

The Episcopal Church in Hawai'i

Financial Statements

December 31, 2017 and 2016

The Episcopal Church in Hawai'i

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Independent Auditor's Report

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

I have audited the accompanying financial statements of The Episcopal Church in Hawai'i (the "Church", a nonprofit organization), which comprise the statements of financial position as of December 31, 2017 and 2016, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for Qualified Opinion

As 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 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. The effects of the above matters on the accompanying financial statements have not been determined.

Qualified Opinion

In my opinion, except for the effects of the matters described in the *Basis for Qualified Opinion* paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Church as of December 31, 2017 and 2016, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

James P. Hasselman, CPA, LLC

Honolulu, Hawai'i
August 20, 2018

The Episcopal Church in Hawai'i
Statement of Financial Position
December 31, 2017

	Current Operations	Long-Term Investment	Plant	Total
Assets				
Cash and cash equivalents	\$ 870,877	\$ 9,345	\$ -	\$ 880,222
Accounts receivable from parishes, missions and other	449,152	-	-	449,152
Prepaid expenses and other assets	17,478	-	-	17,478
Investments	-	39,845,260	-	39,845,260
Loans receivable from parishes, missions and other, net of allowance for credit losses	276,530	-	-	276,530
Property and equipment	-	-	2,899,481	2,899,481
Assets held in trust by others	-	2,398,282	-	2,398,282
Total assets	<u>\$ 1,614,037</u>	<u>\$ 42,252,887</u>	<u>\$ 2,899,481</u>	<u>\$ 46,766,405</u>
Liabilities and Net Assets				
Accounts payable and other accrued expenses	\$ 22,380	\$ -	\$ -	\$ 22,380
Accrued vacation and sabbatical leave	34,060	-	-	34,060
Annuity obligation	-	6,930	-	6,930
Due to parishes and other organizations	55,436	20,604,422	-	20,659,858
Security deposits	17,080	-	-	17,080
Accrued postretirement benefit cost	755,883	-	-	755,883
Notes payable	256,530	-	-	256,530
Total liabilities	<u>1,141,369</u>	<u>20,611,352</u>	<u>-</u>	<u>21,752,721</u>
Net Assets				
Unrestricted	305,720	5,417,061	2,899,481	8,622,262
Temporarily restricted	166,948	7,832,329	-	7,999,277
Permanently restricted	-	8,392,145	-	8,392,145
Total net assets	<u>472,668</u>	<u>21,641,535</u>	<u>2,899,481</u>	<u>25,013,684</u>
Total liabilities and net assets	<u>\$ 1,614,037</u>	<u>\$ 42,252,887</u>	<u>\$ 2,899,481</u>	<u>\$ 46,766,405</u>

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

The Episcopal Church in Hawai'i
Statement of Financial Position
December 31, 2016

	Current Operations	Long-Term Investment	Plant	Total
Assets				
Cash and cash equivalents	\$ 1,759,474	\$ -	\$ -	\$ 1,759,474
Accounts receivable from parishes, missions and other	576,300	-	-	576,300
Prepaid expenses and other assets	29,370	-	-	29,370
Investments	-	33,877,580	-	33,877,580
Loans receivable from parishes, missions and other	694,236	-	-	694,236
Property and equipment	-	-	3,175,813	3,175,813
Assets held in trust by others	-	2,192,092	-	2,192,092
Total assets	<u>\$ 3,059,380</u>	<u>\$ 36,069,672</u>	<u>\$ 3,175,813</u>	<u>\$ 42,304,865</u>
Liabilities and Net Assets				
Accounts payable and other accrued expenses	\$ 63,733	\$ -	\$ -	\$ 63,733
Accrued vacation and sabbatical leave	34,060	-	-	34,060
Annuity obligation	-	6,930	-	6,930
Due to parishes and other organizations	33,967	18,258,328	-	18,292,295
Security deposits	17,511	-	-	17,511
Accrued postretirement benefit cost	608,409	-	-	608,409
Notes payable	494,492	-	-	494,492
Total liabilities	<u>1,252,172</u>	<u>18,265,258</u>	<u>-</u>	<u>19,517,430</u>
Net Assets				
Unrestricted	1,639,761	2,839,167	3,175,813	7,654,741
Temporarily restricted	167,447	6,832,473	-	6,999,920
Permanently restricted	-	8,132,774	-	8,132,774
Total net assets	<u>1,807,208</u>	<u>17,804,414</u>	<u>3,175,813</u>	<u>22,787,435</u>
Total liabilities and net assets	<u>\$ 3,059,380</u>	<u>\$ 36,069,672</u>	<u>\$ 3,175,813</u>	<u>\$ 42,304,865</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, 2017

