

# **The Episcopal Church in Hawai'i**

**Financial Statements**

**December 31, 2009 and 2008**

# The Episcopal Church in Hawai'i

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**Report of Independent Auditor**

To the Diocesan Council of  
The Episcopal Church in Hawai'i

I have audited the accompanying statements of financial position of The Episcopal Church in Hawai'i (the "Church") as of December 31, 2009 and 2008, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Church's management. My responsibility is to express an opinion on these financial statements based on my audits.

I conducted my audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that I 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. I believe that my audits provide a reasonable basis for my opinion.

As more fully described in Note 1 to the financial statements, the Church does not provide for depreciation on its property and equipment nor does it provide for the disclosure of the component cost of land, buildings and other properties which is required by generally accepted accounting principles. Also, as more fully described in Note 9 to the financial statements, the Church does not include in its financial statements the financial position and activities of subsidiary entities as required by generally accepted accounting principles.

In my opinion, except for the effects of not depreciating property and equipment, not providing disclosure regarding the component cost of land, buildings and other properties, and not presenting the consolidated financial position and activities of subsidiary entities, as described in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of The Episcopal Church in Hawai'i as of December 31, 2009 and 2008, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

*James P. Hasselman, CPA, LLC*

Honolulu, Hawai'i  
July 16, 2010

**The Episcopal Church in Hawai'i**  
**Statement of Financial Position**  
**December 31, 2009**

	<b>Current Operations</b>	<b>Long-Term Investment</b>	<b>Plant</b>	<b>Total</b>
<b>Assets</b>				
Cash and cash equivalents	\$ 302,145	\$ -	\$ -	\$ 302,145
Accounts receivable from parishes, missions and other (net of allowance for doubtful accounts of \$232,525)	343,692	-	-	343,692
Prepaid expenses and other assets	66,273	-	-	66,273
Investments (Note 2)	-	30,307,686	-	30,307,686
Loans receivable from parishes, missions and other (Note 5)	789,450	-	-	789,450
Property and equipment (Note 4)	-	-	589,446	589,446
Assets held in trust by others	-	1,952,885	-	1,952,885
Total assets	<u>\$ 1,501,560</u>	<u>\$ 32,260,571</u>	<u>\$ 589,446</u>	<u>\$ 34,351,577</u>
<b>Liabilities and Net Assets</b>				
Accounts payable and other accrued expenses	\$ 50,596	\$ -	\$ -	\$ 50,596
Accrued vacation and sabbatical leave	154,430	-	-	154,430
Annuity obligation	-	7,278	-	7,278
Due to parishes and other organizations	13,192	15,198,955	-	15,212,147
Security deposits	11,484	-	-	11,484
Accrued postretirement benefit cost (Note 7)	642,254	-	-	642,254
Notes payable (Note 5)	789,450	-	-	789,450
Total liabilities	<u>1,661,406</u>	<u>15,206,233</u>	<u>-</u>	<u>16,867,639</u>
<b>Net Assets</b>				
Unrestricted	(233,266)	3,671,786	406,664	3,845,184
Temporarily restricted (Note 8)	73,420	6,241,667	182,782	6,497,869
Permanently restricted (Note 8)	-	7,140,885	-	7,140,885
Total net assets	<u>(159,846)</u>	<u>17,054,338</u>	<u>589,446</u>	<u>17,483,938</u>
Total liabilities and net assets	<u>\$ 1,501,560</u>	<u>\$ 32,260,571</u>	<u>\$ 589,446</u>	<u>\$ 34,351,577</u>

The accompanying notes are an integral part of the financial statements.

**The Episcopal Church in Hawai'i**  
**Statement of Financial Position**  
**December 31, 2008**

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	Current Operations	Long-Term Investment	Plant	Total
<b>Assets</b>				
Cash and cash equivalents	\$ 467,208	\$ -	\$ -	\$ 467,208
Accounts receivable from parishes, missions and other (net of allowance for doubtful accounts of \$173,883)	329,586	-	-	329,586
Prepaid expenses and other assets	51,474	-	-	51,474
Contributions receivable from remainder trust	-	57,205	-	57,205
Investments (Note 2)	-	23,900,657	-	23,900,657
Loans receivable from parishes, missions and other (Note 5)	858,838	-	-	858,838
Property and equipment (Note 4)	-	-	589,446	589,446
Assets held in trust by others	-	1,767,677	-	1,767,677
Total assets	<u>\$ 1,707,106</u>	<u>\$ 25,725,539</u>	<u>\$ 589,446</u>	<u>\$ 28,022,091</u>
<b>Liabilities and Net Assets</b>				
Accounts payable and other accrued expenses	\$ 89,833	\$ -	\$ -	\$ 89,833
Accrued vacation and sabbatical leave	129,234	-	-	129,234
Annuity obligation	-	7,624	-	7,624
Due to parishes and other organizations	15,911	12,370,131	-	12,386,042
Security deposits	11,189	-	-	11,189
Accrued postretirement benefit cost (Note 7)	534,452	-	-	534,452
Notes payable (Note 5)	858,838	-	-	858,838
Total liabilities	<u>1,639,457</u>	<u>12,377,755</u>	<u>-</u>	<u>14,017,212</u>
<b>Net Assets</b>				
Unrestricted	(6,922)	2,583,610	406,664	2,983,352
Temporarily restricted (Note 8)	74,571	3,935,767	182,782	4,193,120
Permanently restricted (Note 8)	-	6,828,407	-	6,828,407
Total net assets	<u>67,649</u>	<u>13,347,784</u>	<u>589,446</u>	<u>14,004,879</u>
Total liabilities and net assets	<u>\$ 1,707,106</u>	<u>\$ 25,725,539</u>	<u>\$ 589,446</u>	<u>\$ 28,022,091</u>

The accompanying notes are an integral part of the financial statements.

