**September 6, 2006**

# Diocesan Reserves Explained

News reports have made reference to the significant reserves the Diocese of Rockville Centre has, claiming that it has more than it reasonably needs. This conclusion is reached by adding together funds from various diocesan reports and compares them to a portion of the annual need.

The diocesan entities have several types of funds. Some of the funds contained in the reports are restricted funds and cannot be used for any other purpose. Other funds have been designated to meet a specific purpose. Appropriately, the Bishop has no intention of invading these funds or using them for other purposes.

An understanding of the question of the adequacy of reserves requires an understanding of the size and complexity of the diocesan entities as well as the current and anticipated future financial condition of the diocese.

There are approximately 1.4 million Catholics within the Diocese of Rockville Centre, which is nearly one-half of the entire population of Long Island. There are 134 parishes located in 115 towns. Last year, there were approximately 20,000 baptisms, 18,000 confirmations, 20,000 first communions and 5,000 marriages in the diocese.

There are approximately 38,000 students enrolled in the 76 Catholic elementary and high schools in the diocese. Annually, the diocese educates over 150,000 children and young adults in the Catholic faith through its religious education program. Catholic Charities provided services to approximately 59,000 people at 60 sites throughout Long Island. The diocesan health care ministry organized under Catholic Health Services (CHS) serves literally hundreds of thousands of people each year in five hospitals, three nursing homes, a regional home care and hospice network and a community-based agency for persons with special needs. These statistics represent only a portion of the work of the diocese. What is clear is that thousands of people work and volunteer in diocesan entities that impact the lives of countless people on Long Island.

## The Need for Reserves

Non-profit organizations do not have capital contributed by shareholders and their need for reserves is dependent upon the predictability of future income and expenses. The Church is heavily dependent upon the generosity of its people and the ability to control costs. While total revenue has increased in the last ten years, it is the result of fewer contributors making larger donations. This, coupled with recent increases in insurance costs, employment costs and energy prices continue to significantly impact diocesan operations. Reserves are needed and used to cushion this impact as best as can be foreseen. The diocese uses reserves to moderate insurance premium increases, cushion the increase in other costs and generate investment income, which provides funding for programs.

Reserves are ordinary and necessary provisions for future needs and both anticipated and unanticipated future obligations. Organizations need reserves, just as a family needs personal savings to cushion for emergencies and to meet expected obligations such as college expenses and to supplement retirement. Many not-for-profit organizations have generated significant investment portfolios, which operate as quasi-endowment funds (i.e. funds that maintain or increase their balance while using investment income for current needs). In the case of the Diocese of Rockville Centre this income has been necessary to balance the budget for the entire decade.

Reserves are essential to ably meet the many challenges faced by the diocese. For instance, due to the explosive population growth in the suburbs in the 1950s and 1960s, many parish buildings were built at the same time and are of an age where major repairs and renovations are needed. In Suffolk, surges in population growth are placing new demands on existing parish plants and will require enhancement to serve the Catholic population in these areas. In fact, expansion may need to take place in areas currently underserved by the church. This will require funding.

Catholic schools serve a significant population but rising school expenses and the high cost of living on Long Island result in increased tuition making the schools too costly an option for many. Rising employment costs, including the cost of fringe benefits, create additional pressures on budgets. We have yet to feel the full impact of escalating energy costs.

**Diocesan High Schools** The diocese operates three high schools: Holy Trinity, St. John the Baptist and McGann-Mercy. For the year ended June 30, 2005, 3,589 students attended these schools and 741 graduated. The financial statements evidence the significant commitment of the diocese to this important ministry. For fiscal 2005, the schools received $2 million in subsidies. It cost almost $31 million to operate the three schools last year. Tuition (net of student aid) covers approximately two thirds of the cost. Diocesan subsidy, fees, ancillary revenue and development efforts make up the balance.

In addition to the subsidy, there is an unfunded financial deficit for the three schools of $2.4 million as of June 30, 2005. Further, a recent study commissioned by the diocese indicates substantial capital repairs are needed at each of the facilities. We need to secure additional funding to meet these needs.

**Seminary of the Immaculate Conception** The seminary is dedicated to the formation of men studying for the priesthood and ongoing clergy formation. The seminary provides support for our deacons and priests who have dedicated their lives to the Church. The seminary is a leading provider of theological education for lay people and Religious through the Masters in Theology and Doctor of Ministry programs. In addition the seminary hosts scores of other Diocesan related events.