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains and other support				
Congregation assessments	\$ 1,575,964	\$ -	\$ -	\$ 1,575,964
Gain on sale of real property	916,794	-	-	916,794
Net unrealized and realized gains on investments	352,126	1,170,449	-	1,522,575
Contributions	36,682	73,717	53,181	163,580
Income on long-term investments	77,879	253,490	-	331,369
Apartment and parking rentals	175,234	-	-	175,234
Income from assets held in trust by others	85,543	24,400	-	109,943
Net change in value of assets held in trust by others	-	-	206,190	206,190
Interest	75	-	-	75
Other	4,113	-	-	4,113
Net assets released from restrictions				
Satisfaction of program requirements	522,699	(522,699)	-	-
Total revenues, gains and other support	<u>3,747,109</u>	<u>999,357</u>	<u>259,371</u>	<u>5,005,837</u>
Expenses				
Ministry and Mission				
Diocesan initiatives	68,379	-	-	68,379
Congregational support	292,324	-	-	292,324
Discipleship	109,713	-	-	109,713
Outreach and justice	32,430	-	-	32,430
Ministry development	194,998	-	-	194,998
Other	67,124	-	-	67,124
	<u>764,968</u>	<u>-</u>	<u>-</u>	<u>764,968</u>
Diocesan Organization				
Episcopate	373,347	-	-	373,347
Bishop's staff	533,142	-	-	533,142
Diocesan expenses	637,804	-	-	637,804
Office building expenses	45,959	-	-	45,959
Travel	42,888	-	-	42,888
Bad debt expense	179,744	-	-	179,744
Other	46,452	-	-	46,452
	<u>1,859,336</u>	<u>-</u>	<u>-</u>	<u>1,859,336</u>
Total expenses	<u>2,624,304</u>	<u>-</u>	<u>-</u>	<u>2,624,304</u>
Postretirement benefit plan changes other than net periodic benefit cost	(155,284)	-	-	(155,284)
Change in net assets	967,521	999,357	259,371	2,226,249
Net assets				
Beginning of year	<u>7,654,741</u>	<u>6,999,920</u>	<u>8,132,774</u>	<u>22,787,435</u>
End of year	<u>\$ 8,622,262</u>	<u>\$ 7,999,277</u>	<u>\$ 8,392,145</u>	<u>\$ 25,013,684</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, 2016