**The Episcopal Church in Hawai'i**  
**Statement of Activities**  
**Year Ended December 31, 2009**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Revenues, gains and other support</b>				
Congregation assessments	\$ 1,669,364	\$ -	\$ -	\$ 1,669,364
Net unrealized and realized gains on investments	1,097,985	2,385,129	-	3,483,114
Contributions	42,801	73,761	4,600	121,162
Income on long-term investments	58,263	173,271	-	231,534
Apartment and parking rentals	139,952	-	-	139,952
Income from assets held in trust by others	113,809	17,787	-	131,596
Net change in value of assets held in trust by others	-	-	179,191	179,191
Interest	505	-	-	505
Change in value of split-interest agreements	800	5,563	71,482	77,845
Other	7,776	-	-	7,776
Net assets released from restrictions				
Satisfaction of program requirements	293,557	(293,557)	-	-
Transfer to reflect donor restrictions		(57,205)	57,205	-
Total revenues, gains and other support	<u>3,424,812</u>	<u>2,304,749</u>	<u>312,478</u>	<u>6,042,039</u>
<b>Expenses and losses</b>				
Mission				
Congregational support	511,341	-	-	511,341
Nation and World	412,837	-	-	412,837
Other commissions and ministries	51,290	-	-	51,290
	<u>975,468</u>	<u>-</u>	<u>-</u>	<u>975,468</u>
Discipleship	214,672	-	-	214,672
Stewardship				
Office of the Bishop	851,172	-	-	851,172
Diocesan support expenses	301,331	-	-	301,331
Retirees	125,589	-	-	125,589
Other support	20,700	-	-	20,700
Communications	15,407	-	-	15,407
	<u>1,314,199</u>	<u>-</u>	<u>-</u>	<u>1,314,199</u>
Bad debt expense	58,641	-	-	58,641
Total expenses and losses	<u>2,562,980</u>	<u>-</u>	<u>-</u>	<u>2,562,980</u>
Change in net assets	861,832	2,304,749	312,478	3,479,059
<b>Net assets</b>				
Beginning of year	<u>2,983,352</u>	<u>4,193,120</u>	<u>6,828,407</u>	<u>14,004,879</u>
End of year	<u>\$ 3,845,184</u>	<u>\$ 6,497,869</u>	<u>\$ 7,140,885</u>	<u>\$ 17,483,938</u>

The accompanying notes are an integral part of the financial statements.

**The Episcopal Church in Hawai'i**  
**Statement of Activities**  
**Year Ended December 31, 2008**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Revenues, gains and other support</b>				
Congregation assessments	\$ 1,712,911	\$ -	\$ -	\$ 1,712,911
Net unrealized and realized losses on investments	(2,698,627)	(3,084,846)	-	(5,783,473)
Contributions	65,618	75,784	4,000	145,402
Income on long-term investments	119,409	137,584	-	256,993
Apartment and parking rentals	133,675	0	-	133,675
Income from assets held in trust by others	113,396	16,556	-	129,952
Net change in value of assets held in trust by others	-	-	(687,134)	(687,134)
Interest	10,444	-	-	10,444
Change in value of split-interest agreements	246	(47,273)	-	(47,027)
Other	12,989	-	-	12,989
Net assets released from restrictions				
Satisfaction of program requirements	301,704	(301,704)	-	-
Total revenues, gains and other support	<u>(228,235)</u>	<u>(3,203,899)</u>	<u>(683,134)</u>	<u>(4,115,268)</u>
<b>Expenses and losses</b>				
<b>Mission</b>				
Congregational support	713,679	-	-	713,679
Nation and World	398,407	-	-	398,407
Other commissions and ministries	106,351	-	-	106,351
	<u>1,218,437</u>	<u>-</u>	<u>-</u>	<u>1,218,437</u>
Discipleship	185,683	-	-	185,683
<b>Stewardship</b>				
Office of the Bishop	940,678	-	-	940,678
Diocesan support expenses	410,491	-	-	410,491
Communications	24,478	-	-	24,478
Other support	20,700	-	-	20,700
Retirees	(4,870)	-	-	(4,870)
	<u>1,391,477</u>	<u>-</u>	<u>-</u>	<u>1,391,477</u>
Demolition of duplex	17,500	-	-	17,500
Bad debt expense	27,443	-	-	27,443
Total expenses and losses	<u>2,840,540</u>	<u>-</u>	<u>-</u>	<u>2,840,540</u>
Change in net assets	<u>(3,068,775)</u>	<u>(3,203,899)</u>	<u>(683,134)</u>	<u>(6,955,808)</u>
<b>Net assets</b>				
Beginning of year	<u>6,052,127</u>	<u>7,397,019</u>	<u>7,511,541</u>	<u>20,960,687</u>
End of year	<u>\$ 2,983,352</u>	<u>\$ 4,193,120</u>	<u>\$ 6,828,407</u>	<u>\$ 14,004,879</u>

The accompanying notes are an integral part of the financial statements.

