

**DIOCESAN FINANCIAL MANAGEMENT  
(A GUIDE TO BEST PRACTICES)**

## NEW ACCOUNTING STANDARDS

The Financial Accounting Standards Board (FASB) has issued several new accounting standards pertaining to not-for-profit entities, revenue recognition, and leasing which will take effect over the next few years. They are:

- Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*.
- ASU No. 2014-15, *Presentation of Financial Statements – Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern*.
- ASU No. 2016-02, *Leases (Topic 842)*, the goal of this guidance is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements.
- ASU 2016-14, *Not-for-Profit Entities (Topic 958) Presentation of Financial Statements of Not-for-Profit Entities*.

These standards may have a significant impact on the financial reporting for the diocese. The implementation of these standards will require time and resources. Diocesan financial officers should begin to develop an implementation plan for review and discussion with their bishops, Finance Councils, and auditors.

# **DIOCESAN FINANCIAL MANAGEMENT (A GUIDE TO BEST PRACTICES) (“DFM”) INTRODUCTION and FORWARD**

The DFM (formerly DFI) was developed by the Committee on Budget and Finance (CBF) of the United States Conference of Catholic Bishops (USCCB), in conjunction with a sub-committee, the Accounting Practices Committee (APC), and it was initially approved by the full body of bishops at its November 2002 General Meeting. The DFM was authorized for publication by Msgr. William P. Fay, General Secretary, USCCB.

As this DFM is revised by the APC, revisions are reviewed and approved through the USCCB and the revised DFM is published on the USCCB website.

This manual is published as an aide to diocesan Financial Officers, Religious Treasurers and other personnel responsible for the financial administration of dioceses and religious institutions of the Roman Catholic Church in the United States. As mentioned above, the DFM was initially adopted in November 2002. However, each year the APC updates the contents of the DFM for the approval of the CBF. The most recent update was drafted in April 2019. Its contents are based upon generally accepted accounting principles in the United States at the time of its annual updates.

The DFM is not intended to be a comprehensive document addressing all financial administration matters that might be encountered by dioceses or religious institutions in the administration of their finances. Rather, it is intended to be a document that addresses and offers best practices in financial administration matters that could be considered unique to dioceses and religious institutions. As such, it is recommended that the DFM be used in conjunction with other authoritative guidance. The APC has recommended Practitioner’s Publishing Company’s (PPC) *Nonprofit Financial and Accounting Manual*, in order to access guidance to accounting and financial reporting matters that are common to all nonprofit organizations. To obtain this Guide, call 1-800-431-9025, or go to [www.ppcnet.com](http://www.ppcnet.com). Other authoritative guidance materials are commonly available.

The APC is a committee comprised of diocesan financial directors and officers, and treasurers of religious institutes that was formed by the CBF in 1981. The APC was formed for the purpose of monitoring, commenting upon and reporting upon accounting and financial reporting principles that are proposed and approved by regulators of such generally accepted principles in the United States. The members of the APC are aided in their mission by expert advisors from the accounting profession. The APC is the successor to the Ad Hoc Committee on Diocesan Financial Statements which was formed by the United States Catholic Conference, predecessor to the USCCB, in 1971. The DFM is the successor to these previous publications: *Diocesan Accounting and Financial Reporting (1971)*; *Accounting Principles and Reporting Practices for Churches and Church-Related Organizations (1981)*; *Diocesan Fiscal Management Instructions (DFI) (2016)*.

We offer our deep gratitude and profound appreciation to the members of the APC for their time and efforts in developing and maintaining this valuable resource to the dioceses and religious institutions of our Church.

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General Secretary, USCCB

Ms. Theresa Ridderhoff,  
Associate General Secretary, USCCB

Most Reverend Dennis M. Schnurr, Archbishop of Cincinnati  
Treasurer, USCCB

#### NOTES:

- Translations are from *Code of Canon Law---English Edition New Translation*, prepared under the auspices of the Canon Law Society of America, Washington, D.C. 1999.
- Excerpts from R.T. Kennedy, *Book V: The Temporal Goods of the Church (cc. 1254-1310)*, in John P. Beal, James A. Coriden, and Thomas J. Greene, eds., *New Commentary on the Code of Canon Law* (Mahwah, N.J.: Paulist Press, 2000), 1468-1469. Reprinted with permission from Paulist Press.
- Certain materials in Chapter VI were used from the tax manual, *Income Taxes for Priests Only*, written by Scott A. Hoselton, CPA, CDFM, and published by Shepherds Advisor.
- The contents of this manual are based upon generally accepted accounting principles in the USA promulgated at the time of publication.

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# I. Financial Management Issues

## Introduction

The Church is responsible for the financial resources which have been entrusted to it. This responsibility includes safeguarding Church assets, exercising prudence in financial matters, accountability to those who provide monetary support to the Church and to regulatory authorities, and compliance with all civil regulations. As such, the Church is committed to the highest standards of fiscal integrity and accountability. Strong systems of internal controls are needed to safeguard assets by reducing the risk of fraud, misuse, waste or embezzlement. It is important that all diocesan officials and all employees within a diocese be sure that best financial practices are being followed. Best financial practices dictate that diocesan organizations review their policies and procedures in light of the continuing developments and those recent developments outlined below.

The American Competitiveness and Corporate Accountability Act of 2002, commonly known as the Sarbanes-Oxley Act was enacted in response to several corporate and accounting scandals that occurred in 2001 and 2002. Its purpose is to rebuild trust in America's corporate sector and promote stability in the financial markets. The law pertains primarily to public companies and addresses auditor independence, corporate responsibility for financial reports and internal controls, and management issues. Certain provisions of Sarbanes-Oxley apply to all organizations, including not-for-profits, because of preexisting law. The record retention provision and the whistle blower protection provisions apply to not-for-profit organizations, including churches. However, it behooves the Church to consider all of the Act's provisions in developing best financial practices.

Not-for-profit organizations are fast becoming the focus of similar oversight measures. For example, California passed the Nonprofit Integrity Act of 2004 which addresses two broad areas of nonprofit activity: management and fundraising. While religious organizations are exempt from most of the provisions of this law, they are subject to its fundraising and compensation review provisions.

The Senate Finance Committee has been considering a host of recommendations intended to strengthen the not-for-profit sector's transparency, management and accountability. Also, the Internal Revenue Service (IRS) has expanded its Form 990 regarding information to be included in the Form relating to a new or expanded section titled "Governance, Management, and Disclosures." The remainder of this chapter addresses several financial management issues that are offered as advice to diocesan bishops to be used in their dioceses as they deem appropriate.

## Internal Controls

The Committee on Budget and Finance of the United States Conference of Catholic Bishops (USCCB) has published a framework entitled *Diocesan Internal Controls: A Framework* that includes discussion on the following topics:

- Internal Control: A Definition
- Internal Control: Relationships and Responsibilities

- Establishing Internal Controls: Specific Practices, Procedures and Techniques
- Guidelines for a Diocesan Internal Controls Review
- Fraud and Irregularities: Concepts, Examples and Detection Rules

Access to the publication can be obtained at <http://www.usccb.org/about/financial-reporting/diocesan-internal-controls-framework.cfm>.

### **Fraud Prevention Programs and Controls**

Guidance to help prevent and deter fraud can be found in *Managing the Business Risk of Fraud: A Practical Guide*. This document was sponsored by the Institute of Internal Auditors, The American Institute of Certified Public Accountants and the Association of Fraud Examiners and has been issued to recommend ways in which boards, senior management and internal auditors can fight fraud in their organization. It provides guidance that defines principles and theories for fraud risk management and describes how organizations of various sizes and types can establish their own fraud risk management program.

This 78-page document can be obtained at:

[https://www.acfe.com/uploadedfiles/acfe\\_website/content/documents/managing-business-risk.pdf](https://www.acfe.com/uploadedfiles/acfe_website/content/documents/managing-business-risk.pdf).

Its outline is:

- Introduction
- Fraud Risk Governance
- Fraud Risk Assessment
- Fraud Prevention
- Fraud Detection
- Fraud Investigation and Corrective Action
- Concluding Comments
- Appendices

### **Communications of Internal Control Related Matters Noted in an Audit**

AU-C Section 265, *Communicating Internal Control Related Matters Identified in an Audit* establishes standards and provides guidance for auditors on communicating matters related to an entity's internal control over financial reporting identified in an audit of financial statements. It is applicable whenever an auditor expresses an opinion on financial statements (including a disclaimer of opinion).

The GAO's *Government Auditing Standards, 2011 Revision* includes internal control terminology consistent with AU-C Section 265. As such, these definitions will be applied by auditors in Single Audits as well.

## **Audit Committee**

An independent audit committee should be established, or those responsibilities should be assigned to the diocesan finance council, if the finance council consists primarily of persons who are not diocesan officials. An audit committee's primary functions include oversight of the internal control structure, evaluating the independent auditors, discussing the audit results with the independent auditors, overseeing the whistle blower and anti-fraud policies, providing guidance in the prevention and reporting of fraud and reviewing compliance with the Code of Conduct. Members of the audit committee should have the necessary professional and technical background to deal with accounting and internal control matters.

*The AICPA Audit Committee Toolkit: Not-for-Profit Organizations* is a valuable publication for audit committees in performing their oversight function effectively and efficiently. The publication is available at: [https://competency.aicpa.org/media\\_resources/208301-the-aicpa-audit-committee-toolkit-not-for-profit-e](https://competency.aicpa.org/media_resources/208301-the-aicpa-audit-committee-toolkit-not-for-profit-e).

Each diocese should consider having an “audit committee financial expert” on its Audit Committee or Finance Council. For public companies, the SEC defines such a person as having the following attributes:

1. An understanding of generally accepted accounting principles and financial statements;
2. The ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves;
3. Experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the diocese's financial statements, or experience actively supervising one or more persons engaged in such activities;
4. An understanding of internal controls and procedures for financial reporting; and
5. An understanding of audit committee functions.