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains and other support				
Congregation assessments	\$ 1,702,062	\$ -	\$ -	\$ 1,702,062
Gain on sale of real property	1,448,816	-	-	1,448,816
Net unrealized and realized losses on investments	789	(11,314)	-	(10,525)
Contributions	264,547	116,091	3,275	383,913
Income on long-term investments	72,302	338,736	-	411,038
Apartment and parking rentals	180,169	-	-	180,169
Income from assets held in trust by others	85,569	23,672	-	109,241
Net change in value of assets held in trust by others	-	-	25,864	25,864
Interest	389	-	-	389
Other	560	-	-	560
Net assets released from restrictions				
Satisfaction of program requirements	518,914	(518,914)	-	-
Total revenues, gains and other support	<u>4,274,117</u>	<u>(51,729)</u>	<u>29,139</u>	<u>4,251,527</u>
Expenses				
Ministry and Mission				
Diocesan initiatives	61,430	-	-	61,430
Congregational support	425,884	-	-	425,884
Discipleship	92,335	-	-	92,335
Outreach and justice	26,910	-	-	26,910
Ministry development	146,579	-	-	146,579
Other	70,061	-	-	70,061
	<u>823,199</u>	<u>-</u>	<u>-</u>	<u>823,199</u>
Diocesan Organization				
Episcopate	349,337	-	-	349,337
Bishop's staff	469,589	-	-	469,589
Diocesan expenses	812,069	-	-	812,069
Office building expenses	39,238	-	-	39,238
Travel	46,463	-	-	46,463
Other	85,559	-	-	85,559
	<u>1,802,255</u>	<u>-</u>	<u>-</u>	<u>1,802,255</u>
Total expenses	<u>2,625,454</u>	<u>-</u>	<u>-</u>	<u>2,625,454</u>
Postretirement benefit plan changes other than net periodic benefit cost	<u>(23,733)</u>	<u>-</u>	<u>-</u>	<u>(23,733)</u>
Change in net assets	<u>1,624,930</u>	<u>(51,729)</u>	<u>29,139</u>	<u>1,602,340</u>
Net assets				
Beginning of year	<u>6,029,811</u>	<u>7,051,649</u>	<u>8,103,635</u>	<u>21,185,095</u>
End of year	<u>\$ 7,654,741</u>	<u>\$ 6,999,920</u>	<u>\$ 8,132,774</u>	<u>\$ 22,787,435</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, 2017 and 2016

	2017	2016
Cash flows from operating activities		
Change in net assets	\$ 2,226,249	\$ 1,602,340
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities		
Net unrealized and realized losses (gains) on investments	(1,522,575)	10,525
Change in value of assets held in trust by others	(206,190)	(25,864)
Gain on sale of property	(916,794)	(1,448,816)
Bad debt expense	179,744	-
Contributions restricted to endowment	(53,181)	(3,275)
Change in receivables	127,148	22,816
Change in prepaid expenses and other	11,461	(2,269)
Change in accounts payable and other accrued expenses	(41,353)	52,118
Change in due to parishes and other organizations	21,469	(71,359)
Change in accrued postretirement benefit cost	147,474	15,389
Net cash provided by (used in) operating activities	<u>(26,548)</u>	<u>151,605</u>
Cash flows from investing activities		
Proceeds from sale of investments	38,218,500	44,363,979
Purchases of investments	(40,878,073)	(44,295,583)
Received from parishes for investment in investment pool	1,968,168	1,695,522
Parish withdrawals and distributions from investment pool	(1,407,606)	(1,961,282)
Loans issued to parishes, missions and other	(278,000)	-
Collection of loans receivable	515,962	399,254
Proceeds from sale of property	1,193,126	2,616,880
Property and equipment purchases	-	(1,168,064)
Net cash provided by (used in) investing activities	<u>(667,923)</u>	<u>1,650,706</u>
Cash flows from financing activities		
Notes payable borrowings	278,000	1,168,126
Payment of notes payable	(515,962)	(1,561,380)
Contributions to permanent endowment	53,181	3,275
Net cash used in financing activities	<u>(184,781)</u>	<u>(389,979)</u>
Net increase (decrease) in cash and cash equivalents	(879,252)	1,412,332
Cash and cash equivalents		
Beginning of year	<u>1,759,474</u>	<u>347,142</u>
End of year	<u>\$ 880,222</u>	<u>\$ 1,759,474</u>
Cash paid during the year for		
Interest	\$ 23,888	\$ 56,640

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

The Episcopal Church in Hawai'i

Notes to Financial Statements

December 31, 2017 and 2016

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 the investment pool are donor restricted. Unrestricted assets in this pool have been designated by the board to be held for long-term investment. Contributions and bequests receivable that are donor restricted for long-term investment are also reflected in this group of assets.

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.

Receivables

Accounts and loans receivable are stated at the amounts owed to the Church by parishes and third parties. Receivables older than 60 days are considered past due and placed on nonaccrual status. An allowance for doubtful accounts is established when needed based on management's judgments about the collectability of receivables. Uncollectible receivables are charged off when management determines the receivable will not be collected.