**The Episcopal Church in Hawai'i**  
**Statements of Cash Flows**  
**Years Ended December 31, 2009 and 2008**

	<b>2009</b>	<b>2008</b>
<b>Cash flows from operating activities</b>		
Change in net assets	\$ 3,479,059	\$ (6,955,808)
Adjustments to reconcile change in net assets to net cash used in operating activities		
Net unrealized and realized gains on investments	(3,483,114)	5,783,473
Change in value of assets held in trust by others	(179,191)	687,134
Change in value of split interest agreements	(6,363)	47,027
Loss on demolition of property	-	17,500
Change in receivables	43,099	50,085
Change in prepaid expenses and other	(14,504)	(4,972)
Change in accounts payable and other accrued expenses	(39,237)	(44,198)
Change in accrued vacation and sabbatical leave	25,196	110,000
Change in due to parishes and other organizations	(2,719)	4,664
Change in accrued postretirement benefit cost	107,802	(21,426)
Net cash used in operating activities	<u>(69,972)</u>	<u>(326,521)</u>
<b>Cash flows from investing activities</b>		
Proceeds from sale of investments	42,393,956	74,640,752
Purchases of investments	(41,806,853)	(73,932,863)
Received from parishes for investment in investment pool	410,994	567,223
Parish withdrawals and distributions from investment pool	(1,093,188)	(1,104,047)
Collection of loans receivable from parishes	69,388	101,760
Net cash provided by (used in) investing activities	<u>(25,703)</u>	<u>272,825</u>
<b>Cash flows from financing activities</b>		
Payment of notes payable	(69,388)	(101,760)
Net cash used in financing activities	<u>(69,388)</u>	<u>(101,760)</u>
Net decrease in cash and cash equivalents	(165,063)	(155,456)
<b>Cash and cash equivalents</b>		
Beginning of year	467,208	622,664
End of year	<u>\$ 302,145</u>	<u>\$ 467,208</u>
<b>Cash paid during the year for</b>		
Interest	\$ 53,441	\$ 59,397

The accompanying notes are an integral part of the financial statements.

# The Episcopal Church in Hawai'i

## Notes to Financial Statements

### December 31, 2009 and 2008

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#### 1. Summary of Significant Accounting Policies

##### **Accounts and Records**

The accompanying financial statements reflect the financial position, activities and cash flows of The Episcopal Church in Hawai'i (the "Church"), which represents the central administrative body for the various departments within the Church's organization in Hawai'i. The accounts and records of the Church do not reflect the financial position and activities of parishes and missions ("parishes") or institutions ("departments, schools and camps"), which conduct much of the activities of The Episcopal Church throughout the State of Hawai'i.

##### **Financial Statement Presentation**

The financial statements have been prepared on the accrual basis of accounting. The statements of financial position present the Church's assets, liabilities and net assets as follows:

##### ***Current Operations***

Reflects assets, liabilities and net assets that result from day-to-day operations and are available to be expended currently.

##### ***Long-Term Investment***

Primarily consists of assets held in an investment pool on behalf of the Church and its affiliated parishes and other related organizations. A substantial portion of the Church's assets in this investment pool are donor restricted. Unrestricted assets in this pool have been designated by the board to be held for long-term investment.

##### ***Plant***

Consists of the Church's real property, furniture, fixtures and equipment.

##### **Use of Estimates in the Preparation of Financial Statements**

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

##### **Cash Equivalents**

The Church considers all highly liquid debt instruments, including short-term cash investments, purchased with an original maturity of three months or less to be cash equivalents, except for money market mutual funds held by the investment pool, which are considered to be investments.

##### **Investments**

The Church, through its fund management advisors and custodians, maintains an investment pool on behalf of itself, parishes and other related organizations. Parish investment funds, which are commingled with the Church's investments and accounted for using a pooled unit system, are reflected as assets and liabilities on the statement of financial position.

Investments are reported at fair value. Fair value is the price that would be received to sell an asset or transfer a liability in an orderly transaction between market participants at the measurement date.

Dividend income is recorded when received. Interest income is recorded on an accrual basis.

# The Episcopal Church in Hawai'i

## Notes to Financial Statements

### December 31, 2009 and 2008

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#### **Endowment Spending Policy**

The Church has a policy of appropriating for distribution each year five percent of its endowment fund's average fair value over the prior twelve quarters through the calendar year-end preceding the fiscal year in which the distribution is planned. The Church expects its long-term investment return to be such that the endowment fund's purchasing power will be preserved while still allowing for annual distributions.

#### **Property and Equipment**

Diocesan real property is carried at cost or estimated fair value at date of donation. The component cost of land and buildings is unavailable as the records of the Church do not provide a detail of cost by category. Immaterial acquisitions costing less than \$5,000 of furniture, fixtures and equipment are expensed by the Church.

Generally accepted accounting principles require not-for-profit organizations to recognize depreciation expense on long-lived tangible assets. Management has opted not to record depreciation expense; the effect of unrecognized depreciation expense has not been determined.

Management considers whether long-lived assets are impaired if events suggest that an impairment may exist. Impairments would be evaluated based on the cash flows expected to be generated by an asset relative to its carrying amount and any impairment loss would be based on the fair value of the asset. No impairment loss was recognized in 2009 or 2008.

Changes in estimates, based on market conditions and various other factors, may impact the future recoverability of the carrying value of long-lived assets.