In fiscal 2005 the seminary received $1.5 million in subsidy, covering approximately 40 percent of its cost. Although blessed with a beautiful facility, the seminary has many financial challenges including the maintenance of its 77-year-old plant. Considering the size of the institution, the seminary has modest financial reserves with endowment funds (only the investment income can be used) of $927,000, other restricted funds (restricted for student aid, capital improvements and technology) of $581,000 and designated funds (interest currently used for operations, principal could be used for capital) of $783,000. We need additional funds to address many of the capital needs.

**Catholic Cemeteries** The diocese currently operates three Catholic Cemeteries (Holy Rood in Westbury, Queen of All Saints in Central Islip and Holy Sepulchre in Coram) and plans to open a new cemetery (Our Lady Queen of Peace in Old Westbury).

Income is derived from the sale of graves and crypts as well as burial fees and investment income. With the sale of each grave or crypt, Catholic Cemeteries accepts an obligation to maintain the site in perpetuity. Since burial space is finite (Holy Rood, in particular, has virtually no remaining graves to sell), it is imperative that funds be earmarked for the future care of these cemeteries. In the future, income from sales and operations will not be adequate to cover the costs necessary to maintain these sacred places. When Catholic Cemeteries began building mausoleums it followed a similar practice earmarking a portion from the sale of each crypt and placing it in a fund, which would generate future income to maintain the buildings. Management regularly reviews all of these funds updating projections to make certain that they will remain adequate.

Of the $121.4 in net assets at August 31, 2005, $92.5 million represents funds set aside for future care ($55.2 million restricted and $37.3 million designated) and $28.9 million represents funds available for current operations. Of this $28.9 million, $15.5 million is invested in land, buildings and equipment. The remaining funds of $13.5 million are needed for working capital, new building projects at the three currently operating cemeteries and the development of the new cemetery in Old Westbury.

If we continue our current policies we should have adequate funds in the future without placing an undue burden on the other diocesan funding sources.

**Catholic Press Association (*The Long Island Catholic*)** The Catholic Press Association publishes the diocesan weekly newspaper *The Long Island Catholic,* which has a circulation of approximately 108,000 subscribers. For the fiscal year ended August 31, 2005, an operating loss of $138,000 was incurred. Investment income offset this loss and provided a small overall profit of $15,000. The newspaper's largest source of operating revenue is the subscription income from the parishes, which represents 56 percent of the operating budget. The Association maintains a reserve to provide investment income, which helps to keep subscription rates lower than would otherwise be necessary. As of August 31, 2005 the Association has net assets of $2.5 million of which $2.0 million is invested in Unitas, Inc and the rest is in non-cash assets (accounts receivable and fixed assets). These funds are needed to provide working capital to operate.

**Telecare** This is the diocesan owned/operated television station, provides educational programming for the diocesan elementary schools and religious programming for a cable channel available throughout Long Island. Many of the programs are produced in house while others are acquired through arrangements with other religious television stations.

For the fiscal year ended August 31, 2005,the station's expenses exceeded revenue by $932,000. During the fiscal year, a significant revenue source did not materialize, leaving the station without the full amount of estimated funding that had been budgeted. As a result the station had to borrow funds from the Diocesan Loan Account to meet its expenses. It is anticipated that additional revenue in 2006 will enable Telecare to repay this indebtedness and meet its budgeted operating costs.

The future funding of Telecare is dependent upon its revenue sources.

**Unitas Investment Fund Inc.** was established in June, 2005 to provide opportunities for diocesan entities to invest in harmony with the teachings of the Church. The year ended August 31, 2005, its first full year of operation, was very successful. As of year-end, deposits totaled $335.6 million. For each of the investment alternatives, a benchmark has been established based on the type of investment and the styles of the managers selected. In the fiscal year ended August 31, 2005, four out of the five funds exceeded their benchmarks.

All of the funds in Unitas belong to parishes, schools and other diocesan entities. This is a worthwhile endeavor that helps all participants earn a more favorable rate of return than could be achieved by investing separately assuming the same level of risk.

**Protected Self-Insurance Program (PSIP)** The diocese administers this program for the self-indemnification of property and casualty losses, workers' compensation and auto liability of participating parishes, health facilities, institutions and organizations within the diocese. PSIP also has an Uninsured Perils Fund which is used to fund the safe environment program including the Office for the Protection of Children and Young People, the required criminal background screenings of all Church personnel and volunteers, and the required Virtus training program. As of August 31, 2005, the program had net assets of $56.5 million, a decrease of $2.1 million since last year.