The Episcopal Church in Hawai'i

Notes to Financial Statements

December 31, 2017 and 2016

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.

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. This policy was revised to four percent beginning with fiscal 2018. 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 2017 or 2016.

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 may 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.

The Episcopal Church in Hawai'i

Notes to Financial Statements

December 31, 2017 and 2016

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 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 loans and mortgages obtained by the Church for the benefit of parishes. Proceeds of notes are advanced to the parishes and the Church recognizes a receivable for those amounts. Interest expense 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 asset 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.
- **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.

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.

The Episcopal Church in Hawai'i

Notes to Financial Statements

December 31, 2017 and 2016

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 represent a significant source of support to the Church and assessments from one particular parish are in excess of ten 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 \$90,000 in 2017 and \$89,000 in 2016. Also includes apartment building rental income from tenants.

Ministry and Mission

- Diocesan Initiatives – support for mission ministries
- Congregational Support – support to parishes and missions; audit oversight
- Discipleship – activities to develop spiritual and leadership programs and ministries relating to youth and young adults; diversity programs; native Hawaiian ministry programs; other new ministry; planned giving
- Outreach and Justice – support for A Cup of Cold Water (mobile outreach activities)
- Ministry Development – Curacy support; local ordination formation program; clergy conference
- Other – discretionary grants as approved by the Council; Bishop's emergency reserve

Diocesan Organizaion

- Episcopate - compensation, benefits and other support costs for the Bishop and his executive assistant
- Office of Bishop Staff - compensation, benefits and other support costs for all other personnel of the Office of the Bishop
- Diocesan expenses - general and administrative expenses related to the Diocese; includes an assessment paid to the National Church and the 8th Province and funds to support delegates to attend the General Convention
- Ault memorial office building expenses – office building repair and maintenance, cleaning, security, shared expenses
- Travel – for governance groups and staff
- Other – subsidies for health benefits of retired clergy and surviving spouses; property taxes for land held for a future congregation; support to a mission for lease rent expense; property development planning activities

The Episcopal Church in Hawai'i

Notes to Financial Statements

December 31, 2017 and 2016

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. The tax years ended 2016, 2015, and 2014 are still open to examination for both federal and state purposes.

Concentrations of Credit Risks

The Church's cash balances are held with two financial institutions. Each account is covered by FDIC or SIPC insurance (\$250,000 limit per institution). Cash balances at December 31, 2017 and 2016 were 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 2016 balances have been reclassified to conform to the 2017 presentation. These reclassifications had no impact on the change in net assets reported for 2016.

Subsequent Events Review

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 August 20, 2018, the date the financial statements were available to be issued.

2. Investments

The composition of investments is presented in Note 3. The return on investments for 2017 and 2016 was as follows:

	2017	2016
Interest and dividend income	\$ 515,771	\$ 562,389
Net unrealized and realized gains (losses)	1,522,575	(10,525)
Management fees and other costs	(184,402)	(151,351)
Total return on investments	<u>\$ 1,853,944</u>	<u>\$ 400,513</u>

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 issuers and industry groups. Additionally, the Church attempts to minimize market risk by diversifying its investments in common and preferred stock among various issuers and industry groups.

Investment Return Objectives

The Church's investment objective is to seek a return, which allows it to meet its spending policy, as well as provide inflation protection of its principal. Over the longer term, the objective is to earn a return of 8% per year with 4% being derived from income and the remaining 4% from capital appreciation. The investment pool will be invested in an appropriate manner to meet this objective.

The Episcopal Church in Hawai'i

Notes to Financial Statements

December 31, 2017 and 2016

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 there 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. Level 3 inputs also include assets held in perpetual trusts that cannot be redeemed by the organization as beneficiary.

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, 2017 and 2016.

Equity Securities: Common stock and publicly traded master limited partnerships 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 and other mutual funds: Valued at the closing price reported on active 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. These assets are classified as Level 3 pursuant to guidance issued by the American Institute of Certified Public Accountants, since the assets cannot be redeemed by the organization.