The Church's Canons provide for the Church to serve as the custodian of record for certain real property and land lease agreements on behalf of individual parishes and other affiliated organizations. Such real property, related lease obligations and asset retirement obligations are not reflected in the Church's financial statements since in substance, the individual parishes and other organizations are the beneficial owners of the real property and related lease agreements. Should the parishes and other organizations not be able to honor their commitments under these obligations, the Church would be contingently liable to do so.

#### **Split-Interest Agreements**

The Church recognizes split-interest agreements such as charitable remainder trusts, charitable gift annuities, charitable lead trusts and perpetual trusts when a donor purchases an annuity contract or makes an initial irrevocable gift to a trust in which the Church has a beneficial interest.

Contributions receivable from remainder trust represents the beneficial interest in trust assets under agreements whereby assets are held by an independent trustee. The contributions receivable are not available to the Church until after the death of the donor, who, while living, receives an annual payment from the trust based on a fixed percentage of the trust assets. The contributions receivable are based on the present value of estimated future cash flows to be received by the Church.

Under charitable gift annuity agreements whereby the Church serves as trustee, the Church recognizes the assets at fair value. The portion of these assets held for the benefit of others is carried at the estimated present value of future payments to be distributed over the donor's

# The Episcopal Church in Hawai'i

## Notes to Financial Statements

### December 31, 2009 and 2008

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expected life based on Internal Revenue Service valuation tables, and is classified as an annuity obligation. The difference is recognized as contribution revenues in the year of the gift.

Assets held in trust by others represents assets held at fair value in charitable lead trusts and perpetual trusts by independent trustees and represent resources neither in the possession nor under the control of the Church, although the Church derives income from the assets of such trusts.

#### **Notes Payable**

Notes payable consist of secured and unsecured loans and mortgages obtained by the Church for the benefit of other parishes. Proceeds of notes are advanced to the parishes and the Church recognizes a receivable for those amounts. Interest expenses accrued and paid under the notes are recognized by the parishes and reimbursed to the Church.

#### **Net Assets**

The statements of activities, as well as net assets presented in the statements of financial position, have been presented to reflect the Church's three net assets categories, which are based on donor restrictions. The three net asset categories are as follows:

- **Unrestricted** – Net assets which are free of donor-imposed restrictions; all revenues, expenses, gains and losses that are not changes in permanently or temporarily restricted net assets. Included in this category are endowment assets that have been freed of donor-imposed restrictions through the incurrence of qualifying expenditures, whether or not paid for from endowment assets.
- **Temporarily Restricted** – Net assets whose use by the Church is limited by donor-imposed stipulations that either expire with the passage of time or can be fulfilled or otherwise removed by the actions of the Church. Temporarily restricted net assets consist primarily of endowment assets held for long-term investment that are available to support certain program and administrative expenses.
- **Permanently Restricted** – Net assets whose use by the Church is limited by donor-imposed stipulations that neither expire with the passage of time nor can be fulfilled or otherwise removed by the actions of the Church. Included in this category are assets held in trusts by others, the income from which is distributed to the Church for its use in operations, and endowment assets that must be held in perpetuity pursuant to donor stipulations.

In August 2008, the Financial Accounting Standards Board issued Staff Position No. FAS 117-1, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds* (subsequently codified by the FASB under ASC 958-205). ASC 958-205 provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA). ASC 958-205 also improves disclosures about an organization's endowment funds (both donor restricted endowment funds and board designated endowment funds) whether or not the organization is subject to UPMIFA. The Church implemented the disclosure requirements of this pronouncement in 2008.

# **The Episcopal Church in Hawai'i**

## **Notes to Financial Statements**

### **December 31, 2009 and 2008**

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The State of Hawaii adopted UPMIFA as of July 1, 2009 and the Church implemented the remaining (UPMIFA related) provisions of ASC 958-205 in 2009. The provisions implemented in 2009 did not have a material impact on the Church's financial statements.

#### **Contributions**

Contributions received are recognized as revenues when the donor's commitment is received. The Church reports contributions as restricted support if they are received with donor stipulations that limit the use of the donated assets. 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 and reported in the statement of activities as net assets released from restrictions.

#### **Donated Services**

Donated materials and services received in connection with the Church's program and management and general activities have not been recognized in the financial statements since these donations do not meet the recognition criteria under generally accepted accounting principles.

#### **Definition of Certain Revenues and Expenses**

The Church's major revenues and expenses are described below. Expenses are generally charged directly to each department, and allocations of costs between departments are not significant. Fundraising expenses are inconsequential and not separately reported.

#### ***Congregation Assessments***

Represents payments to the Church from parishes to help fund the operations and programs of the Church. Assessments are accounted for as exchange transactions and are recorded in the period they become due. Assessments from one parish are in excess of 10 percent of total parish assessments.

#### ***Apartment and Parking Rentals***

Represents rental income from St. Andrew's Priory for rental of a parking lot, amounting to approximately \$77,000 in 2009 and \$73,000 in 2008. Also includes apartment building rental income from tenants.

#### ***Congregational Support***

Represents subsidy support to parishes and missions.

#### ***Nation and World***

Represents an assessment paid to the National Church and the 8th Province. Also includes the funds to support delegates to attend the General Convention.

#### ***Other Commissions and Ministries***

Represents various other programmatic activities including emerging generations mission and congregational health and growth.

#### ***Discipleship***

Represents activities to develop spiritual and leadership programs and ministries relating to youths and young adults; diversity programs; native Hawaiian ministry programs; and other new ministry development.