Although the program has significant net assets, it has significant exposures as well. In order to be a financially sound insurer of these risks it needs considerable capital. In addition the Insurance Board is preparing to expand coverage in certain areas. Finally additional funds will be needed to pay for the safe environment program when the Uninsured Perils funds are depleted. The balances in this fund are adequate to cover all these items. Should these funds not be needed they would be returned to the participating entities or used to reduce future premiums.

**Ecclesia Assurance Company** was created in 2003 as a New York State captive insurance company. The diocese wholly owns Ecclesia which provides insurance on a direct basis to diocesan parishes, high schools, hospitals, and other diocesan entities. Ecclesia maintains adequate capital funding to meet its regulatory and liquidity requirements.

**Diocesan Services Inc.** engages in the brokering of insurance for ecclesiastical entities of the diocese. In its early years most of the diocesan insurance policies were purchased through this entity. In recent years, it has been used to obtain student accident insurance and other related insurance coverage. In the fiscal year ended August 31, 2005 the corporation earned a modest profit of $15,000. It has equity of $143,000. These funds are adequate for the purpose served by this entity.

**The Health Insurance Program** administered by the diocese provides health coverage, dental insurance, life insurance and disability benefits for clergy and lay employees of the various parishes, schools and other diocesan entities. Many entities are not in a position to be retroactively charged for a shortfall, so reserves are maintained to moderate bad claim experience. The program has net assets of $6 million. These funds are adequate for needed working capital, to stabilize premiums and to cushion the self-insurance exposure.

**Catholic Charities** has $19.9 million in designated fund balance at December 31, 2005. These funds came from bequests, proceeds of property sales, and investment income. The Board of Catholic Charities designated these funds to be used as a quasi endowment fund for Catholic Charities programs in keeping with the intention of the initial bequest. Catholic Charities relies on a portion of the annual earnings of this fund to meet its budget, as many governmental subsidies are being cut and there are many vulnerable people who rely on these services. The Board of Catholic Charities carefully monitors the level of reserves balancing current and future needs.

**Propagation of the Faith and Mission Office** is a member of the National Society for the Propagation of the Faith. Its goal is to provide financial and spiritual support of missionaries and their work. The funds raised by this arm of the diocese are remitted directly to the national mission office, to various missions and missionaries, or reinvested in the expansion of their services.

**The Mission Assistance Fund** was part of the Diocesan Administrative Offices in 2005. With net assets of $26.4 million, the fund is intended to be the primary lender of inter-diocesan loans in future years. At the close of 2005, the diocese owed the Fund $5.6 million for acquisition costs on future parish sites, and parishes had borrowed $10.5 million for capital and operating purposes. In fiscal 2006, the new Mission Assistance Corp. began to assume responsibility for the related assets and lending activities of the Fund.

There are approximately 16 parishes in arrears on their operating bills, and Mission Assistance provides assistance in the form of low interest loans and grants. Of significant concern is that almost half of the parishes had operating deficits in each of the last two years (66 in fiscal 2004 and 60 in fiscal 2005).

**Diocesan Administrative Offices** The centrally administered programs/departments of the Diocesan Pastoral Center are categorized in the areas of Pastoral Services, Educational Services, Health and Social Services, Religious Personnel Development and Administration. Many core ministries of the Church are included among those managed by the Pastoral Center Offices. Funds from the administrative offices also provide subsidies to the three high schools, Catholic Charities, the seminary and the diocesan television station, Telecare.

For the year ended August 31, 2005, the Administrative Offices suffered a decline in net assets of $1.1 million. As of August 31, 2005, the Administrative Offices had unrestricted net assets of $70.1 million. These funds are made up of four components: Plant and other properties - $11.3 million, Designated Funds - $37.8 million, Undesignated Fund deficit - $4.5 million, and Mission Assistance Fund - $26.4 million. Mission was described above; the others are clarified here.

- **Plant and Other Properties**- This represents the amount of funds invested in fixed assets (i.e. operating properties, plant and equipment) as well as properties held for future operating sites.

- The **Designated Funds** ($37.8 million) Most of these funds function as Quasi endowment funds providing a stream of income to fund the operating and capital budgets. Each year an estimate of the investment earnings is made in determining the overall revenue for the diocesan budget. Without this investment income, there would not be adequate funding for the diocesan programs currently underway. These funds could be used for any diocesan needs. They have been designated to function like endowment funds but the principal could be used if needed.

