment assets that will ultimately provide a predictable stream of funding to provide support for the various programs and ministries of the Diocese of California. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity as well as board-designated funds. Under this policy, as approved by the Executive Council, the endowment assets are invested in a manner that is intended to realize a competitive rate of return comparable to index benchmarks.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the Diocese relies on a diversified asset investment strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Diocese targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

The Diocese is expecting to provide annual distributions of 5% of the market value of the portfolio as calculated on a 3 year rolling average. The investment managers are required to invest funds so as to ensure that required distributions of income or principal are met.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Net changes in endowment funds for the year ended December 31, 2011 were as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Net Assets, December 31, 2010	\$ (573,741)	\$ 11,978,281	\$ 8,403,491	\$ 19,808,031
<hr/>				
Investment Return:				
Income		402,157		402,157
Net depreciation	(566,114)	(861,225)		(1,427,339)
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Total investment return	(566,114)	(459,068)		(1,025,182)
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Contributions		62	350,149	350,211
Depreciation of endowment assets		(1,585,028)		(1,585,028)
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Endowment Net Assets, December 31, 2011	\$ (1,139,855)	\$ 9,934,247	\$ 8,753,640	\$ 17,548,032

Note 11 - Net Assets:

Temporarily restricted net assets are restricted for specific purposes as of December 31, 2011.

	Custodial	Endowment	Deferred Gifts	Total
Support Diocese	\$ 129,133	\$ 3,254,655	\$ 399,063	\$ 3,782,851
Education		41,787	49,734	91,521
Congregational Support		1,676,272	104,611	1,780,883
Congregational Development	676,191	1,243,713		1,919,904
Social Ministry	34,002	2,014,904	33,596	2,082,502
Scholarships	156,576	1,702,916		1,859,492
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	\$ 995,902	\$ 9,934,247	\$ 587,004	\$ 11,517,153

Net assets were released from donor restrictions by incurring expenses satisfying the purpose of the restriction for the year ended December 31, 2011 and 2010.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Permanently restricted net assets are invested in perpetuity with the income available to support the programs of the Diocese as of December 31, 2011 are as follows:

	Endowment	Deferred Gifts	Total
Support Diocese	\$ 5,955,735	\$ 681,181	\$ 6,636,916
Education	217,197	279,215	496,412
Congregational Support	1,535,080	536,430	2,071,510
Congregational Development	318,952	151,805	470,757
Social Ministry	525,860	672,802	1,198,662
Scholarships	200,816		200,816
	<hr/>	<hr/>	<hr/>
	\$ 8,753,640	\$ 2,321,433	\$ 11,075,073

Note 12 - Related Parties:

Included in accounts payable, related party at December 31, 2011 are funds held for others in the amount of \$340,519. Two churches gave these funds to the Diocese to invest and hold for them.

Note 13 - Retirement Plans:

The Diocese funds defined contribution pension plans covering lay employees. The Diocese contributes between 5% and 9% of employee compensation depending upon the employee contribution. The 2011 and 2010 contribution by the Diocese to the defined contribution pension plans approximated \$50,302 and \$51,830, respectively.

The Diocese also provides pension benefits for the clergy through a national plan. The plan is a defined benefit pension plan funded by specific assessments charged to the Diocese based on a specified percentage of compensation. In 2011 and 2010, the Diocese contributed approximately \$135,698 and \$169,829 (18% of compensation), respectively, to the clergy defined benefit pension plan.

The Episcopal Church in the Diocese of California

Notes to Financial Statements

Note 14 - Concentrations of Credit Risk:

The Diocese has identified its financial instruments which are potentially subject to credit risk. These financial instruments consist principally of cash and cash equivalents, investments in securities, and notes receivable held for investment.

The Diocese invests its cash deposits with three financial institutions. Periodically, throughout the year, the Diocese has maintained balances in operation and money market accounts in excess of federally insured limits.

Investments in securities are diversified into various equity instruments and other investment securities in order to limit the concentration of market risk.

The notes receivable held for investments, as described in Note 6, consist of notes secured by property and unsecured notes.

The Diocese bills and collects assessment revenue from the various parishes. Assessment revenues comprised 70% of all non investment revenue the Diocese received in 2011.

The Episcopal Church in the Diocese of California

Changes in Fund Asset Balance (See Independent Auditors' Report on Changes in Fund Asset Balance)

Year Ended December 31, 2011

	Operating	Custodial and Unexpended Income	Endowment and Trust	Deferred Gifts	Total All Funds
Beginning Balance - December 31, 2010	\$ 5,501,673	\$ 469,302	\$ 19,808,031	\$ 3,112,380	\$ 28,891,386
Income:					
Assessment income	3,323,315				3,323,315
Gifts and grants	458,095	826,153	350,211		1,634,459
Investment income, net	(22,511)				(22,511)
Realized and unrealized gains			(1,025,182)	(203,943)	(1,229,125)
Expenses:					
Operating departments (exclude payments to beneficiaries and other custodial)	(4,017,848)				(4,017,848)
Interfund Transfer:					
Endowments Fund to Operating Fund	1,460,168		(1,460,168)		
Less: payments to beneficiaries	(365,902)				(365,902)
Custodial Funds to Operating Fund	424,413	(424,413)			
Less: payments to beneficiaries	(424,413)				(424,413)
Endowment Fund to Custodial Fund		124,860	(124,860)		
Deferred Gifts to Endowment Fund					
Ending Balance - December 31, 2011	\$ 6,336,990	\$ 995,902	\$ 17,548,032	\$ 2,908,437	\$ 27,789,361