# The Episcopal Church in Hawai'i

## Notes to Financial Statements

### December 31, 2009 and 2008

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#### *Office of the Bishop*

Represents compensation, benefits and other support costs for all personnel of the Office of the Bishop.

#### *Diocesan Support Expenses*

Represents general and administrative expenses related to the Office of the Bishop and the Diocese.

#### *Retirees*

Represents subsidies for health benefits of retired clergy and surviving spouses.

#### *Other Support*

Represents support to a mission for lease rent expenses.

#### *Communications*

Represents production costs of printed newsletters, publications, brochures, etc.

#### **Tax Status**

The Episcopal Church in Hawai'i is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. Management believes the Church does not have any unrelated business income that would be subject to taxation, or other uncertain tax positions. All previous tax years are open to examination by the Internal Revenue Service.

#### **Concentrations of Credit Risks**

The Church's cash balances are held with two financial institutions. Each account is covered by FDIC or SIPC insurance. Cash balances are occasionally in excess of available insurance coverage, however management does not believe the Church is exposed to any significant credit risk on cash balances. Accounts and loans receivable are with various parishes in Hawai'i.

#### **Reclassifications**

Certain 2008 departmental expense groupings and various disclosure amounts have been reclassified to conform to the 2009 presentation. These reclassifications had no impact on the change in net assets reported for 2008.

## **2. Investments**

The composition of investments is presented in Note 3. The return on investments for 2009 and 2008 was as follows:

	<b>2009</b>	<b>2008</b>
Interest and dividend income	\$ 346,555	\$ 388,387
Net unrealized and realized gains	3,483,114	(5,783,473)
Management fees and other costs	(115,021)	(131,394)
Total return on investments	<u>\$ 3,714,648</u>	<u>\$ (5,526,480)</u>

# The Episcopal Church in Hawai'i

## Notes to Financial Statements

### December 31, 2009 and 2008

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The Church attempts to minimize credit risk by limiting its investments in debt securities to U.S. Treasury notes and bonds, and to high-quality corporate notes and bonds diversified among various industry groups. Additionally, the Church attempts to minimize market risk by diversifying its investments in common and preferred stock among various industry groups.

#### *Investment Return Objectives*

The Church's investment objectives are to seek consistency of investment return with primary emphasis on capital appreciation and secondary emphasis on income. The Church seeks to hedge both income and principal against erosion in buying power resulting from inflation. The Church also seeks to generate a reasonable level of current income as practical, while hedging against inflation. Under this policy, the investment pool is invested in a manner that is intended to produce results that exceed the price and yield results of the market index, as defined in the policy statement, or 5 percentage points above the Consumer Price Index on a trailing 3 year basis.

To satisfy its long-term rate-of-return objectives, the Church 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 Church 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.

### **3. Fair Value Measurements**

Generally accepted accounting principles provide a framework for establishing fair value measurements. That framework provides a fair value hierarchy for inputs used in measuring fair market value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are those that market participants would use in pricing the asset or liability based on the best information available in the circumstances. This fair value hierarchy consists of three broad levels:

- Level 1 inputs consist of unadjusted quoted prices in active markets such as stock exchanges for identical assets and have the highest priority;
- Level 2 inputs consist of significant other observable inputs such as quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset and liability, either directly or indirectly, for substantially the full term of the financial instrument;
- Level 3 inputs consist of significant unobservable inputs and include situations where is little, if any, market activity for the investment. The inputs require significant judgment or estimates, such as those associated with discounted cash flow methodologies and appraisals.

The Church uses appropriate valuation techniques based on the available inputs to measure fair value. When available, the Church measures fair value using Level 1 inputs because they generally provide the most reliable evidence of fair value.

Following is a description of the valuation methodologies used for assets at fair value. There have been no changes in the methodologies used at December 31, 2009 and 2008.

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*Equity Securities:* Common stock and exchange traded funds are valued at the closing price reported on active stock exchanges (Level 1). Preferred stock is valued primarily by pricing models that incorporate available trade, bid and other market information (Level 2).

*Fixed Income Securities:* This asset class consists of corporate and convertible bonds, and U.S. government securities. Such securities are valued primarily by pricing models that incorporate available trade, bid and other market information (Level 2).

*Money market mutual funds:* Valued at the closing price reported on active stock exchanges (Level 1).

*Assets held in trust by others:* These assets have been valued based on the Church's beneficial interest percentage in the trust assets, which consist of marketable securities (valued at fair value) held by and reported to the Church by third party trustees (Level 2).

*Contributions receivable from remainder trust:* Valued based on present value techniques and actuarial tables (Level 3).