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Fair values of assets measured on a recurring basis are as follows as of December 31, 2017:

	Fair Value	Quoted Prices (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments				
Common stock				
Basic materials	\$ 1,012,740	\$ 1,012,740	\$ -	\$ -
Capital goods/industrials	862,667	862,667	-	-
Consumer goods	2,086,891	2,086,891	-	-
Energy	1,521,817	1,521,817	-	-
Financials	3,085,769	3,085,769	-	-
Health care	1,320,609	1,320,609	-	-
Technology/info com	3,201,692	3,201,692	-	-
Other	1,437,986	1,437,986	-	-
Total common stock	<u>14,530,171</u>	<u>14,530,171</u>	-	-
Preferred stock				
Capital goods	447,951	-	447,951	-
Consumer goods	79,453	-	79,453	-
Financials	3,269,912	-	3,269,912	-
Other	1,192,145	-	1,192,145	-
Total preferred stock	<u>4,989,460</u>	-	<u>4,989,460</u>	-
Master limited partnerships				
Energy	144,376	144,376	-	-
Utilities	101,277	101,277	-	-
Total limited partnerships	<u>245,653</u>	<u>245,653</u>	-	-
Convertible corporate notes	4,632,058	-	4,632,058	-
Corporate notes and bonds	7,449,263	-	7,449,263	-
U.S. government securities	4,833,158	-	4,833,158	-
Money market mutual funds	3,001,342	3,001,342	-	-
Accrued income and other	164,155	-	164,155	-
Total investments	<u>\$ 39,845,260</u>	<u>\$ 17,777,166</u>	<u>\$ 22,068,094</u>	<u>\$ -</u>
Assets held in trust by others	<u>\$ 2,398,282</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,398,282</u>

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Fair values of assets measured on a recurring basis are as follows as of December 31, 2016:

	Fair Value	Prices (Level 1)	Inputs (Level 2)	Inputs (Level 3)
Investments				
Common stock				
Basic materials	\$ 444,067	\$ 444,067	\$ -	\$ -
Capital goods/industrials	727,095	727,095	-	-
Consumer goods	1,782,698	1,782,698	-	-
Energy	1,156,474	1,156,474	-	-
Financials	2,407,586	2,407,586	-	-
Health care	1,353,434	1,353,434	-	-
Technology/info com	2,596,878	2,596,878	-	-
Other	523,179	523,179	-	-
Total common stock	<u>10,991,411</u>	<u>10,991,411</u>	<u>-</u>	<u>-</u>
Preferred stock				
Capital goods	655,020	-	655,020	-
Consumer goods	368,373	-	368,373	-
Financials	5,256,811	-	5,256,811	-
Other	1,218,519	-	1,218,519	-
Total preferred stock	<u>7,498,723</u>	<u>-</u>	<u>7,498,723</u>	<u>-</u>
Master limited partnerships				
Energy	732,587	732,587	-	-
Capital goods	128,983	128,983	-	-
Utilities	941,837	941,837	-	-
Total limited partnerships	<u>1,803,407</u>	<u>1,803,407</u>	<u>-</u>	<u>-</u>
Convertible corporate notes	3,792,628	-	3,792,628	-
Corporate notes and bonds	5,652,743	-	5,652,743	-
U.S. government securities	2,232,931	-	2,232,931	-
Money market mutual funds	1,645,544	1,645,544	-	-
Mutual funds - equity	102,775	102,775	-	-
Accrued income and other	157,418	-	157,418	-
Total investments	<u>\$ 33,877,580</u>	<u>\$ 14,543,137</u>	<u>\$ 19,334,443</u>	<u>\$ -</u>
Assets held in trust by others	<u>\$ 2,192,092</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,192,092</u>

Investments in 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:

Assets held in trust by others

December 31, 2017

Beginning balance	\$ 2,192,092
Gains or losses (realized and unrealized) included in changes in net assets	206,190
Contributions	-
Ending balance	<u>\$ 2,398,282</u>

