



Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office

Financial Report (Reviewed)
June 30, 2016

Contents

| | |
|--------------------------------------|------|
| Independent accountant's report | 1-2 |
| <hr/> | |
| Financial statements | |
| Statements of financial position | 3 |
| Statements of activities | 4 |
| Statements of changes in net deficit | 5 |
| Notes to financial statements | 6-10 |



RSM US LLP

Independent Accountant's Review Report

The Most Reverend Bishop James V. Johnston
Catholic Diocese of Kansas City—St. Joseph
Diocesan Insurance Office
Kansas City, Missouri

We have reviewed the accompanying statements of financial position of the Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office (the Office) as of June 30, 2016 and 2015, the related statements of activities and changes in net deficit for the years then ended, and the related notes to the financial statements. A review includes primarily applying analytical procedures to management's financial data and making inquiries of the Office management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, we do not express such an opinion.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the 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.

Accountant's Responsibility

Our responsibility is to conduct the reviews in accordance with Statements on Standards for Accounting and Review Services promulgated by the Accounting and Review Services Committee of the American Institute of Certified Public Accountants. Those standards require us to perform procedures to obtain limited assurance as a basis for reporting whether we are aware of any material modifications that should be made to the financial statements for them to be in accordance with accounting principles generally accepted in the United States of America. We believe that the results of our procedures provide a reasonable basis for our conclusion.

Accountant's Conclusion

Based on our reviews, except for the issue noted in the Known Departure From Accounting Principles Generally Accepted in the United States of America paragraph, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in accordance with accounting principles generally accepted in the United States of America.

Known Departure From Accounting Principles Generally Accepted in the United States of America

Statements of cash flows for the years ended June 30, 2016 and 2015, have not been presented. Accounting principles generally accepted in the United States of America require that such statements be presented when financial statements purport to present financial position and results of activities of the organization.

Other Matter

The accompanying financial statements have been prepared assuming that the Office will continue as a going concern. As discussed in Note 7 to the financial statements, the Office has suffered recurring losses, and total liabilities exceed its total assets. These conditions indicate that the Office may be unable to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Management's plans in regard to address these matters are discussed in Note 7.

RSM US LLP

Kansas City, Missouri
November 21, 2016

Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office

Statements of Financial Position

June 30, 2016 and 2015

See Independent Accountant’s Review Report

| | 2016 | 2015 |
|---|-------------------|-------------------|
| Assets | | |
| Current assets: | | |
| Cash | \$ 20,073 | \$ 32,470 |
| Prepaid premiums | 59,295 | 40,194 |
| Accounts receivable (Note 2) | 387,114 | 311,674 |
| Total current assets | 466,482 | 384,338 |
| Office equipment | 41,242 | 41,242 |
| Less accumulated depreciation | (41,242) | (41,242) |
| | - | - |
| Investments (Note 5): | | |
| Deposits with Catholic Diocese of Kansas City—St. Joseph | 135,899 | 117,803 |
| Investments, National Catholic Risk Retention Group Stock | 1,693 | 1,693 |
| | 137,592 | 119,496 |
| | \$ 604,074 | \$ 503,834 |
| Liabilities and Net (Deficit) | | |
| Current liabilities: | | |
| Auto premium reserve | \$ 121,772 | \$ 144,580 |
| Claims and expenses payable (Note 4) | 1,774,092 | 2,348,497 |
| Claims and expenses—self-funded health insurance (Note 6) | 513,525 | 587,463 |
| Total current liabilities | 2,409,389 | 3,080,540 |
| Notes payable to Diocese | 7,503,937 | 8,458,626 |
| Claims incurred but not reported | 3,124,737 | 2,856,546 |
| Total long-term liabilities | 10,628,674 | 11,315,172 |
| Unrestricted net deficit | (12,433,989) | (13,891,878) |
| | \$ 604,074 | \$ 503,834 |

See notes to financial statements.

Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office

Statements of Activities

Years Ended June 30, 2016 and 2015

See Independent Accountant's Review Report

| | 2016 | 2015 |
|--|---------------------|---------------------|
| Revenues: | | |
| Premium income: | | |
| Clergy benefits | \$ 1,453,826 | \$ 1,272,133 |
| Lay employee benefits | 7,748,999 | 7,681,845 |
| Property and casualty program | 5,870,013 | 5,314,073 |
| Other revenue from operations: | | |
| Other | 18,881 | 11,041 |
| Recovery from excess insurer | 9,314 | 624,732 |
| Total operating revenues | 15,101,033 | 14,903,824 |
| Investment income | 2,494 | 20,205 |
| Contribution from Chancery Operation | 568,213 | 1,000,000 |
| Total revenues | 15,671,740 | 15,924,029 |
| Expenses: | | |
| Operating expenses: | | |
| Benefit expense: | | |
| Clergy benefits | 1,090,448 | 1,092,818 |
| Lay employee benefits | 8,608,331 | 7,386,923 |
| Property and casualty expense: | | |
| Administration | 1,819,932 | 1,927,749 |
| Insured and uninsured claims | 1,618,982 | 3,056,873 |
| Office administration | 523,779 | 502,494 |
| Interest | 284,188 | 233,300 |
| Total operating expenses | 13,945,660 | 14,200,157 |
| Increase in incurred but not reported claims | 268,191 | 529,173 |
| Total expenses | 14,213,851 | 14,729,330 |
| Net revenues over expenses | \$ 1,457,889 | \$ 1,194,699 |

See notes to financial statements.

Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office

**Statements of Changes in Net Deficit
Years Ended June 30, 2016 and 2015
See Independent Accountant’s Review Report**

| | 2016 | 2015 |
|----------------------------|-------------------------------|------------------------|
| Unrestricted net deficit: | | |
| Beginning of year | \$ (13,891,878) | \$ (15,086,577) |
| Net revenues over expenses | 1,457,889 | 1,194,699 |
| End of year | <u>\$ (12,433,989)</u> | <u>\$ (13,891,878)</u> |

See notes to financial statements.

Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office

Notes to Financial Statements

See Independent Accountant's Review Report

Note 1. Nature of Organization and Significant Accounting Policies

Nature of organization: In January 1, 1975, the Catholic Diocese of Kansas City—St. Joseph (the Diocese) established a self-insurance program for property and casualty insurance coverages. Under this plan, the Diocese self-insures the property and casualty coverages (except for boiler insurance, which is a deductible program) for all diocesan parishes, schools, early childhood centers, Catholic Cemeteries Association, Catholic Charities of Kansas City—St. Joseph, and other diocesan institutions. The self-insurance programs provide coverage for buildings, machinery and equipment, boiler, workers' compensation, automobile, student accident, comprehensive general liability, fiduciary liability, professional liability, sexual misconduct liability and cyber liability. The program includes a limit on each claim payable by the Diocese. Claims in excess of the self-insured retention are insured by licensed insurance carriers. Under the program, the Diocese contract for the administration of claims, appraisals, and loss control and prevention services. The Diocesan Insurance Office coordinates the placement of coverage, payment of claims and premiums with insurance companies and service providers.

In addition to the self-insurance coverages, the Diocesan benefits office administers the clergy and lay employee benefit programs, which include pension, life insurance, short-term disability, long-term disability, health care insurance, voluntary dental care, voluntary supplemental life insurance, flexible spending accounts, health savings accounts, long-term care (clergy), and supplemental medical reimbursement (clergy).

Premiums for the self-insurance property and casualty coverages are based on loss cost factors published for the state of Missouri by the Insurance Services Office, a national rating organization, then multiplied by an industry experience factor and discounted by the Diocese according to the current claims experience for each type of coverage. Premiums are collected by the Diocesan office and used to pay claims as they are incurred. Premiums for insured coverages are collected by the Diocese from all entities of the Catholic Diocese of Kansas City—St. Joseph, Catholic Cemeteries Associated of Kansas City—St. Joseph, and Catholic Charities of Kansas City—St. Joseph.

The financial statements of the Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office (the Office) have been prepared in accordance with accounting principles and reporting practices for churches and church-related organizations, adopted by the National Conference of Catholic Bishops. The accounting principles promulgated by the above conference do not differ in any material respects from accounting principles generally accepted in the United States of America.