Fair values of assets measured on a recurring basis are as follows as of December 31, 2009:

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs Other Than Active Markets (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Investments</b>				
Common stock				
Basic materials	\$ 1,759,302	\$ 1,759,302	\$ -	\$ -
Capital goods/industrials	2,139,357	2,139,357	-	-
Consumer staples	1,115,656	1,115,656	-	-
Energy	1,887,371	1,887,371	-	-
Financials	2,752,059	2,752,059	-	-
Health care	2,405,445	2,405,445	-	-
Technology/info com	5,884,210	5,884,210	-	-
Other	1,099,904	1,099,904	-	-
Total common stock	19,043,304	19,043,304	-	-
Preferred stock	2,890,861	-	2,890,861	-
Convertible corporate notes	4,568,204	-	4,568,204	-
Corporate notes and bonds	2,203,986	-	2,203,986	-
Money market mutual funds	1,386,138	1,386,138	-	-
Foreign obligations	113,588	-	113,588	-
Accrued income and other	101,605	-	101,605	-
Total investments	\$ 30,307,686	\$ 20,429,442	\$ 9,878,244	\$ -
<b>Assets held in trust by others</b>	\$ 1,952,885	\$ -	\$ 1,952,885	\$ -

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Fair values of assets measured on a recurring basis are as follows as of December 31, 2008:

	<b>Fair Value</b>	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Observable Inputs Other Than Active Markets (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
<b>Investments</b>				
Common stock				
Basic materials	\$ 446,428	\$ 446,428	\$ -	\$ -
Capital goods/industrials	1,146,856	1,146,856	-	-
Consumer staples	1,620,133	1,620,133	-	-
Energy	1,193,064	1,193,064	-	-
Financials	1,787,055	1,787,055	-	-
Health care	2,345,675	2,345,675	-	-
Technology/info com	3,364,389	3,364,389	-	-
Other	1,247,611	1,247,611	-	-
Total common stock	<u>13,151,211</u>	<u>13,151,211</u>	-	-
Preferred stock	1,632,433	-	1,632,433	-
Convertible corporate notes	3,782,838	-	3,782,838	-
Corporate notes and bonds	3,497,301	-	3,497,301	-
Money market mutual funds	1,220,687	1,220,687	-	-
Foreign obligations	130,356	-	130,356	-
U.S. government bonds	199,328	-	199,328	-
Exchange traded funds	170,891	170,891	-	-
Accrued income and other	115,612	-	115,612	-
Total investments	<u>\$ 23,900,657</u>	<u>\$ 14,542,789</u>	<u>\$ 9,357,868</u>	<u>\$ -</u>
<b>Assets held in trust by others</b>	<b>\$ 1,767,677</b>	<b>\$ -</b>	<b>\$ 1,767,677</b>	<b>\$ -</b>
<b>Contributions receivable from remainder trust</b>	<b>57,205</b>	<b>-</b>	<b>-</b>	<b>57,205</b>

Investments in preferred stock, convertible corporate notes, and corporate notes and bonds are diversified among various industry groups, substantially all of which are U.S. based issuers.

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*Additional Disclosures for Level 3 assets:*

**Contributions Receivable from Remainder Trust**

**December 31, 2008**

Beginning balance	\$ 89,480
Gains or losses (realized and unrealized) included in changes in net assets	(32,275)
Contributions, purchases, sales, and settlements (net)	-
Ending balance	<u>\$ 57,205</u>

**December 31, 2009**

Beginning balance	\$ 57,205
Gains or losses (realized and unrealized) included in changes in net assets available for benefits	-
Contributions, purchases, sales, and settlements (net)	(57,205)
Ending balance	<u>\$ -</u>

**4. Property and Equipment**

Property and equipment at December 31, 2009 and 2008 consisted of the following:

	<b>2009</b>	<b>2008</b>
McCray/Canterbury house	\$ 276,332	\$ 276,332
Bishop's condominium, 30% interest	182,782	182,782
Cluett apartments	96,963	96,963
Other property and improvements	11,869	11,869
Other land, furniture and equipment	21,500	21,500
	<u>\$ 589,446</u>	<u>\$ 589,446</u>

The Church and the Bishop jointly own a condominium for the Bishop's residence. The Church has a 30% interest in the condominium. The Church and the Bishop have executed an Equity Share and Security Agreement, which provides the mechanism for the Bishop to acquire the Church's interest in the condominium, at fair market value.

In June 2010, the Church acquired land in Kapolei, Hawai'i for approximately \$2.6 million. The purchase was funded by the Church's investment portfolio.

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**5. Notes Payable**

Notes payable at December 31, 2009 and 2008 consisted of:

	<b>2009</b>	<b>2008</b>
<b>Collateralized</b>		
Camp Mokule'ia – \$517,000 note, payable in monthly installments including interest (\$3,225 at December 31, 2009); due February 2037. The note bears interest at 6.375% until February 2017, then adjusts to 2.75% above average U.S. Treasury rates, annually. Certain camp real property is pledged as collateral.	\$ 499,208	\$ 505,856
St. Phillip's – \$978,720 note, payable in \$4,593 monthly installments including interest; due September 2013. The note bears interest at 1.5% over the bank's prime rate (6.625% at December 31, 2009). Certain parish real property is pledged as collateral.	150,171	207,121
St. Christopher's – \$154,500 mortgage note, payable in \$970 monthly installments including fixed interest at 6.625%. Note is due June 2030. Certain parish real property is pledged as collateral.	130,376	133,276
<b>Unsecured</b>		
St. Stephen's – \$12,766 note, payable in \$310 monthly installments including fixed interest at 7.38%; due November 2012.	9,695	12,585
	<u>\$ 789,450</u>	<u>\$ 858,838</u>

Annual maturities of notes payable for the next five years are as follows:

<b>Years ending</b>	
2010	\$ 59,852
2011	63,946
2012	67,973
2013	13,071
2014	13,172
Thereafter	571,436
	<u>\$ 789,450</u>

All of the notes listed above were obtained by the Church for the purpose of loaning the proceeds to the indicated parish, for their use in capital improvements. Loans receivable from parishes, missions and others on the statement of financial position in the amount of \$789,450 and \$858,838 at December 31, 2009 and 2008, respectively, corresponds to the outstanding balances on these bank notes payable.