December 31, 2016

Beginning balance	\$ 2,166,228
Gains or losses (realized and unrealized) included in changes in net assets available for benefits	25,864
Contributions	-
Ending balance	<u>\$ 2,192,092</u>

4. Property and Equipment

Property and equipment at December 31, 2017 and 2016 consisted of the following:

	2017	2016
Cluett apartments	\$ 96,963	\$ 96,963
Queen Emma roadway	124,221	124,221
Kapolei real property	2,644,928	2,644,928
Other	33,369	33,369
McCray/Canterbury house	-	276,332
	<u>\$ 2,899,481</u>	<u>\$ 3,175,813</u>

In June 2010, the Church acquired land in Kapolei, Hawai'i for the purpose of building a new parish property. Once the parish property is developed and placed into service, it is expected that the cost of this land will be transferred to the accounts of the new parish.

In April 2016, the Church acquired the real property associated with St. George's Episcopal Church. The Church sold this property to an unrelated third party in June 2016, netting a gain on sale of approximately \$1.4 million.

In 2017, the Church sold the McCray/Canterbury house for net proceeds of \$1,193,126, resulting in a net gain on the sale of \$916,794.

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5. Notes Payable and Loans Receivable

Notes payable at December 31, 2017 and 2016 consisted of:

	2017	2016
St. Peter's Church - \$350,000 note of which \$98,000 was undrawn at December 31, 2017. Interest only payments at 4.15% due monthly. Annual principal repayments of \$100,000 due beginning August 2019. \$64,590 repaid in 2017.	\$ 187,410	\$ -
Christ Church – \$271,629 note, payable in \$1,689 monthly installments including interest at 5.625%. Note was refinanced May 2017 with a principal amount of \$50,046, monthly payments of \$948 including interest at 4.92%, and maturity date of May 2022.	43,516	55,788
Holy Innocents Church – \$26,000 note, payable in \$205 monthly installments including interest at 4.92%, with a final payment of \$19,620 due at maturity in August 2022. Maturity date may be extended for five years provided the principal balance is paid down to \$10,500. Note was repaid in July 2018.	25,604	-
Camp Mokule'ia – \$517,000 note, payable in \$3,225 monthly installments including interest at 6.375%. Interest rate was adjusted in March 2017 to 4.375%. Certain camp real property was pledged as collateral. Note was due in February 2037 but was repaid in November 2017.	-	438,704
	<u>\$ 256,530</u>	<u>\$ 494,492</u>

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

Years ending	
2018	\$ 10,670
2019	46,620
2020	111,780
2021	64,450
2022	23,010
	<u>\$ 256,530</u>

Two of the above loan agreements contain restrictive covenants, including restrictions on making loans/investments to other parties, and on the incurrence of additional debt obligations.

The Church had previously provided loan guarantees on behalf of St. Mark's parish and Camp Mokule'ia. The Church was released from these guarantee obligations in 2017.

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In April 2016, the Church financed the purchase of the real property associated with St. George's Episcopal Church, borrowing \$1.2 million under a short term loan. This loan was repaid from the proceeds of the sale of this property, which occurred in June 2016.

All of the notes listed above were obtained by the Church for the purpose of loaning the proceeds to the indicated camp/parish, for their use in capital improvements. Loans receivable from parishes, missions and others on the statement of financial position are as follows:

	2017	2016
St. Peter's Church	\$ 187,410	\$ -
St. John the Baptist	134,727	134,727
St. John the Baptist	45,017	45,017
Christ Church	43,516	55,788
Holy Innocents Church	25,604	-
Church Investment Group	20,000	20,000
Camp Mokule'ia	-	438,704
	<u>456,274</u>	<u>694,236</u>
Less allowance for credit losses	(179,744)	-
	<u>\$ 276,530</u>	<u>\$ 694,236</u>

In developing the allowance for credit losses, management considers various credit quality indicators, primarily the debtor's cash flow and ability to service the loan. Loans receivable from St. John the Baptist are in delinquent status and collection in the near term is doubtful. For financial reporting purposes, an allowance for credit losses has been provided for these loans.