A summary of the Office's significant accounting policies follows:

Basis of presentation: Financial statement presentation follows the recommendations of the *FASB Accounting Standards Codification* (ASC) 958, Not-for Profit Entities. Under ASC 958, the Office is required to report its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets and permanently restricted net assets.

The services performed by the Diocesan Insurance Office are not necessarily required by the operation of the Diocesan administrative offices and could be contracted out to others, or administered by the Diocese as an auxiliary service.

Revenue recognition: The Office recognizes premiums and reimbursements as revenue as they are earned.

Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office

Notes to Financial Statements

See Independent Accountant's Review Report

Note 1. Nature of Organization and Significant Accounting Policies (Continued)

Fair value of financial instruments: Financial instruments are described as cash and cash or contractual obligations or rights to pay or receive cash. The fair value of certain financial instruments approximates the carrying value because of the short-term maturity of the instruments, which include cash, accounts receivable, investments (deposits with Catholic Diocese of Kansas City—St. Joseph and National Catholic Risk Retention Group stock), accounts payable, accrued expenses and other current liabilities.

Accounts receivables: Accounts receivables are carried at original invoice amount less an estimate made for doubtful receivables based on a review of all outstanding amounts on a monthly basis. Management determines the allowance for doubtful accounts by regularly evaluating individual customer receivables and considering a customer's financial condition, credit history and current economic conditions. Trade receivables are written off when deemed uncollectible. Recoveries of trade receivables previously written off are recorded when received.

An account receivable is considered to be past due if any portion of the receivable balance is outstanding for more than 90 days. Interest is not charged on trade receivables.

Office equipment: Office equipment is carried at cost or, if donated, at the approximate fair value at the date of donation. Major renewals and betterments are capitalized, and maintenance and repairs which do not improve or extend the life of the respective assets are charged against net assets in the current period. Depreciation is computed using the straight-line method over the useful lives of the assets, ranging from three to five years.

Use of estimates: The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain 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 revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates subject to change in the near term include claims incurred but not reported.

Claims incurred but not reported: Claims incurred but not reported have been estimated using information provided by the claims administrator, who used factors taken from industry-wide data supplied to insurance companies.

Note 2. Accounts Receivable

Accounts receivable consisted of the following at June 30:

| | 2016 | 2015 |
|--|-------------------|-------------------|
| Automobile and school bus premiums—priests and parishes | \$ 121,611 | \$ 141,335 |
| Property and casualty premiums—parishes and institutions | 214,517 | 167,597 |
| Other | 50,986 | 2,742 |
| | <u>\$ 387,114</u> | <u>\$ 311,674</u> |

Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office

Notes to Financial Statements

See Independent Accountant's Review Report

Note 3. Income Taxes

The Office is exempt from income taxes under provisions of section 501(c)(3) of the Internal Revenue Code due to its religious affiliation through the Catholic Diocese of Kansas City—St. Joseph and its inclusion in the Catholic Register. Uncertain tax provisions, if any, are recorded in accordance with FASB ASC 740, Income Taxes (previously FIN 48). FASB ASC 740 requires the recognition of a liability for tax positions taken that do not meet the more-likely-than not standard that the position will be sustained upon examination by the taxing authorities. There is no liability for uncertain tax positions recorded at June 30, 2016 or 2015.

Note 4. Commitments

In connection with pending first-party and third-party claims, the Office financial statements include accruals of a liability of \$1,774,092 and \$2,348,497 as of June 30, 2016 and 2015, respectively. The first-party claims are property damage claims asserted by insured parishes. The third-party claims are liability claims brought by third parties asserting workers' compensation, property damage and personal injury claims, including sexual misconduct claims.

Additional sexual misconduct or other claims, which may or may not be timely, may be filed in the future. If there are any such additional claims, the Office expects that it will incur future charges related to the defense of such matters but cannot reasonably estimate the potential costs it will incur or the future reimbursements it may receive.

Payments made to satisfy the loss contingency could have a material impact on the Catholic Diocese and the Office and, in the future, could impact the activities, programs and ministries of the Administrative Office it provides for parishes and schools in the Catholic Diocese.