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In April 2010, the Church executed a \$200,000 loan guaranty on behalf of Camp Mokule'ia, in connection with a bank loan obtained by the Camp for the purpose of financing certain Camp improvements.

**6. Pension Benefits**

The Church maintains a defined contribution pension plan, which covers substantially all full-time lay employees of the Office of the Bishop. Contributions are determined as a percentage of each covered employee's salary. Pension expense for fiscal 2009 and 2008 amounted to \$24,856 and \$21,789, respectively, for this plan.

The Church also participates in the Church Pension Fund, a multiemployer pension fund established by the Canon of the General Convention, which covers clergy of all dioceses, parishes, missions and other ecclesiastical organizations. Pension expense for fiscal 2009 and 2008 amounted to \$43,575 and \$41,533, respectively, for this plan.

**7. Other Postretirement Benefits**

The Church provides a postretirement supplemental Medicare health plan benefit for retired clergy and certain lay personnel. The plan purchases supplemental Medicare insurance from third-party providers. The plan is contributory, with retiree contributions providing for 40% of the insurance cost. The plan is unfunded.

The Church uses a December 31 measurement date for the plan. The funded status of the plan as of December 31, 2009 and 2008 was:

	<b>2009</b>	<b>2008</b>
Accumulated postretirement benefit obligation	\$ (642,254)	\$ (534,452)
Fair value of plan assets	-	-
Funded status	<u>\$ (642,254)</u>	<u>\$ (534,452)</u>

As of December 31, 2009 and 2008, the accrued postretirement benefit liability recognized in the statements of position was \$642,254 and \$534,452, respectively. Assumptions used to determine the accumulated postretirement benefit obligation at December 31, 2009 and 2008 included:

	<b>2009</b>	<b>2008</b>
Discount rate	5.85%	6.50%
Health care cost trend rate over the next year	6.00%	6.00%
Ultimate health care cost trend rate	6.00%	6.00%
Mortality rates	Retired Pensioners Mortality Tables (RP 2000)	
Retirement and withdrawal rates	Specific identification	

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Cash activity for the years ended December 31, 2009 and 2008 was as follows:

	<b>2009</b>	<b>2008</b>
Employer contributions	\$ 17,471	\$ 16,556
Participant contributions	12,126	8,461
Benefits paid	29,597	25,017

Amounts recognized in the statements of activities for the years ended December 31, 2009 and 2008 were as follows:

	<b>2009</b>	<b>2008</b>
Amounts recognized in the statement of activities:		
Net loss (gain) arising during the period	\$ 87,734	\$ (37,526)
Amortization of prior service cost and net gains	(1,198)	302
Total benefit changes other than net periodic benefit cost	86,536	(37,224)
Net periodic benefit cost	38,737	32,354
	<u>\$ 125,273</u>	<u>\$ (4,870)</u>
Discount rate for interest cost component of benefit cost	6.50%	5.75%

Amounts reflected in unrestricted net assets that have not yet been recognized as a component of net periodic benefit cost are as follows:

	<b>2009</b>	<b>2008</b>
Unamortized actuarial gains	\$ (39,323)	\$ (141,779)
Unamortized transition obligation	79,595	95,515
	<u>\$ 40,272</u>	<u>\$ (46,264)</u>

These unamortized items will continue to be amortized as a component of net periodic benefit cost in future years, with an offsetting reclassification adjustment to change in net assets. Amortization expense of the unamortized transition obligation is \$15,920 annually. Fiscal 2010 amortization (income) of unamortized actuarial gains is expected to be negligible.

The Church expects to contribute \$14,875 to the plan in 2010.

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The following summarizes the benefits expected to be paid in future years based on the current enrollment, assumed future participation, and the same assumptions used to measure the accumulated postretirement benefit obligation:

Years ending December 31,	Benefits estimated to be paid	Estimated source	
		Employer contributions	Retiree contributions
2010	\$ 24,792	\$ 14,875	\$ 9,917
2011	25,299	15,179	10,120
2012	31,566	18,940	12,626
2013	33,212	19,927	13,285
2014	34,915	20,949	13,966
2015 - 2019	199,039	119,423	79,616

**8. Net Assets**

The Church's endowment consists of numerous individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the governing board to function as endowments. Endowment net assets, reflecting the purposes of the funds, as well as non-endowment net assets consisted of the following at December 31, 2009:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Donor Restricted Endowments</b>				
Episcopate	\$ -	\$ 2,460,068	\$ 1,684,231	\$ 4,144,299
Congregational development	-	13,786	6,392	20,178
Communication	-	12,244	6,023	18,267
Land and building	-	1,722,678	-	1,722,678
Loan fund	-	485,121	167,114	652,235
Other programs	-	932,769	584,543	1,517,312
Discretionary	-	584,018	2,779,845	3,363,863
	-	6,210,684	5,228,148	11,438,832
<b>Other Endowments</b>				
Board designated for endowment	3,669,899	-	-	3,669,899
Split interest agreements	1,887	30,983	-	32,870
Perpetual trusts	-	-	1,912,737	1,912,737
Subtotal endowment funds	3,671,786	6,241,667	7,140,885	17,054,338
<b>Non-Endowments</b>				
Operating fund	(233,266)	73,420	-	(159,846)
Property and equipment	406,664	182,782	-	589,446
	173,398	256,202	-	429,600
Total net assets	\$ 3,845,184	\$ 6,497,869	\$ 7,140,885	\$ 17,483,938