The need for qualified people on audit committees at a diocese is just as important as it is for a public company.

A sample charter addressing the Audit Oversight Responsibilities of the Audit Committee (or Diocesan Finance Council) is attached to this chapter as Sample E.

## **Compensation Committee**

A best practice is that each diocese is to establish a compensation committee or designate the finance council to administer the pay and benefits of highly compensated employees. If a separate committee is established, then such committee should work under the auspices of the Diocesan Finance Council. Highly compensated employees are those whose total compensation equal or exceed \$120,000 per annum as determined by the IRS for 2018.

A compensation committee is composed of at least three (3) individuals, all of whom are deemed independent, having no conflicts of interest. The compensation committee is responsible for assuring that the conditions of the rebuttable presumption (See Chapter XX – Income Tax) are



met, that compensation is administered consistently within the diocese and that the related policies and practices are consistently applied.

The committee should meet at least two times each year. At one meeting the policies and procedures should be reviewed and approved. At the second meeting compensation for the coming year should be reviewed, adjusted as necessary and approved; and the current year's compensation reviewed to assure that it has been paid in accord with the prior year's approval or any subsequent approval. Decisions must be based on appropriate comparability data and contemporaneous documentation of the committee's deliberations and decisions should be made.

Finally, a viable compensation committee should also have access to and the authority to engage appropriate compensation consultants and/or attorneys to support the work of the committee.

### **Conflict of Interest Policy**

Each diocese should establish a conflict of interest policy. Although such a policy cannot prevent illegal or unethical behavior, it will help establish and create a proper control environment. The following items should be considered when developing a conflict of interest policy.

- It should be decided who is to monitor and ensure compliance with the conflict of interest policy. It should also be decided which personnel are required to provide a written acknowledgement of compliance with the conflict of interest policy and disclose all potential conflicts of interest.
- Dealings with the diocese that appear to have dual interests, or a conflict of interest should be evaluated closely (e.g. transactions with entities in which a diocesan employee or volunteer has a direct or indirect financial interest, or support being provided to other organizations with which an employee or volunteer is directly associated).
- Whether a matter is of significant importance to constitute a conflict of interest should be determined by the bishop or his designee (e.g. legal counsel).

An example of a policy statement is attached as Sample B.

### **Whistleblower Policy**

A strong preventive and detective measure against fraud in any organization is the opportunity for employees and other constituents to anonymously report suspected wrongdoing (whistleblowing) without the threat of retaliation. Each diocese should consider adopting a policy to report wrongdoing (commonly referred to as a whistleblower policy) and developing procedures to address "whistleblower" complaints regarding ethics, integrity, internal controls, and accounting or auditing matters. A sample policy to report wrongdoing is attached to this chapter as Sample C.

### **Anti-Fraud Policy**

Each diocese should have an anti-fraud policy that is clear, concise and documented. As such, each diocese should consider drafting a written anti-fraud policy. The policy should state that fraud is not tolerated and stipulate that the consequences of participating in fraudulent acts include,

but are not limited to, termination, and civil and criminal prosecution. It should also define fraudulent actions and address how to report suspected cases of fraud. A sample anti-fraud policy is attached to this chapter as Sample D.

### **Records Retention Policy**

Each diocese should have a records retention policy and procedure. See Chapter IV for additional information on record retention guidelines.

### **Code of Conduct**

Each diocese should establish a written Code of Conduct and promulgate it to the people of the diocese. A Code of Conduct memorializes in a clear and distinct manner appropriate behavior and practices that will be followed by all clergy, religious, lay employees and volunteers. A sample Code of Conduct is attached to this chapter as Sample A.

### **Internal Audits**

Each diocese should implement some level of internal audit. Such a function is a very important component of a sound internal control environment for parishes, schools and other diocesan entities.

The primary role of the internal audit function is to aid pastors and others in fulfilling their canonical and legal responsibilities. An effective internal audit will help safeguard the assets of a parish, review recordkeeping, internal control, accounting and financial reporting of the parish, identify areas of improvement and report findings and observations to the pastor, parish finance council and the audit or accounting committee of the diocese. Ideally, the internal auditors serve as pro-active, cooperative management advisory partners to the pastor. A well-developed internal audit team will function most effectively as consultants rather than compliance monitors, adding value through reviewing the parish business operation and making recommendations for improvement.

An internal audit also provides an independent review and verification that an organization is complying with laws and policies of the diocese and is making economical and efficient use of its resources. An internal audit assists management by providing independent and objective analysis of activities and controls. Internal audits are an objective review of the policies and systems a parish, school or other diocesan entity has in place that sometimes are never tested. Thus, an internal audit is designed to determine whether internal controls are in place and functioning so as to safeguard assets, provide reasonable assurance that financial activities are being properly recorded, summarized and reported, and provide reasonable assurance of compliance with diocesan policies and civil regulations.

The following models, or a combination thereof, are suggested as options to achieve an effective internal audit function, depending upon the financial resources available. These three models represent three different staffing alternatives. When only minimal financial resources are available for the internal audit function, the scope of work performed could be limited to the most high-risk entities and/or activities. The determination of the frequency of audits and the scope of the work

should be a function of general and specific risk analysis, considering such factors as parish size, staffing, volume of activity, history, etc.

### Staffing a Department

It is recommended as a best practice that dioceses hire internal audit staff to routinely visit parishes to assess financial management, internal controls and adherence to diocesan policy and civil regulation.

### Outsourcing to Qualified CPA Firms

If a lack of funds prevents hiring internal audit staff, a diocese could consider outsourcing the internal audit function through contracting with independent Certified Public Accountants (CPA's) to perform an internal review and agreed upon procedures that will give limited assurance of the adequacy of financial management. The cost of the CPA services could be shared or paid by the individual parishes.

### The Use of Appropriately Qualified/Credentialed Volunteers

A third alternative is to consider recruiting volunteers, such as retired CPA's, accountants or auditors to visit parishes and conduct financial reviews. The diocese should establish criteria/credentials for those volunteers and should select the volunteer auditors. Parish Finance Council members should not serve in the capacity of reviewing their own parish financial operations.

In all of the above staffing models, the diocese should develop the work program utilized in performing internal audits. Furthermore, the individuals performing the internal audits should report to the chief fiscal officer of the diocese, as he/she typically has the best understanding of parish financial issues. This does not typically create a conflict of interest because the chief fiscal officer of the diocese does not have direct responsibility for the parish, school or other entity accounting.

Conducting internal audits of all parishes, schools and entities on an annual basis represents a desirable goal; however, it may not be feasible in many dioceses due to financial and/or personnel constraints. A diocese can have an effective internal audit process with less frequent internal audits if a proper risk assessment process is utilized.

## **Summary of Good Financial Management Recommendations**

A recap of recommended standards for good financial management contained in this chapter and elsewhere in this manual follows:

### A. Adopt a Code of Conduct (Sample A) that:

1. addresses principles of ethics and integrity for all Church personnel;
2. stipulates guidelines for working with minor children;
3. addresses conduct for pastoral counselors and spiritual directors;
4. forbids harassment;

5. identifies prohibited political activities, addresses confidentiality, and identifies a mechanism for reporting potential violations; and
6. dictates non-tolerance of retaliation.

B. Adopt a Conflict of Interest Policy (Sample B) that:

1. requires reporting of potential or real conflicts of interest;
2. prohibits gifts and favors of value that could influence, or be construed as influencing a decision or obligation in the performance of one's duties;
3. prohibits board members from soliciting business or favors and from voting on decisions that may constitute a conflict of interest or could give an *appearance* of a conflict of interest; and
4. prohibits board members from influencing any activity that could confer a benefit on such member or anyone in the member's family or business.

C. Adopt a Whistleblower Policy (Sample C) that:

1. requires reporting of violations of civil and criminal laws or of the Code of Ethics by Church personnel;
2. stipulates that all reporting parties will be treated in confidence as much as the diocese's duty to investigate allows;
3. stipulates that all reported violations of the Code of Ethics will be investigated; and
4. prohibits retaliation against a person who makes a complaint or provides information regarding any reasonably perceived reportable activity.

D. Adopt an Anti-fraud Policy (Sample D) that:

1. clearly states that fraud or financial misconduct is not tolerated and that the prevention of fraud or financial misconduct is the responsibility of all personnel involved in Church administration;
2. stipulates that all suspected cases of fraud or financial misconduct are to be reported and provides assurance against recrimination; and
3. defines actions constituting fraud or financial misconduct, outlines reporting and investigating procedures, and stipulates that fraudulent acts and financial misconduct will be subject to disciplinary action, up to and including termination and civil and criminal prosecution.

E. Adopt an Audit Services Pre-approval and Independence Policy that:

1. requires the audit committee or Diocesan Finance Council to pre-approve all services to be provided by an audit firm and the fees for those services;
2. precludes specific services that could impair the auditor's independence;
3. considers audit partner rotation after seven consecutive years of service; and
4. stipulates minimum reporting standards by auditors to the audit committee or Diocesan Finance Council.