6. Pension Benefits

The Church participates in several multiemployer retirement plans which cover substantially all full-time clergy and lay employees of the Diocese. Contributions are determined as a percentage of each covered employee's salary. Pension expense for fiscal 2017 and 2016 amounted to the following:

Plan Name	Plan Type	2017	2016
The Church Pension Fund Clergy Pension Plan	DB	\$ 48,068	\$ 37,078
The Episcopal Church Lay Employees' Retirement Plan	DB	13,209	12,916
The Episcopal Church Lay Employees' Defined Contribution Retirement Plan	DC	33,435	36,664
		<u>\$ 94,712</u>	<u>\$ 86,658</u>

Plan types are either defined benefit ("DB") or defined contribution ("DC") plans.

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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 60% 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, 2017 and 2016 was:

	2017	2016
Accumulated postretirement benefit obligation	\$ (755,883)	\$ (608,409)
Fair value of plan assets	-	-
Funded status	<u>\$ (755,883)</u>	<u>\$ (608,409)</u>

As of December 31, 2017 and 2016, the accrued postretirement benefit liability recognized in the statements of position was \$755,883 and \$608,409, respectively. Assumptions used to determine the accumulated postretirement benefit obligation at December 31, 2017 and 2016 included:

	2017	2016
Discount rate	3.45%	3.87%
Health care cost trend rate over the next year	5.50%	5.50%
Ultimate health care cost trend rate	5.50%	5.50%
Retirement and withdrawal rates	Specific identification	

Mortality assumptions were based on the Retired Pensioners Mortality Tables (RP-2014) in 2016 and 2017. In 2017 the projection scale was projected generationally with Scale MP-2017 whereas in 2016 the Scale MP-2014 was utilized. The change in mortality assumption resulted in an increase in the benefit obligation of \$205,384 in 2017. This actuarial loss was partially offset by an actuarial gain pertaining to demographic experience of \$154,185.

Cash activity for the years ended December 31, 2017 and 2016 was as follows:

	2017	2016
Employer contributions	\$ 23,880	\$ 23,736
Participant contributions	29,280	29,304
Benefits paid	53,160	53,040

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Amounts recognized in the statements of activities for the years ended December 31, 2017 and 2016 were as follows:

	2017	2016
Amounts recognized in the statement of activities:		
Net loss (gain) arising during the period	\$ 139,740	\$ 7,912
Amortization of prior service credit and net gains	15,544	15,821
Total benefit changes other than net periodic benefit cost	155,284	23,733
Net periodic benefit cost	16,070	15,391
	<u>\$ 171,354</u>	<u>\$ 39,124</u>
Discount rate for interest cost component of benefit cost	3.87%	4.00%

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

	2017	2016
Unamortized actuarial losses	\$ 233,954	\$ 98,341
Unamortized prior service cost (credit)	(137,698)	(157,369)
	<u>\$ 96,256</u>	<u>\$ (59,028)</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. Fiscal 2018 amortization expense of unamortized actuarial losses is expected to be \$21,197. Fiscal 2018 amortization income of unamortized prior service cost (credit) is expected to be \$19,671.

The Church expects to contribute \$28,713 to the plan in 2018.

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
2018	\$ 28,713
2019	30,415
2020	31,162
2021	34,309
2022	35,013
2023 - 2027	184,673

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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, 2017:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor Restricted Endowments				
Episcopate	\$ -	\$ 2,541,064	\$ 1,684,231	\$ 4,225,295
Congregational development	-	15,398	6,392	21,790
Communication	-	13,708	6,023	19,731
Land and building	-	1,333,203	-	1,333,203
Loan fund	-	807,795	167,114	974,909
Support for missions	-	336,757	735,571	1,072,328
Other programs	-	1,554,173	663,810	2,217,983
Discretionary	-	1,194,983	2,779,845	3,974,828
	<u>-</u>	<u>7,797,081</u>	<u>6,042,986</u>	<u>13,840,067</u>
Other Endowments				
Board designated for endowment	5,410,116	-	-	5,410,116
Split interest agreements	6,945	35,248	-	42,193
Perpetual trusts	-	-	2,349,159	2,349,159
Subtotal endowment funds	<u>5,417,061</u>	<u>7,832,329</u>	<u>8,392,145</u>	<u>21,641,535</u>
Non-Endowments				
Operating fund	305,720	166,948	-	472,668
Property and equipment	2,899,481	-	-	2,899,481
	<u>3,205,201</u>	<u>166,948</u>	<u>-</u>	<u>3,372,149</u>
Total net assets	<u>\$ 8,622,262</u>	<u>\$ 7,999,277</u>	<u>\$ 8,392,145</u>	<u>\$ 25,013,684</u>