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Changes in endowment net assets for the year ending December 31, 2009 were as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Endowment Funds, January 1, 2009</b>	\$ 2,583,610	\$ 3,935,767	\$ 6,828,407	\$ 13,347,784
Interest and dividends, net of investment expense	56,404	175,127	-	231,531
Net realized/unrealized gains (losses)	1,097,985	2,385,129	-	3,483,114
Contributions	-	-	4,600	4,600
Amounts appropriated for expenditure	(67,013)	(202,714)	-	(269,727)
Transfer of net asset restrictions	-	(57,205)	57,205	-
Increase in value of perpetual trusts	-	-	179,191	179,191
Change in value of split interest agreements	800	5,563	71,482	77,845
<b>Endowment Funds, December 31, 2009</b>	<u>\$ 3,671,786</u>	<u>\$ 6,241,667</u>	<u>\$ 7,140,885</u>	<u>\$ 17,054,338</u>

Endowment and non-endowment net assets consisted of the following at December 31, 2008:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Donor Restricted Endowments</b>				
Episcopate	\$ -	\$ 1,644,291	\$ 1,684,231	\$ 3,328,522
Congregational development	-	9,645	6,392	16,037
Communication	-	8,496	6,023	14,519
Land and building	-	1,262,422	-	1,262,422
Loan fund	-	325,155	167,114	492,269
Other programs	(11,949)	603,133	451,256	1,042,440
Discretionary	(239,360)	-	2,779,845	2,540,485
	<u>(251,309)</u>	<u>3,853,142</u>	<u>5,094,861</u>	<u>8,696,694</u>
<b>Other Endowments</b>				
Board designated for endowment	2,833,832	-	-	2,833,832
Split interest agreements	1,087	82,625	-	83,712
Perpetual trusts	-	-	1,733,546	1,733,546
Subtotal endowment funds	<u>2,583,610</u>	<u>3,935,767</u>	<u>6,828,407</u>	<u>13,347,784</u>
<b>Non-Endowments</b>				
Operating fund	(6,922)	74,571	-	67,649
Property and equipment	406,664	182,782	-	589,446
	<u>399,742</u>	<u>257,353</u>	<u>-</u>	<u>657,095</u>
Total net assets	<u>\$ 2,983,352</u>	<u>\$ 4,193,120</u>	<u>\$ 6,828,407</u>	<u>\$ 14,004,879</u>

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Changes in endowment net assets for the year ended December 31, 2008 were as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Endowment Funds, January 1, 2008</b>	\$ 5,390,111	\$ 7,134,831	\$ 7,511,541	\$ 20,036,483
Interest and dividends, net of investment expense	119,409	137,583	-	256,992
Net realized/unrealized gains (losses)	(2,698,627)	(3,084,846)	-	(5,783,473)
Contributions	41,143	66,846	4,000	111,989
Amounts appropriated for expenditure	(268,672)	(271,374)	-	(540,046)
Decrease in value of perpetual trusts	-	-	(687,134)	(687,134)
Change in value of split interest agreements	246	(47,273)	-	(47,027)
<b>Endowment Funds, December 31, 2008</b>	<u>\$ 2,583,610</u>	<u>\$ 3,935,767</u>	<u>\$ 6,828,407</u>	<u>\$ 13,347,784</u>

As a result of stock market declines in 2008, the fair value of two of the Church's endowment funds as of December 31, 2008 was less than the historic gift value of the funds, which is the value that the donors indicated must be maintained permanently. In accordance with generally accepted accounting principles, deficiencies of this nature are reported in unrestricted net assets. Such deficiencies amounted to \$251,309 as of December 31, 2008. There were no such deficiencies as of December 31, 2009.

***Interpretation of UPMIFA***

The governing board (Council) of the Church, in consultation with legal counsel, has interpreted Hawaii's Uniform 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 donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Church classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, and (b) the original value of subsequent gifts to the permanent endowment. 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 UPMIFA, and upon satisfaction of any purpose restrictions on the fund.

**9. Unconsolidated Entities**

Generally accepted accounting principles, as reflected in "Reporting of Related Entities by Not-for-Profit Organizations" establishes a framework for determining when a not-for-profit reporting entity should consolidate the financial position and activities of another not-for-profit entity. The determining criterion for consolidation within the framework is whether the reporting entity has both control over and an economic interest in the other entity. Management has evaluated the criterion in relation to numerous organizations and determined that two entities meet the criterion for consolidation: St. Andrew's Priory and Camp Mokule'ia. Management has decided not to consolidate these entities and instead is presenting the financial position and activities of the Church on an unconsolidated basis. Accordingly, the Church's consolidation policy is not in accordance with generally accepted accounting principles.

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Summarized financial information for these two entities have not been provided as audited financial statements as of their respective year ends (December 31, 2009 for the Camp and July 31, 2009 for the Priory) are not available.

**10. Subsequent Events**

The U.S. stock market continued to be volatile in 2010. Through June 30, 2010, the Church's investment portfolio was down approximately 6%.

Management has reviewed and considered whether events occurring after year end should be reflected or disclosed in these financial statements. The date through which this review was conducted was July 16, 2010, the date the financial statements were available to be issued.