F. Establish a Diocesan Finance Council (see Chapter II of this manual) with a written charter to monitor diocesan finances and to fulfill the requirements of canon law. Among other

responsibilities, the Diocesan Finance Council, which is advisory to the diocesan bishop, should be required to recommend to the diocesan bishop:

1. approval of the hiring of an independent audit firm;
  2. approval of the budget of the diocese;
  3. approval of the annual financial report;
  4. responses to the required communications from the audit firm;
  5. approval of asset allocation ranges for diocesan investments; and
  6. approval of diocesan assessments and all transactions requiring Finance Council approval by canon law.
- G. Submit an annual Representation Statement to the metropolitan bishop (or senior suffragan bishop) signed by the Diocesan Finance Council members, the bishop and chief financial officer certifying that the Diocesan Finance Council executed its responsibilities and specifying meeting dates during the previous fiscal year and since yearend.
- H. Have independent audits performed for all significant diocesan entities.
- I. Publish the annual financial report of the diocese (including financial statements and footnotes, and the report of the independent auditor) so that it is available to all registered households.
- J. Adopt an Investment Policy Statement and Socially Responsible Investment Guidelines that are reviewed periodically.
- K. Establish an Investment Committee with a standard charter to review and approve investment policies, monitor investments and ensure compliance with the investment policy and socially responsible investment guidelines.
- L. Parish Financial Management – See Chapter V.
- M. Issue budgeting and financial reporting guidelines for all diocesan parishes, schools and agencies, stipulating that:
1. budgets are to be prepared annually;
  2. the pastor and finance council are to review actual revenues and expenses against budgeted amounts on a regular basis;
  3. periodic financial reports are to be issued to the parish council and an annual financial report is to be issued to the entire parish community; and
  4. the financial reports and supporting schedules required by the diocese are to be submitted timely.
- N. Adopt a Clergy Remuneration Policy that stipulates compensation levels for all clergy, delineates travel, housing, and meal expenses that are the responsibility of the parish, and summarizes benefit plans available to diocesan priests.
- O. Issue a records retention schedule for financial records that is consistent with the guidelines published by the United States Conference of Catholic Bishops.

- P. Require compliance with diocesan guidelines to open all bank and investment accounts.
- Q. Establish standard procurement procedures and require competitive bids when hiring an outside vendor/contractor when the total cost exceeds a specified dollar amount.
- R. Establish guidelines for new acquisitions and construction or renovation projects that address the necessary planning, financial requirements, fundraising, and construction process.
- S. Establish standard cash collection count procedures that require multiple unrelated counters, the use of locked or sealed bags for storing and transporting deposits, and the use of standard count sheets that are signed by all counters.
- T. Codify all financial policies and procedures for parishes, missions and schools in a manual that is available through the internet or intranet.
- U. Conduct annual workshops for parish finance council members, parish financial staff and pastors that address timely issues pertaining to parish financial policies and procedures and civil regulations.
- V. Perform parish financial reviews or internal audits designed to test the existence and effectiveness of parish internal accounting controls and compliance with diocesan policies and civil regulations.

## **Sample A: Code of Conduct**

*Insert diocesan Mission Statement and statement as to importance of complying with the Code of Conduct.*

All clergy, religious, lay employees and volunteers (representatives) of the diocese, its parishes (and parish schools), diocesan high schools and other diocesan entities must, at all times, comply with all applicable laws and regulations. The diocese will not condone the activities of those who achieve results through violation of the law or unethical or immoral business dealings. This includes any payments for illegal acts, indirect contributions, rebates, bribery and other similar types of activity.

All conduct should be clearly above the minimum standards required by law and expected by the Church. Accordingly, all representatives must ensure that their actions cannot be interpreted as being, in any way, in contravention of laws, regulations or principles governing the activities and mission of any diocesan entity. Representatives that are uncertain about the application or interpretation of any legal requirements should refer the matter to their supervisor, who, if necessary, should seek the advice of the bishop's office or his designee(s).

### **General Conduct**

All representatives of diocesan entities are expected to conduct themselves in a professional, Christian, businesslike manner. Drinking, illegal drug use, gambling, fighting, swearing, and similar unprofessional activities are strictly prohibited while on the job. Representatives must not engage in harassment (including but not limited to sexual harassment), discrimination, or retaliation or conduct themselves in a way that could be construed as such, for example, by using inappropriate language or jokes, keeping or posting inappropriate materials in their work areas, or accessing inappropriate materials on workplace computers.

### **Conflicts of Interest**

All representatives of diocesan entities are expected to perform their duties conscientiously, honestly, and in accordance with the best interests of the Church. Representatives must not use their position or the knowledge gained as a result of their position for private or personal advantage. Regardless of the circumstances, if a representative senses that a course of action they have pursued, are presently pursuing, or are contemplating pursuing may involve them in a conflict of interest; they should immediately communicate all the facts to their supervisor.

### **Outside Activities of Employees**

All Church employees are called always to act in a manner that is consistent with Catholic principles and teachings and have a serious responsibility for good public relations. Their readiness to help parishes, schools, and other charitable and educational activities is encouraged. Employees must, however, avoid acquiring any business interest or committing to any other activity that would, or would appear to:

- Create an excessive demand upon their time and attention, thus depriving their diocesan employer of their best efforts on the job, or
- Create a conflict of interest – an obligation, interest, or distraction – that may interfere with the independent exercise of judgment in their employer’s best interest.

### **Employee Relationships with Clients and Suppliers**

Employees should avoid investing in or acquiring a financial interest for their own accounts in any business that has a contractual relationship with the diocese, or that provides goods or services, or both to the diocese, if such investment or interest could influence or create the impression of influencing their decisions in the performance of their duties on behalf of the diocese.

### **Gifts, Entertainment and Favors**

Representatives must not accept entertainment, gifts, or personal favors that could influence, or appear to influence, Church business decisions in favor of any person or company with whom or with which we are likely to have business dealings. Similarly, representatives must not accept any other preferential treatment under these circumstances because it may be perceived to place them under an obligation. Meals, entertainment, holiday gifts and similar items that are infrequent and of modest value are not considered violations of this Code of Conduct. In cases of doubt, one should discuss the matter with their supervisor.

### **Kickbacks and Secret Commissions**

Employees may not receive payment or compensation of any kind, except as authorized under their employer’s remuneration policies. In particular, the acceptance of kickbacks and secret commissions from suppliers or others is strictly prohibited. Any breach of this rule may result in immediate termination and prosecution to the fullest extent of the law.

### **Diocesan Funds and Other Assets**

Representatives who have access to diocesan entity funds in any form must follow the prescribed policies and procedures for recording, handling, and protecting these funds as detailed in the dioceses and parishes, etc. policies, manuals and related materials. Policies and procedures are in place to prevent fraud and dishonesty. If an employee becomes aware of any evidence of fraud and dishonesty, they should immediately advise the designated personnel so they can promptly investigate the matter.

When a representative’s position requires spending diocesan entity funds or incurring any reimbursable personal expenses, that individual must use good judgment on the entity’s behalf to ensure that good value is received for such expenditures.

Diocesan entity funds and all other assets of a diocesan entity are for that entity’s purposes only and not for personal benefit.

### **Records and Communications**



Accurate and reliable records of many kinds are necessary to meet various legal and financial obligations, and to manage the affairs of diocesan entities. An entity's books and records must reflect all business transactions in an accurate and timely manner. The employees responsible for accounting and any other record keeping must exercise diligence in fulfilling these responsibilities.

Representatives must not make or participate in making any false record or communication of any kind, whether internal or external, including but not limited to:

- False expense, attendance, financial or similar reports and statements
- False advertising, deceptive practices, or other misleading representations

### **Dealing with Outside People and Dioceses**

Representatives must take care to separate their personal roles from their official positions when communicating on matters not involving diocesan entity business. Employees must not use diocesan entity identification, stationery, supplies or equipment for personal or political matters.

When communicating publicly on matters that involve any diocesan entity's business, representatives must not presume to speak for the entity or diocese on any topic, unless they are certain that the views they express are those of the entity, and it is the entity's desire that such views be publicly disseminated.

When dealing with anyone, including public officials outside the diocese, representatives must take care not to compromise the integrity or damage the reputation of either the bishop or the diocesan entity, or any individual, business, or government body.

### **Prompt Communications**

In all matters relevant to parishioners, churches, schools, government authorities, the public and others in the diocese, all representatives must make every effort to achieve complete, accurate, and timely communications – responding promptly and courteously to all proper requests for information and to all complaints.

### **Privacy and Confidentiality**

When handling financial and personal information about the diocese, parishes, parishioners, or others with whom we have dealings, representatives must observe the following principles:

1. Collect, use and retain only the personal information necessary for the business. Whenever possible, obtain any relevant information directly from the person concerned. Use only reputable and reliable sources to supplement this information.
2. Retain information only for as long as necessary or as required by law. Protect the physical security of the information.

3. Limit internal access to personal information to those with a legitimate business reason for seeking that information. Use only personal information for the purposes for which it was originally obtained. Obtain the consent of the person concerned before externally disclosing any personal information, unless legal processes or contractual obligation provides otherwise.

## **Sample B: Conflicts of Interest/Private Inurement Policy**

### **Purpose**

The purpose of this policy is to protect the diocese's interest when it is contemplating entering into a transaction or arrangement that might benefit the interests of private individuals, including but not limited to employees and individuals performing work on behalf of the diocese and other persons in a position to influence the affairs of the diocese. This policy is intended to supplement but not replace any applicable state laws governing conflicts of interest applicable to non-profit and charitable corporations. This policy should be distributed to existing and future executives, officers, trustees, directors, and members of advisory boards, councils and committees.

### **Introduction**

Non-profit charitable, religious, and educational organizations obtain their tax-exempt status under the theory that they perform valuable services for society and lessen the burdens of government. If a tax-exempt organization allows its money or other property to be used for private rather than public gain (e.g. for "private inurement" or "private benefit"), then it risks losing its exemption. In addition, under the "intermediate sanctions" provisions of the Internal Revenue Code, "disqualified persons" such as bishops, CFOs, other diocesan officials, board members, major donors doing work for the diocese, etc., who receive "excess benefits" are subject to an excise tax ranging from 25% to 200%, depending on the circumstances. Furthermore, any organizational manager who knowingly facilitates such an excess benefit is subject to a 10% tax. In light of these IRS restrictions and, more importantly, in order to assist the diocese in fulfilling its responsibilities to act as a competent and trustworthy steward of church goods, the diocese has developed this policy.