Note 5. Fair Value Measurements

The Office has adopted the provisions of FASB ASC 820, Fair Value Measurements and Disclosures, for assets measured at fair value. FASB ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. FASB ASC 820 requires the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. In that regard, FASB ASC 820 establishes fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

Level 1: Inputs are quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs are inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office

Notes to Financial Statements

See Independent Accountant’s Review Report

Note 5. Fair Value Measurements (Continued)

Level 3: Significant unobservable inputs are inputs that reflect a reporting entity’s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

A description of the valuation methodologies used for assets on a recurring basis is set forth below.

If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, or discounted cash flow. Level 2 securities would include U.S. agency securities, mortgage-backed agency securities, obligations of states and political subdivisions, and certain corporate, asset-backed and other securities. In certain cases where there is limited activity or less transparency around inputs to the valuation including alternative investments, securities are classified within Level 3 of the valuation hierarchy.

The following tables summarize the assets measured at fair value on a recurring basis, segregated by the general classification of such instruments pursuant to the valuation hierarchy:

| | June 30, 2016 | | | |
|--|-------------------|-------------|-------------------|-----------------|
| | Total | Level 1 | Level 2 | Level 3 |
| Investments: | | | | |
| Deposits with Catholic Diocese of Kansas City—St. Joseph | \$ 135,899 | \$ - | \$ 135,899 | \$ - |
| National Catholic Risk Retention Group Stock | 1,693 | - | - | 1,693 |
| | <u>\$ 137,592</u> | <u>\$ -</u> | <u>\$ 135,899</u> | <u>\$ 1,693</u> |

| | June 30, 2015 | | | |
|--|-------------------|-------------|-------------------|-----------------|
| | Total | Level 1 | Level 2 | Level 3 |
| Investments: | | | | |
| Deposits with Catholic Diocese of Kansas City—St. Joseph | \$ 117,803 | \$ - | \$ 117,803 | \$ - |
| National Catholic Risk Retention Group Stock | 1,693 | - | - | 1,693 |
| | <u>\$ 119,496</u> | <u>\$ -</u> | <u>\$ 117,803</u> | <u>\$ 1,693</u> |

The fair value of investments categorized as Level 3 investments was \$1,693 as of June 30, 2016 and 2015. There were no realized or unrealized gain/losses, purchases or sales reported by the Diocesan Insurance Office during the year ending June 30, 2016 and 2015. Due to the limited activity, fair value approximates original cost.

The Office does not have assets and liabilities recorded at fair market value on a nonrecurring basis.

The fair value estimates presented are based on pertinent information available to management at June 30, 2016 and 2015. Although management is not aware of any factors that would significantly affect the estimated fair value measurements, such amounts have been comprehensively revalued for purposes of the financial statements since that date; therefore, current estimates of fair value may differ significantly from the amounts presented herein.

Catholic Diocese of Kansas City—St. Joseph Diocesan Insurance Office

Notes to Financial Statements

See Independent Accountant's Review Report

Note 6. Health Care Plan

The Office started a self-insured health care plan as of January 1, 2014, which is administered by a third-party administrator. The plan provides for payments of hospitalization and medical benefits for lay employees and clergy of the Diocese, with excess claims funded by an insurance carrier. The carrier provides reinsurance on claims that exceed \$75,000 for the policy years ending December 31, 2016 and 2015. Plan premium income for this plan for the years ended June 30, 2016 and 2015, was \$7,491,585 and \$7,298,985, respectively; expenses were \$7,964,517 and \$6,273,323, respectively.

Note 7. Going Concern and Management's Plan

The Office recognizes that the recurring losses and total liabilities exceeding its total assets are conditions that may indicate the Office may be unable to continue as a going concern. The recurring losses that significantly contributed to this situation arose out of claims of sexual misconduct relating to incidents alleging to have occurred between the period from 1940 to early 1980 and were reported starting in June 2011. The Office reached a settlement with these claimants in October 2014 for the amount of \$9,950,000.

The Office plans to alleviate this financial condition by reductions in claim expenses, specifically reductions in legal services, premium rating increases and by planned release of funds (nonloan) from Chancery Operation and proceeds from the sale of certain nonparish/nonschool properties over an eight- to 10-year period to repay the loan to the Office and rebuild reserves.