Changes in endowment net assets for the year ending December 31, 2017 were as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Funds, January 1, 2017	\$ 2,839,167	\$ 6,832,473	\$ 8,132,774	\$ 17,804,414
Interest and dividends, net of investment expense	77,879	253,490	-	331,369
Net realized/unrealized gains (losses)	352,126	1,170,449	-	1,522,575
Contributions	2,232,981	51,257	53,181	2,337,419
Amounts appropriated for expenditure	(85,092)	(475,340)	-	(560,432)
Increase in value of perpetual trusts	-	-	206,190	206,190
Endowment Funds, December 31, 2017	<u>\$ 5,417,061</u>	<u>\$ 7,832,329</u>	<u>\$ 8,392,145</u>	<u>\$ 21,641,535</u>

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Endowment and non-endowment net assets consisted of the following at December 31, 2016:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor Restricted Endowments				
Episcopate	\$ -	\$ 2,300,637	\$ 1,684,231	\$ 3,984,868
Congregational development	-	14,150	6,392	20,542
Communication	-	12,581	6,023	18,604
Land and building	-	1,159,350	-	1,159,350
Loan fund	-	709,189	167,114	876,303
Support for missions	-	275,726	735,571	1,011,297
Other programs	-	1,356,811	610,629	1,967,440
Discretionary	-	968,781	2,779,845	3,748,626
	-	6,797,225	5,989,805	12,787,030
Other Endowments				
Board designated for endowment	2,832,222	-	-	2,832,222
Split interest agreements	6,945	35,248	-	42,193
Perpetual trusts	-	-	2,142,969	2,142,969
Subtotal endowment funds	2,839,167	6,832,473	8,132,774	17,804,414
Non-Endowments				
Operating fund	1,639,761	167,447	-	1,807,208
Property and equipment	3,175,813	-	-	3,175,813
	4,815,574	167,447	-	4,983,021
Total net assets	\$ 7,654,741	\$ 6,999,920	\$ 8,132,774	\$ 22,787,435

Changes in endowment net assets for the year ended December 31, 2016 were as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Funds, January 1, 2016	\$ 2,580,380	\$ 6,908,246	\$ 8,103,635	\$ 17,592,261
Interest and dividends, net of investment expense	72,302	338,736	-	411,038
Net realized/unrealized gains (losses)	789	(11,314)	-	(10,525)
Contributions	279,215	58,070	3,275	340,560
Amounts appropriated for expenditure	(93,519)	(461,265)	-	(554,784)
Increase in value of perpetual trusts	-	-	25,864	25,864
Endowment Funds, December 31, 2016	\$ 2,839,167	\$ 6,832,473	\$ 8,132,774	\$ 17,804,414

Interpretation of HUPMIFA

The governing board (Council) of the Church, in consultation with legal counsel, has interpreted Hawaii's Uniform Management of Institutional Funds Act (HUPMIFA) 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

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those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by HUPMIFA, and upon satisfaction of any purpose restrictions on the fund.

9. Unconsolidated Entities

Generally accepted accounting principles establish 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 three entities meet the criterion for consolidation: St. Andrew's Schools, Camp Mokule'ia, and A Cup of Cold Water. 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.

Summarized financial information for these entities has not been provided as audited financial statements are not available.

10. Litigation

In 2016, the Church was named as a co-defendant in a lawsuit. This matter was resolved in 2016.