### **Identifying a Private Inurement or Private Benefit Problem**

In brief, "private inurement" is the *payment* or diversion of an exempt organization's assets to its officials, officers, directors, employees, relatives, friends, major donors, or others in a special relationship to the organization who can influence or control the policy or the day-to-day activities of the organization *for less than full and adequate consideration*. It is a broad concept that can exist in a variety of transactions under a variety of circumstances. Private inurement also extends to the use of organizational assets for "private benefits" such as sales, leasing, construction contracts, service transactions, etc., at other than fair market value or the exploitation of the exempt organization *for the benefit of a private business* (e.g. "sweetheart deals," promotional schemes, and/or giveaways to private individuals or businesses). Thus, under IRS regulations, a private benefit is similar to, but broader than, private inurement.

To avoid a material private inurement or benefit in the types of transactions described above, the particular diocesan parish, school, or agency must enter into transactions for its benefit, rather than for a private party's benefit, and exercise due diligence to ensure that the proposed transaction is fair and reasonable such that under the circumstances the organization could not have obtained a more advantageous arrangement with reasonable effort. In addition to screening proposed

transactions through the applicable councils, boards, or trustees, care should be taken to follow diocesan policies and procedures pertaining to the signing of contracts.

### **Conflicts of Interest**

A conflict of interest may exist when persons employed by the diocese (i.e. the Central Administrative Office, parishes, schools, diocesan agencies, and/or affiliated entities), those volunteers of the diocese holding trusteeships or other management authority, or those serving on advisory or consultative boards, councils or committees have a direct or indirect financial interest, as defined below.

### **Financial Interest**

A person has a “financial interest” if the person has, directly or indirectly, through business, investment, or family (including spouses; brothers or sisters; spouses of brothers or sisters; ancestors; children, grandchildren and great grandchildren; and spouses of children, grandchildren, and great grandchildren), any one of the following:

- a. an ownership or investment interest in any entity with which the diocese has a transaction or arrangement;
- b. a compensation arrangement with the diocese or with any entity or individual with whom the diocese has a transaction or arrangement;
- c. a potential ownership or investment interest with, or compensation arrangement with, any entity or individual with whom the diocese is negotiating a transaction or arrangement. Compensation includes direct and indirect remuneration as well as gifts or favors that are substantial in nature.

### **Duty to Disclose**

In connection with any actual or possible conflict of interest, an interested person must disclose the existence and nature of his or her financial interest and all material facts. Reports should be made to diocesan personnel as designated by the bishop, (i.e. vicar general, chancellor, attorney, chief financial officer or internal auditor). Reports should include relevant information that is discernible.

### **Investigation**

The designated diocesan personnel shall be responsible for a thorough and expeditious investigation of the actual/possible conflict of interest.

Proposed decisions on disposition of a case will be discussed with the bishop or his designee(s). The results of all reported conflicts of interest and the final resolution shall be reported to the Audit Committee.

### **Subsequent Conflicts and Disclosures**

Notwithstanding previous disclosures of actual or potential conflicts of interest, an individual shall make a new disclosure of conflicts when any matter involving the conflict of interest arises for discussion or action. In the event that an individual is uncertain whether an actual or potential conflict of interest exists, the individual should make disclosure of the circumstances that may give rise to an actual or potential conflict.

### **Confidential or Privileged Information**

Information known to be confidential that is acquired by individuals in the course of employment or association with the diocese and its affiliated entities shall be used only for the benefit and purposes of the diocese. Individuals shall neither disclose confidential information outside the scope of their authorized duties nor utilize their position or association with the diocese for personal identification or advantage, although there may be instances, based on the use of careful discretion and judgment, where incidental use of the association with the diocese may be appropriate.

## **Sample C: Whistleblower Policy**

### **Sample Policy to Report Wrong-doing**

Federal and/or State regulatory requirements for establishing whistleblower reporting programs and for the protection of employees from retaliatory actions should be considered in developing and implementing a policy to report wrong-doing such as the example that follows.

### **Diocese of N Policy to Report Wrong-doing**

The Diocese of N Code of Conduct requires all representatives of the Church, including clergy, religious, directors, and other volunteers, and lay employees, to observe high standards of business and personal ethics in the conduct of their duties and responsibilities. All representatives of the Church must practice honesty and integrity in fulfilling their responsibilities and comply with all applicable laws and regulations.

The objectives of the Policy to Report Wrong-doing are to establish policies and procedures for:

- The submission of concerns regarding questionable financial or legal matters, violations and suspected violations of the Code of Conduct, Code of Canon Law and other concerns by the stakeholders of the Church, on a confidential and anonymous basis;
- The receipt, retention, and treatment of complaints received by the organization; and
- The protection of anyone reporting concerns from retaliatory actions.

### **Reporting Responsibility**

Each representative of the Diocese of N has an obligation to report in accordance with this policy (a) questionable or improper accounting or auditing matters, (b) violations and suspected violations of Diocese's Code of Conduct and (c) other financial, legal or canonical concerns (hereinafter collectively referred to as Concerns).

Reports of Concerns should be made to diocesan personnel as designated by the bishop, (i.e. vicar general, chancellor, attorney, chief financial officer or internal auditor). All Concerns are to be reported as soon as possible. Reports of Concerns should include all relevant information about the suspected act, including any material evidence that exists.

### **No Retaliation**

This policy is intended to encourage and enable stakeholders to raise Concerns within the organization for investigation and appropriate action. With this goal in mind, no stakeholder who, in good faith, reports a Concern shall be subject to retaliation or, in the case of an employee, adverse employment consequences. Moreover, anyone who retaliates against someone who has reported a Concern in good faith is subject to discipline up to and including dismissal from their position within the Church.

## Investigation

The designated diocesan personnel shall be responsible for a thorough and expeditious investigation of the reported Concern. Proposed decisions on disposition of a case will be discussed with the bishop or his designee(s). The results of all reported Concern investigations and the final resolution shall be reported to the Audit Committee.

## Acting in Good Faith

Anyone reporting a Concern must act in good faith and have reasonable grounds for believing the information disclosed indicates an improper accounting or auditing practice, or a violation of the Code of Conduct or other management policies. The act of making allegations that prove to be unsubstantiated, and that prove to have been made maliciously, recklessly, or with the foreknowledge that the allegations are false, will be viewed as a serious disciplinary offense and may result in discipline, up to and including dismissal from their position with the Church. Such conduct may also give rise to other actions, including civil lawsuits.

## Confidentiality

Reports of Concerns, and investigations pertaining thereto, shall be kept confidential to the extent possible, consistent with the need to conduct an adequate investigation. Disclosure of reports of Concerns to individuals not involved in the investigation will be viewed as a serious disciplinary offense and may result in discipline, up to and including termination of the violator's position in the Church. Such conduct may also give rise to other actions, including civil lawsuits.

| <b>Sample Whistleblower Tracking Report</b> |                        |                               |  |  |                      |                 |
|---|------------------------|-------------------------------|--|--|----------------------|-----------------|
| <b>Date Submitted</b>                       | <b>Tracking Number</b> | <b>Description of Concern</b> | <b>Submitted By</b><br>(CL) Clergy<br>(R) Religious Lay<br>(E) Employee<br>(C) Constituent<br>(V) Vendor<br>(S) Stakeholder<br>(O) Other | <b>Current Status</b><br>(R) Resolved<br>(UI) Under Investigation<br>(D) Dismissed<br>(W) Withdrawn<br>(P) Pending/No Action | <b>Actions Taken</b> |                 |
|   |                        |                               |  |  | <b>Date</b>          | <b>Comments</b> |
|   |                        |                               |  |  |                      |                 |
|   |                        |                               |  |  |                      |                 |

## Documentation

Before using this sample, the diocese should review any applicable state or local laws or regulations, and the appropriate rules promulgated by other relevant regulatory bodies, if any.

## **Sample D: Anti-Fraud Policy**

### **Policy Statement**

The Diocese of N promotes a culture of honest and accountable stewardship of God's gifts. There is a significant responsibility associated with being stewards of the temporal resources of the Church: responsibility to safeguard the Church's assets, to exercise prudence in financial matters, to be accountable to those who provide monetary support to the Church, and to comply with all civil regulations.

Fraud is not tolerated. The prevention of fraud is the responsibility of all clergy, religious, lay employees, trustees, finance council members and other volunteers involved in church administration by adherence to diocesan policies and procedures. The diocese expects that any suspected case of fraud will be reported and provides assurance against recrimination. Persons found to have participated in fraudulent acts will be subject to disciplinary action, including termination, and civil and criminal prosecution.

### **Actions Constituting Fraud**

The Diocese of N defines fraud as the intentional misuse or misappropriation of a diocesan entity's resources or assets for the personal enrichment of the perpetrator or others. Fraud also includes the intentional false representation or concealment of a material fact relating to the misuse or misappropriation of a diocesan entity's resources or assets. Additionally, fraud also includes any intentional falsification of, or misrepresentation in, financial statements. Actions constituting fraud include, but are not limited to:

- misappropriation of funds, securities, supplies or other assets;
- impropriety in the handling or reporting of money or financial transactions;
- breach of fiduciary duty, including disclosing confidential information to outside parties;
- seeking anything of value from contractors, vendors or persons providing (or seeking to provide) services/materials to a diocesan entity for one's or another's personal benefit;
- accepting anything of value from contractors, vendors or persons providing (or seeking to provide) services/materials to a diocesan entity for one's or another's personal benefit, in violation of the diocesan Conflict of Interest Policy;
- bribery;
- inappropriate use of computer systems or other property of the diocesan entity;
- unauthorized destruction or removal of records, furniture, fixtures and equipment;
- intentional falsification of, or misrepresentation in, financial statements; and
- any dishonest act.



## **Reporting Fraud to the Diocese**

Suspected fraud should be reported to diocesan personnel as designated by the bishop (i.e. vicar general, chancellor, attorney, chief financial officer or internal auditor). All suspected frauds are to be reported as soon as possible. Failure to promptly report suspected acts of fraud may jeopardize the diocese's ability to recover stolen funds and/or property, or to correct improperly prepared financial statements on a timely basis. Reports of suspected fraud should include all relevant information about the suspected act, including any material evidence that exists.