- **Undesignated fund deficit**- $4.5 million This represents the excess of expenses over revenues accumulated over the last few years. The deficit will be addressed in 2006 by transferring funds from the designated funds.

*Total Net Assets of diocesan entities include permanently restricted funds (endowments) and temporarily restricted funds (terms of use set by donors or contractual agreement.) Unrestricted net assets include property (such as cemeteries), buildings and equipment, as well as special purpose designation and unrestricted funds. The latter two categories are itemized below:*

| ***Diocesan Institutions, $ in 000's*** | ***Special Purpose Designation*** | **Notes** | ***Unrestricted & Undesignated*** | **Notes** |
|---|---|---|---|---|
| DIOCESAN HIGH SCHOOLS | *$0* | | *($2,358)* | **a** |
| SEMINARY OF THE IMMACULATE CONCEPTION | *783* | **b** | *85* | **b** |
| CATHOLIC CEMETERIES | *37,286* | **c** | *13,465* | **d** |
| CATHOLIC PRESS ASSOCIATION | *0* | | *2,220* | **e** |
| TELECARE | *0* | | *(750)* | **f** |
| DIOCESAN INSURANCE PROGRAMS | *64,871* | **g** | *142* | **g** |
| CATHOLIC CHARITIES | *19,883* | **h** | *4,117* | **h** |
| PROPAGATION OF THE FAITH & MISSION OFFICE | *970* | **i** | *0* | |
| MISSION ASSISTANCE FUND / DIOCESAN DEPOSIT & LOAN ACCOUNT | *26,368* | **j** | *0* | |
| DIOCESAN ADMINISTRATIVE OFFICES & PASTORAL CENTER | *37,780* | **k** | *(4,469)* | **l** |
| *UNRESTRICTED NET ASSETS, OTHER THAN PLANT* | *$187,941* | | *$12,452* | |

**Notes**

a. Despite operating subsidies of $2 million, schools ended 2005 with a cumulative deficit of $2.4 million.

b. Funds set aside to address capital improvement and operating needs in fiscal 2006 and future years.

c. Income from designated funds support perpetual care for older cemeteries and mausoleums.

d. Principal and income used to support development of new cemeteries and current operations.

e. Principal and income provide working capital for operations and equipment upgrades.

f. Deficit spending in anticipation of future revenue funded from Diocesan loans.

g. Diocesan-owned and operated insurance programs include Health Insurance Program (for employee health benefits); Protected Self Insurance Program (for casualty, property, workers' compensation & automobile coverage); Diocesan Service Inc. (brokerage); and Ecclesia (reinsurance). Insurance investments provide funds to meet capital requirements and liquidity for claims, deductibles, uninsurable losses, and loss prevention initiatives. Investment income and principal are used to stabilize premiums.

h. Quasi-endowment created from a generous bequest provides long-term support of Charities. Liquidity from this and other sources also meet debt covenant requirements and provide flexibility to meet government grant reimbursement limitations.

i. Funds are for pastoral work in the missions.

j. Funds are committed to provide low interest loans and grants to parishes and Diocesan entities, on a short-term basis for emergency operating needs and on a long-term basis for capital and programmatic enhancements.

k. Invested amounts provide programmatic funding stability and income to subsidize operating budget. Some assets are reserved for future parish site development and others are short-term receivables.

l. Diocesan operations and pastoral services operated at a loss in 2005 by borrowing internally.

**Conclusion**

The Diocese of Rockville Centre has true discretionary funds in reserve that can be used for cross funding other diocesan entities if and when necessary. These discretionary funds are found in the diocesan administrative offices and pastoral center budget and amount to the combination of funds with special purpose designation ($37,780,000) less the carry forward deficit ($4,469,000). These are the only central diocesan funds that can be tapped to address needs in other entities. Hence true discretionary funds amounts to $33.31 million.

As noted earlier, however, the diocese seeks to invest these funds to yield income supporting its mission and to make principal expenditures only when it best serves the balanced needs of all of the Catholic entities it supports. Without these funds, the diocese would have to cut back on levels of serves in almost every diocesan entity.

As the diocese has done in the past, it will continue to communicate how and to what extent it is carrying out its mission within the framework of transparent and open financial disclosure.