## **Investigation**

The designated diocesan personnel shall be responsible for a thorough and expeditious investigation of the suspected fraud. Unless the report was anonymous, the person submitting the initial report will receive confirmation indicating that their report was received and that the subsequent investigation is confidential. That person may or may not be contacted during the investigation.

Proposed decisions on disposition of a case will be decided by the diocesan bishop or his designee(s). The results of all reported fraud investigations and the final resolution of all confirmed acts of financial fraud shall be reported to the Audit Committee/Finance Council.

## **Records Retention**

Fraud investigation files should be retained in accordance with guidelines established by the diocesan attorney.

## **Confidentiality**

Information about cases will be disclosed to those parties with a legitimate need to know. All parties with knowledge of such cases are to maintain confidentiality in order to avoid damaging the reputations of persons suspected but subsequently found innocent of wrongful conduct, and to protect the diocese from potential civil liability.

## **Sample E: Audit Oversight Responsibilities of the Audit Committee (or Diocesan Finance Council)**

### **Summary**

The Diocesan Finance Council has a responsibility to oversee the financial reporting process of diocesan entities and to advise the bishop in matters pertaining to financial reporting and the annual financial audit.

However, it is not the responsibility of the Diocesan Finance Council to provide expert assurance regarding the financial statements or the annual financial audit. Furthermore, diocesan officials are responsible for the preparation of the financial statements, for the fair presentation in the financial statements of the entities' financial position, results of its activities and cash flows in conformity with accounting principles generally accepted in the United States, and for the design and implementation of its systems of internal accounting control.

Furthermore, the Diocesan Finance Council is advisory to the bishop, in most matters, and discharges its duty by (1) acting in good faith; (2) utilizing the care that an ordinary prudent person in a like position would exercise under similar conditions; and (3) acting in a manner that they reasonably believe to be in the best interests of the diocese.

The inquiries, discussions and reviews required in the following key responsibilities are to be performed by the Diocesan Finance Council or may be wholly or partially performed by a Diocesan Audit Committee. However, if any such matters are assigned to an Audit Committee, the Finance Council should require the Audit Committee to report fully all significant matters or findings to the Finance Council.

### **Key Responsibilities**

#### ***Systems of Internal Accounting Controls***

1. Inquire whether diocesan officials are setting the appropriate tone by communicating the importance of internal controls so that all individuals possess an understanding of their roles and responsibilities.
2. Inquire whether diocesan officials are using independent firms to review computer systems and applications, the security of such systems and applications, and the contingency plan for processing financial information in the event of a systems breakdown.
3. Discuss with the independent auditors any internal control recommendations made during the course of their audit and inquire from both the outside auditors and diocesan officials as to whether internal control recommendations identified by the independent auditors have been implemented.
4. Inquire of the independent auditors, diocesan officials and legal counsel about any suspected or confirmed fraud, illegal acts, or deficiencies in internal controls.

5. Regarding complaints pertaining to accounting and auditing matters:
  - a. Inquire whether procedures have been established for the confidential, anonymous submission by employees of concerns regarding questionable accounting and auditing matters; and
  - b. Review the receipt and treatment of complaints received regarding accounting or auditing matters that were submitted by any party, internal or external to the organization.

### ***Compliance with Laws and Regulations***

1. Review the findings of any examinations by regulatory agencies.
2. Review with counsel any legal matters that could have a significant impact on the financial statements.

### ***Compliance with Code of Conduct and Other Management Policies***

1. Ensure that a policy addressing ethical conduct is formalized in writing and that it is communicated to all employees and volunteers. It is recommended that diocesan employees annually sign statements acknowledging that they understand and are complying with the policy.
2. Ensure that whistleblower and anti-fraud policies are formalized in writing and that they are communicated to all employees and volunteers. It is recommended that diocesan employees annually sign statements acknowledging that they understand and are complying with the policy.
3. Periodically obtain updates from management and general counsel regarding compliance with the Code of Conduct.
4. Periodically obtain the results of all reported fraud and whistleblower investigations.
5. Inquire whether conflict of interest forms have been received from appropriate officials and reviewed for conflict issues.

### ***Financial Reporting***

Before the audited financial statements are issued to the public, meet with diocesan officials and the independent auditors to review the annual financial statements and the results of the audit. This meeting should take place not later than approximately four months after the end of the fiscal year. Ask diocesan officials and the independent auditors about significant risks and exposures, the accounting and disclosure of these risks and exposures in the annual financial statements and plans to minimize such risks in the future. Also, ask the auditors their assessment of the quality of accounting principles, the degree of reasonableness of estimates and about other significant

judgments made by diocesan officials in preparing the financial statements and disclosures. Ask the independent auditors to report on and to discuss the following:

1. All changes to significant accounting policies and practices used by the diocese; including critical accounting estimates, and how current and anticipated future events impact those determinations;
2. All changes in alternative treatments (accounting and disclosure) of financial information within generally accepted accounting principles for policies and practices related to material items that have been discussed with diocesan officials, including the ramifications of the use of such alternatives and the treatment preferred by the auditors; and
3. Other material written communications between the auditors and diocesan officials. The following are examples, not all-inclusive, of written communications that should be reviewed:
  - a. Schedules of material unadjusted differences and a listing of material adjustments and reclassifications not recorded, if any, for all entities;
  - b. Diocesan managements' representation letter for the audit of the financial statements;
  - c. Reports on observations and recommendations on internal controls;
  - d. The engagement letter for the audit of the financial statements;
  - e. The audit firm's independence in relation to all diocesan entities; and
  - f. The final billing for services rendered, if different than the pre-approved amount.

### ***Independent Auditors***

1. Recommend to the bishop the appointment or discharge of the independent auditors.
2. Recommend all audit, review and attest services, all agreed-upon procedures, and all other services to be performed for all diocesan entities by the independent auditors.
3. Review and confirm the independence of the independent auditors by:
  - a. Reviewing the non-audit services performed by the auditors;
  - b. Reviewing the auditors' lead and concurring audit partners' rotation schedules; and
  - c. Recommend approval of the independent auditor's fees.

### ***Other Matters***

1. Meet with the independent auditors and diocesan officials in separate executive sessions to discuss any matters that the Audit Committee/Finance Council believes should be discussed privately.
2. Ensure that significant findings by the independent auditors are received and addressed on a timely basis.
3. If necessary, recommend to the bishop that he institute special investigations and, if appropriate, hire special counsel or experts.
4. Advise the diocese concerning the possible hiring of a member of the audit engagement team for a financial reporting oversight position in the diocese.
5. Annually review and update this document, as needed.

## II. Diocesan Finance Councils

**Canon 492 of the Code of Canon Law mandates all dioceses to establish a finance council:**

Canon 492 §1. In every diocese a finance council is to be established, over which the diocesan bishop himself or his delegate presides and which consists of at least three members of the Christian faithful truly expert in financial affairs and civil law, outstanding in integrity, and appointed by the bishop.

Canon 492 §2. Members of the finance council are to be appointed for five years, but at the end of this period they can be appointed for other five-year terms.

Canon 492 §3. Persons who are related to the bishop up to the fourth degree of consanguinity or affinity are excluded from the finance council.

### **Roles and Responsibilities of the Finance Council**

The diocese should prepare statutes for the finance council that includes, at a minimum, the following roles and responsibilities (sample statutes are included later in this chapter). The finance council must prepare the annual diocesan budget according to the instruction of the diocesan bishop (c. 493). While the annual budget may initially be prepared by the staff of the diocese, final approval and recommendation to the bishop rests with the finance council.

The finance council must examine the annual report of income and expenditures prepared by the diocesan finance officer (cc. 493, 494). This examination may take the form of reviewing the annual audited financial statements as presented by the diocese's independent auditors.

The finance council is to give *counsel* to the bishop on the following:

1. Appointment of a finance officer (c. 494)
2. Removal of the finance officer (c. 494)
3. Imposition of taxes, either ordinary or extraordinary (c. 1263)
4. Decisions relative to the more important acts of administration (it is for the conference of bishops to define what is meant by acts of extraordinary administration) (c. 1277)
5. Determination of the meaning of acts of extraordinary administration for institutes subject to his control if the statutes are not specific (c. 1281 §2)
6. Review of annual reports submitted to him by clerical and lay administrators of any ecclesiastical goods (c. 1287 §1)
7. Leasing of ecclesiastical goods owned by the diocese when the market value of the property to be leased exceeds \$400,000 (see Chapter XIII, subtopic: *Leasing*, c. 1297 and USCCB Complementary Norms for Canon 1297)
8. Investment of tangible and intangible property assigned to an endowment (c. 1305)
9. Modification of the obligations imposed in executing last wills for pious causes if such obligations cannot be fulfilled (c. 1310 §2)

The finance council must give or withhold *consent* to the bishop on the following:

- Performance of an act of extraordinary administration as defined by the United States Conference of Catholic Bishops (USCCB) (c. 1277):
  - i. Initiating a program of financing by the issuance of instruments such as bonds, annuities, mortgages or bank debt in excess of the minimum amount set in accord with Canon 1292 §1.
  - ii. Resolving an individual or aggregate claim(s) by financial settlement in excess of the minimum amount set in accord with Canon 1292 §1.
  - iii. Engaging in the regular management or operation of a trade or business that is not substantially related to the performance of the religious, spiritual, educational or charitable purposes of the Church, for the purpose of generating income to carry on such activities.
  - iv. Entering into any financial transaction or contractual agreement, the terms of which address matters involving an actual or potential conflict of interest for the diocesan bishop, auxiliary bishop(s), vicar(s) general, episcopal vicar(s), or the diocesan finance officer.
- Leasing of ecclesiastical goods owned by the diocese when the market value of the property to be leased exceeds \$1,000,000 or the lease is to be for three years or longer (see Chapter XIII, subtopic: *Leasing*, c. 1297 and the USCCB Complementary Norms for Canon 1297)
- Alienation of property at or above the “minimum” amount established by the USCCB (c. 1292 §1) (see Chapter XIII, subtopic: *Alienation and Acts of Ordinary and Extraordinary Administration*)
- Alienation of property of other public juridic persons subject to the diocesan bishop at or above the “minimum” amount established by the USCCB (c. 1292 §1) (see Chapter XIII, subtopic: *Alienation and Acts of Ordinary and Extraordinary Administration*)
- In addition to alienation, the entering into any transaction that worsens the patrimonial condition of the diocese (c. 1295)

**Be aware that consent must also be obtained from the Holy See for alienation of property given to the Church by vow, property precious for artistic or historical reasons or when the value of the property exceeds the “maximum” amount established by the USCCB (see Chapter XIII, subtopic: *Alienation and Acts of Ordinary and Extraordinary Administration*). Consent of the Holy See is also required for the valid leasing of ecclesiastical goods when the market value of the goods exceeds \$5,000,000 (see USCCB Complementary Norms for Canon 1297 – Leasing of Church Property).**

### **Other**

The diocese should consult with its canon lawyer to clarify the role of the diocesan finance council and ensure that it operates consistent with canon law. In addition to specific canon law requirements, diocesan bishops should consider consulting with their finance councils on the following:

- Appointment of auditors (in addition, the diocesan finance council should perform the audit committee oversight role if an audit committee does not exist, including oversight of financial management policies and the implementation thereof)
- Appointment of legal counsel
- Employee compensation and benefits
- Insurance and risk management
- Property management
- Construction management
- Investment policies
- Internal controls
- Development (fundraising) – see USCCB Complementary Norms for Canon 1262 (effective August 15, 2007) and U.S. Catholic bishops, *Principles and Guidelines for Fundraising by Dioceses, Diocesan Agencies and Religious Institutes* (November 16, 1977), available from the USCCB Finance Office
- Banking arrangements
- Fulfilling the requirements of the Resolution on diocesan Financial Reporting that became effective January 1, 2001

At its General Meeting in November 2000 the bishops unanimously adopted a Resolution on diocesan Financial Reporting, effective January 1, 2001 requesting each suffragan bishop to send an annual letter to his metropolitan archbishop (and each metropolitan archbishop to send an annual letter to the senior suffragan bishop in the province) specifying compliance with certain provisions of canon law. At its November 2011 meeting the Resolution was extended to remain in effect through November 2016. At its Plenary Assembly held November 2016 the Resolution was extended to remain in effect through November 2021. The finance council should assist the bishop in fulfilling the requirements of the resolution. The resolution and reporting form are reproduced later in this chapter.



## SAMPLE

### *Sample Statutes of Diocesan Finance Council*

#### STATUTES FOR THE FINANCE COUNCIL OF THE DIOCESE OF N

**ARTICLE I**           The name of this body shall be the Diocesan Finance Council referred to sometimes as “DFC”

**ARTICLE II**           Purpose

The Diocesan Finance Council is one of the three major councils of the Diocese of N. It is established by the bishop for the purpose of advising and assisting him in financial matters.

The finance council must prepare the annual diocesan budget (while the annual budget may initially be prepared by the staff of the diocese, final approval and recommendation to the bishop rests with the finance council).

The finance council must examine the annual report of income and expenditures prepared by the diocesan finance officer (this examination may take the form of reviewing the annual audited financial statements as presented by the diocese’s independent auditors).

The finance council must give or withhold consent to the bishop on the following:

- Performance of an act of extraordinary administration as defined by the United States Conference of Catholic Bishops (USCCB) (c. 1277):
  - i. Initiating a program of financing by the issuance of instruments such as bonds, annuities, mortgages or bank debt in excess of the minimum amount set in accord with Canon 1292 §1.
  - ii. Resolving an individual or aggregate claim(s) by financial settlement in excess of the minimum amount set in accord with Canon 1292 §1.
  - iii. Engaging in the regular management or operation of a trade or business that is not substantially related to the performance of the religious, spiritual, educational or charitable purposes of the Church, for the purpose of generating income to carry on such activities.
  - iv. Entering into any financial transaction or contractual agreement, the terms of which address matters involving an actual or potential conflict of interest for the diocesan bishop, auxiliary bishop(s), vicar(s) general, episcopal vicar(s), or the diocesan finance officer.
- Leasing of ecclesiastical goods owned by the diocese when the market value of the property to be leased exceeds \$1,000,000 or the lease is to be for three years or longer (c. 1297 and USCCB Complementary Norms for Canon 1297).
- Alienation of property at or above the amount established by the USCCB (c. 1292 §1) and updated annually based on the consumer price index.

- Alienation of property of other public juridic persons subject to the archbishop at or above the amount established by the USCCB (c. 1292 §1) and updated annually based on the consumer price index.
- In addition to alienation, the entering into any transaction that worsens the financial condition of the diocese (c. 1295).

The finance council is to give counsel to the bishop on the following:

1. Appointment of a finance officer (c. 494)
2. Removal of the finance officer (c. 494)
3. Imposition of taxes, either ordinary or extraordinary (c. 1263)
4. Decisions relative to the more important acts of administration (it is for the conference of bishops to define what is meant by acts of extraordinary administration) (c. 1277)
5. Determination of the meaning of acts of extraordinary administration for institutes subject to his control if the statutes are not specific (c. 1281 §2)
6. Review of annual reports submitted to him by clerical and lay administrators of any ecclesiastical goods (c. 1287 §1)
7. Leasing of ecclesiastical goods owned by the diocese when the market value of the property to be leased exceeds \$400,000 (see Chapter XIII, subtopic: *Leasing*, c. 1297 and USCCB Complementary Norms for Canon 1297)
8. Investment of tangible and intangible property assigned to an endowment (c. 1305)
9. Modification of the obligations imposed in executing last wills for pious causes if such obligations cannot be fulfilled (c. 1310 §2)

In addition to the canon law requirements outlined above, the finance council will also advise the bishop with regard to the following:

- Appointment of auditors (in addition, the finance council will perform the audit committee oversight role, including oversight of financial management policies and the implementation thereof)
- Appointment of legal counsel
- Employee compensation and benefits
- Insurance and risk management
- Property management
- Construction management
- Investment policies
- Internal controls
- Development (fundraising) – see USCCB Complementary Norms for Canon 1262 (effective August 15, 2007) and U.S. Catholic Bishops, *Principles and Guidelines for Fundraising by Dioceses, Diocesan Agencies and Religious Institutes* (November 16, 1977), available from the USCCB Finance Office
- Banking arrangements
- Fulfilling the requirements of the Resolution on Diocesan Financial Reporting that became effective January 1, 2001

### **ARTICLE III**          Membership

DFC shall be composed of not fewer than 19 persons, including the Bishop of N, or the person who, in his stead, exercises ordinary jurisdiction over the spiritual and temporal affairs of the Diocese of N in accordance with legislation of the Roman Catholic Church and the Vicar General of the Diocese.

1. Two members of this Council shall be elected by the Diocesan Pastoral Council.
2. Two members of this Council shall be priests serving the Diocese of N, elected by the Presbyterial Council of the Diocese.
3. One member of this Council shall be a religious sister serving the Diocese of N, elected by the Sisters Council of the Diocese.
4. One member of this Council shall be a permanent deacon, serving the Diocese of N, elected by the Deacon Council of the Diocese.
5. At least eight members of this Council shall be appointed to at-large positions by the bishop.
6. Three members of this Council shall be appointed by the bishop as:
  - a. Chair of the Diocesan Finance Council
  - b. Chair of the Revenue Committee
  - c. Chair of the Allocations Committee

The Vicar of Finance shall also be an ex-officio, non-voting member of this Council.

It shall be the responsibility of each of the six elected members of the DFC to communicate non-confidential activities and recommendations of the DFC to the body which elected each such member and to encourage that body to exercise care in the election of its members to ensure its representatives have the interest and time to serve, and to communicate to the DFC the observations or recommendations of the organizations which elected them in regards to matters being considered by the DFC.

### **ARTICLE IV**          Term of Office

1. The regular term of office of the elected or appointed at-large members of the DFC shall be five years, with approximately one-third of those members' terms expiring each year.
2. No elected or appointed at-large members shall serve more than two consecutive five-year terms.
3. The Chair of the Revenue Committee and the Chair of the Allocations Committee shall be appointed to a two-year term. These Chairs may not serve more than three consecutive two-year terms. The Chair of this Council shall be appointed for a one-year term.

**ARTICLE V**            Vacancies

Vacancies on the DFC by reason of resignation, death, disability, termination of office, or otherwise, shall be filled by the same constituency or person which originally selected the member whose position has become vacant.

**ARTICLE VI**           Officers and Duties

The officers of the DFC shall be a Chair and a Vice-Chair.

1. The Chair of this Council shall conduct all meetings of the DFC and its Executive Committee.
2. The Vice-Chair of the Council shall act in the place of the Chair when the Chair is absent or unable to attend a meeting of the DFC or the Executive Committee and shall assist the Chair in the performance of the Chair's duties. The Vice-Chair shall be appointed by the bishop from among the membership of the Council for a one-year term.

**ARTICLE VII**         Meetings

Meetings of the DFC shall be held at the call of either the bishop, the Chair, or by a majority of the full membership of the DFC. The Vicar of Finance shall provide the necessary staff support for effective meetings of the DFC.

**ARTICLE VIII**       Committees

There shall be an Executive Committee and two standing committees of the DFC. The standing committees shall be the Revenue Committee and the Allocations Committee. All DFC members shall serve on at least one of the three committees. Members may indicate their committee preference prior to appointment.

The Vicar of Finance shall provide the necessary staff support for effective meetings of all committees of the DFC.

1. Executive Committee: There shall be an Executive Committee composed of the bishop or his delegate, the Chair of the DFC, who shall be the Chair of the Executive Committee, the Vice-Chair of the DFC, the Chair of the Revenue Committee, the Chair of the Allocations Committee, and two members of the DFC elected to one-year terms by the DFC.

The Executive Committee shall be responsible for the affairs of the Council between meetings, adoption of a yearly schedule of DFC meetings, preparing agendas for the DFC meetings, assigning DFC members to the standing committees, approving the annual plans and schedules of standing committees, recommending policies and procedures guiding the budget process and the operations of the DFC, and for determining the purpose, membership and term of each ad hoc committee. It shall report all of its activities and actions to the DFC at the next meeting of the DFC for ratification.

2. Revenue Committee: The Revenue Committee shall consist of a Chair appointed by the bishop, at least five members of the DFC appointed by the Executive Committee, and up to five or six others recommended by the DFC Revenue Committee members and approved by the bishop for three-year terms.

The Revenue Committee shall review and coordinate revenue projections of all sources of operating and capital funds and assist and advise on the annual and multi-year fundraising strategies and efforts of the Diocesan Central Corporation prior to any major fundraising campaigns.

The Revenue Committee acts as a central area for communications on all major fundraising by agencies, departments, and institutions both inside and outside the Diocesan Corporation to help monitor and coordinate these efforts.

3. Allocations Committee: The Allocations Committee shall consist of a Chair appointed by the bishop, at least five members of the DFC appointed by the Executive Committee and the Chairs of the Allocation Panels. Allocation Panel Chairs shall be suggested by the Allocations Committee Chair, recommended by the DFC and approved by the bishop for a one-year term.

The Allocations Committee and its panel, each consisting of up to six persons appointed to staggered three-year terms by the Allocations Committee Chair, shall review the three-year and annual proposals for new and expanded programs, the three-year goals and annual objectives and the three-year and annual budgets of each department and agency requesting funds from the Central Corporation, and it shall prepare recommendations for the DFC on them. The panels shall further establish contact with their respective agencies/departments, conduct budget hearings, and prepare and present to the Allocations Committee recommendations from their respective panels.

The Allocations Committee shall annually prepare a recommended total budget including funds and comments on existing, expanded and new programs, from the panel recommendations and submit it to the Bishop's Cabinet and the DFC. The Allocations Committee and its panels shall review needs on a year-round basis and recommend to the DFC such changes in allocations as it deems necessary.

The Revenue and Allocations Committees shall work closely with the division directors and other staff as appropriate, to become informed about proposals, plans and studies that can impact revenue or spending, the goals or objectives of departments and agencies, and strategies and funding to achieve them.

## **ARTICLE IX**            Quorum and Voting

A majority of the full membership shall be necessary and sufficient to constitute a quorum for the transactions of business at all meetings of the DFC and its committees so long as all the members of the council or committees were properly notified of the meeting in accordance with Canon 127. The act of a majority of the members present at any meeting at which there is a quorum shall be the act of the DFC or its committees.

## **ARTICLE X**            Amendments

Amendments to these statutes shall be proposed at any meeting of the DFC, following a two-week notice, and if approved by two-thirds of the full membership of the DFC they shall be proposed to the bishop. They shall become effective upon approval by the bishop.

### **Diocesan Financial Reporting – USCCB Resolution**

The Diocesan Finance Council has a recommended reporting responsibility in accord with the USCCB resolution on diocesan financial reporting.

## **Preamble**

At the November 2000 Plenary Assembly, the United States Conference of Catholic Bishops (USCCB) approved a "Resolution on Diocesan Financial Reporting." Affirming the episcopal conference's longstanding commitment to promote financial accountability in the pastoral governance of the diocesan bishop, the resolution encouraged the adoption of a voluntary financial reporting system as a means of offering further evidence of the diocese's compliance with the prescriptions of canon law pertaining to fiscal administration. Since its original passage, the resolution has been renewed by the USCCB approximately every five years.

"As the one who presides over the particular Church, it falls to the Bishop to organize the administration of ecclesiastical goods" entrusted to his care (*Directory for the Pastoral Ministry of Bishops*, n. 188). In doing so, he "must seek the collaboration of the college of consultors and the finance council in those matters determined by the universal law of the Church and when prudence so dictates, because of the importance of the case or its particular circumstances" (*Directory for the Pastoral Ministry of Bishops*, n. 189, a).

The "Resolution on Diocesan Financial Reporting" acknowledges the legitimate rights of the diocesan bishop to administer the material resources of the diocese that he shepherds as a "good householder" (c. 1284, §1 CIC). At the same time, it provides a vehicle for fraternal cooperation and support among all of the bishops of the province and assists the metropolitan archbishop in his own special solicitude for the suffragan dioceses (c. 436 §1, 1° CIC).

## **Resolution**

Annually, after the end of the fiscal year, each suffragan bishop is asked to send a letter to his metropolitan archbishop containing:

1. the names and professional titles of the members of his diocesan finance council;
2. the dates on which the finance council has met during the preceding fiscal year and since the end of that fiscal year;
3. a statement signed by the finance council members and the finance officer stating that they have met, reviewed, and discussed the [audited] financial statements of the diocese for that fiscal year and, if any, the management letter and the recommendations made by the auditors;
4. a statement that the finance council was consulted in accord with the prescriptions of canon law.

The metropolitan archbishop will provide this same letter to the senior suffragan bishop in promotion in the province.

This resolution, approved by the United States Conference of Catholic Bishops at the November 2016 Plenary Assembly, becomes effective January 1, 2017 and will remain effective through November 2021.

**NOTE: A sample diocesan financial reporting form can be found on the following page.**

**SAMPLE**

**DIOCESAN FINANCIAL REPORTING FORM**

**Name and Professional Titles of Diocesan Finance Council Members**

**NAME**

**TITLE**

- 1.
- 2.
- 3.
- 4.
- etc.

**Diocesan Finance Council Meeting Dates**

- 1.
- 2.
- 3.
- 4.
- etc.

**Diocesan Finance Council and Finance Officer Attestation**

*We have met, reviewed and discussed the [audited] financial statements of the (insert name of diocese) and the management letter for the fiscal year ended (insert year) including the recommendations made by the auditors.*

*We have been consulted in accord with the prescriptions of canon law.*

**SIGNATURE**

**PRINTED NAME**

- 1.
- 2.
- 3.
- 4.
- etc.



## **III. Diocesan Finance Officer**

### **Canon Law**

Canon 494 §1. In every diocese, after having heard the college of consultors and the finance council, the bishop is to appoint a finance officer who is truly expert in financial affairs and absolutely distinguished for honesty.

Canon 494 §2. The finance officer is to be appointed for a five-year term but can be appointed for other five-year terms at the end of this period. The finance officer is not to be removed while in this function except for a grave cause to be assessed by the bishop after he has heard the college of consultors and the finance council.

Canon 494 §3. It is for the finance officer to administer the goods of the diocese under the authority of the bishop in accord with the budget determined by the finance council and, from the income of the diocese, to meet expenses which the bishop or others designated by him have legitimately authorized.

Canon 494 §4. At the end of the year, the finance officer must render an account of receipts and expenditures to the finance council.

As a best practice for diocesan financial management in accord with the preceding provisions of canon law, the Chief Financial Officer is responsible for making sure the annual audit is completed in a timely fashion.

### **Qualifications**

The diocesan finance officer may be a cleric or a layperson in communion with the Church and must be someone of high integrity and an expert in financial matters. A certified public accountant or someone with similar qualifications and experience usually is preferred.

### **Position Description**

Each diocese should develop a position description for the finance officer that describes the qualifications, duties, and reporting responsibilities for that position. The position description also should include clear requirements, expectations, and relationships that will exist with other offices in the diocese.

### **Other References**

See Cusak, Barbara Anne, “The Finance Council and the Finance Officer” in *New Commentary on the Code of Canon Law*, edited by John P. Beal, James A. Coriden and Thomas J. Green, (Mahwah, NJ: Paulist Press, 2000): 645-652.

## IV. Records Retention

This Records Retention policy is recommended for all dioceses that are not subject to a litigation hold resulting from lawsuits, civil or criminal subpoenas, or canon law directives. Dioceses that are subject to litigation holds should comply with the requirements of the litigation holds.

### Introduction

A records management and retention policy is an important component of the administration of each diocese. Records are important for sacramental purposes, day-to-day management and administration, when needed for litigation, efficient management of space, etc. Each diocese should review and comply with the retention requirements applicable to that particular jurisdiction and the nature of the diocese's documents.

Many dioceses have developed and implemented such policies after careful thought, analysis and consultation with legal counsel. It is recommended that dioceses that do not have such a policy consult with those that do, particularly in the same province or state. The formulation of a compliant, practical policy should be done in collaboration with diocesan legal and canonical counsel, the Vicar General, CFO, Chancellor and Archivist.

### Definition of Records

Records retention policies should include paper records and electronic files, data and e-mails. Such records would likely be included in the following categories:

- Administrative
- Personnel
- Financial
- Legal
- Property
- Cemetery
- Publications
- Sacramental

Within each group, records could be categorized into the respective appropriate retention periods. Records older than the retention period should be destroyed. Those of permanent value should be stored appropriately.

*Confidential* records should be made available only to diocesan/parish representatives with a legitimate right to know, unless their disclosure is compelled by some legal action.

A comprehensive records retention policy should include the following:

1. Complete listing of all types of records and their retention periods.

2. Documentation to be used in storing, including indexing, labeling, pre-determined destruction dates, inventorying, etc.
3. Internal controls over retrieval, returns and destruction, along with appropriate documentation standards.
4. A process and calendar for updating records into and out of storage and destruction at least annually.
5. Security over stored records.
6. Training and education of all staff on the entire policy and the actual processes. Particular attention should be given to appropriate retention and deletion policies and practices for emails, recorded voicemails, etc. as electronic media, technology and related state and federal laws continue to evolve.
7. If an external shredding service is used for the destruction of records no longer needed, it will often be prudent for the archivist to bring the documents to the shredding service and to witness the actual destruction.

A sample policy from a large diocese is included herein for reference purposes. Please consult local counsel when developing a Records Retention Policy.

## **SAMPLE POLICY – *Consult with Legal Counsel***

*Note: this records management and retention policy is provided only as an example. Please consult your local diocesan canon lawyer and civil legal counsel when developing a records retention policy for your diocese.*

### **Records Management and Retention Policy and Schedule Roman Catholic Diocese of N [date]**

#### **General:**

1. Definition of records: the word “records” used in this policy refers to all recorded information, documents, letters, maps, books, photographs, films, sound recordings, tapes (magnetic and otherwise), electronic data processing records, emails sent and received, recorded voicemails, electronic data banks and other documentary material created, received, maintained or preserved by any department or employee of the Diocese of N in the course of transaction of business or ministry or in pursuit of its legal obligations.
2. Ownership of records: all records as defined above and created or preserved by a department, ministry or employee of the Diocese of N in the course of employment or in the transaction of diocesan business are solely the property of the diocese.
3. Conservation of records: no records shall be removed, destroyed, transferred, stored, transferred onto other media or otherwise disposed of except in compliance with diocesan policies.
4. Retention periods: retention periods in this policy are absolute, except when legally halted by official notice. They are not minimum guidelines. There are no exceptions.
5. Disposal of expired records: Annually, the second week of [month], each department of the Diocese of N will dispose of records whose retention time has expired. Records may be shredded or, if electronic, deleted or destroyed by another approved method. No exceptions may be made, the retention times are absolute. Arrangements will be made for commercial shredding. A copy of the Certificate of Destruction will be executed and signed by the department head. One copy should be sent to Archives and the other retained by the department.
6. Certification of disposal of expired records: Each year, by [month] 1<sup>st</sup>, every department head will submit to the Chancellor a letter testifying to the fact that all expired records pertaining to his/her department have been destroyed in accordance with the Records Retention Schedule.
7. Off-site storage of inactive records: records that are generally inactive but must be retained permanently or for a set period of time will be stored off-site. Records will be prepared for storage annually during the second week of [month]. Boxes will be provided for the records. Each box will be identified with a label to be provided. A Certificate of Off-Site

Storage must be completed in triplicate. One copy should be placed in the storage box. One copy sent to Archives and one copy retained by the department.

8. Conversion of records to electronic medium: paper records may be scanned or otherwise transferred to an electronic medium. When the conversion is complete the paper records will be destroyed in accordance with number 6 above.
9. Administration: administration of the Records Management and Retention Program will be the responsibility of the chancellor of the diocese and will be the specific responsibility of the Diocese of N Archivist, who will publish the exact dates and confirm conformance to this policy by all departments. The Archivist will submit a written report of conformance to the Chancellor by [month, date] of each year.
10. Changes and implementation: changes to this policy or the Records Retention Schedule may be made only with the written approval of the Bishop of N. This policy will become effective upon approval of the Bishop of N with the first period for record disposal the month following promulgation.

**Email:**

1. Email messages are similar to other forms of communicated messages such as correspondence, memoranda and letters. These include non-record (transitory) emails and official record emails.
  - A. Non-record or transitory electronic communications are considered to have no administrative, legal, fiscal or archival requirements for their retention. Examples of such non-record electronic communications include the following:
    1. Personal correspondence not relating to conducting diocesan business such as lunch invitations, unsolicited advertisements and spam;
    2. Routine requests for information or publications which require no administrative action, policy decision, or special compilation or research and copies of replies;
    3. Originating office copies of letters of transmittal that do not add any information to that contained in the transmitted material;
    4. Quasi-official notices including memoranda and other records that do not serve as the basis of official actions (i.e., holiday notices, meeting confirmations etc.);
    5. Non-email electronic communications including, but not limited to, instant messaging, texting, paging, voice recording and other electronic communication technologies other than email.
  - B. Official-record emails include any writing containing information relating to the conduct of the diocese's business prepared, owned, used or retained by diocesan employees. Official record emails should be retained for the appropriate period of time based on the content and subject matter of the email and the corresponding

retention period for that subject matter as prescribed by the Document Retention Schedule.

Examples of emails that may constitute an official record include the following: policies and directives, correspondence or memoranda relating to diocesan ministries and other activities (excluding duplicates), agendas and minutes of meetings, any document that initiates, authorizes or completes a business transaction and final reports or recommendations.

## 2. Responsibility for Retention

The sender of the email is responsible for ensuring proper retention of official record emails sent. All other copies of internal email are duplicates and may be deleted. However, if a record email was sent by an outside organization, a member of the public or anyone outside the diocese, the recipient is responsible for retention. **Warning** – Email will not be the repository of official electronic records retention. See Method of Retention below.

## 3. Method of Retention

Official record emails that have not met their retention should be saved by one of the following methods:

- A. Print the email and store the hard copy in the appropriate file.
- B. Move the email out of the email system and store it on a shared network drive.

## 4. Information Technology (IT) Department Email Management

- A. Ensures that email account or mailbox will be limited to a maximum size of 2GB data. This includes all folders and subfolders and containers that reside within a user's email account or mailbox. Examples include the inbox, sent items, deleted items, drafts, contacts and calendar items.
- B. If a mailbox exceeds the 2GB of data size limit, the mailbox will not function to send or receive email until the space is cleared.
- C. Users will be notified when their mailbox reaches 90% of capacity.
- D. Emails in the "Deleted" folder will be purged daily and not backed up. This is the default email system setting and may not be configured differently.
- E. Data that remains within the mailbox (including the inbox, sent items, drafts, contacts and calendar items) will be archived for a period of three years. Mailbox items will be archived every sixty days. After three years, these emails will be purged. Contacts and Calendar items will not be purged as part of this process; it will be up to the user to determine if those items need to be purged for space requirements.

## 5. Email Management

- A. Staying below the maximum mailbox size of 2GB is the responsibility of the mailbox user.
- B. Official record emails and attachments should either be printed or moved off the email system to a shared network drive.
  - 1. To prevent the loss of non-record emails after the three-year archival period, the user may:
  - 2. Print the email and store the hard copy in the appropriate file.
  - 3. Move the email out of the email system and store it on a shared network drive.

## 6. Litigation Proceedings

Regardless of retention requirements, email and all other electronic correspondence pertaining to threatened or actual legal proceedings must be retained until the litigation is finally concluded. It is the responsibility of the department involved to notify the IT department in writing of the need for the hold on the destruction of electronic communications.

## 7. Email Accounts When Employee Leaves Employment

When an employee is no longer employed, it is the responsibility of that department to immediately notify the IT Department. That user's mailbox will be maintained for sixty calendar days. Individual user mailboxes will be purged after sixty calendar days. It is the department head's responsibility to ensure that official record emails that have not met their retention have been saved by the end of the sixty-day period by one of the following methods:

- A. Print the email and store the hard copy in the appropriate file.
- B. Move the email out of the email system and store it on a shared network drive.

## Sample Records Retention Policy

| Record Group  | Type of Record  | Time                 | Medium     | Retained         | Disposal |
|---|---|----------------------|------------|------------------|----------|
| <i>The fact that a record is electronic or email should not affect its retention. The schedule to be followed should be determined by the context of the record. For example, an email about finance matters would follow the schedule for financial records.</i> |   |                      |            |                  |          |
| <b><u>Administrative Records (ALL Departments)</u></b>  |   |                      |            |                  |          |
|   | Administrative Records (correspondence, memoranda, rules and regulations, etc.)                     |                      |            |                  |          |
|   | a. Records originating in the organization that document policy, procedure, rules or regulations    | Permanent            | Paper/elec | On-site/Off-site |          |
|   | b. Records that document routine activities   | 2 years              | Paper/elec | On-site/Off-site |          |
|   | Abstracts, deeds (property)   | Permanent            | Paper      | On-site/Off-site |          |
|   | Annual reports to Pastoral Center (Status Animarum)   | Permanent            | Paper      | On-site/Off-site |          |
|   | Articles of Incorporation (of the church corporation, parish)                                       | Permanent            | Paper      | On-site/Off-site |          |
|   | Bequest and estate papers   | Permanent            | Paper      | On-site/Off-site |          |
|   | Bishop's Decrees  | Permanent            | Paper/elec | On-site/Off-site |          |
|   | Communications from the Bishop regarding the parish   | Permanent            | Paper/elec | On-site/Off-site |          |
|   | Constitution and Bylaws (Diocesan Agencies)   | Until Dissolved      | Paper      | On-site/Off-site |          |
|   | Correspondence, legal   | Permanent            | Paper/elec | On-site/Off-site |          |
|   | Correspondence, official ( <i>paper and email</i> ) regarding diocesan directives and/or procedures | Permanent            | Paper/elec | On-site/Off-site |          |
|   | Correspondence, routine   | Biennial review      | Paper      | On-site/Off-site |          |
|   | Donor lists   | Permanent            | Paper/elec | On-site/Off-site |          |
|   | Finance Committee Minutes   | Permanent            | Paper/elec | On-site/Off-site |          |
|   | Insurance policies  | Permanent            | Paper      | On-site/Off-site |          |
|   | Inventories of property and equipment   | Permanent            | Paper/elec | On-site/Off-site |          |
|   | Leases  | Expiration + 7 years | Paper      | On-site/Off-site |          |
|   | Office files, general   | Biennial review      | Paper/elec | On-site/Off-site |          |
|   | Diocesan Pastoral Council constitutions   | Until superseded     | Paper/elec | On-site/Off-site |          |
|   | Diocesan Pastoral Council minutes   | Permanent            | Paper/elec | On-site/Off-site |          |
|   | Policy statements   | Superseded + 7 years | Paper/elec | On-site/Off-site |          |
|   | Subject files (memos, rules, schedules, etc.)   | Annual review        | Paper/elec | On-site/Off-site |          |
|   | Wills, testaments, codicils   | Permanent            | Paper/elec | On-site/Off-site |          |
| <b><u>Archives</u></b>  |   |                      |            |                  |          |
|   | Parish History Files  | Permanent            | Paper      | On-site/Off-site |          |
|   | Deceased Clergy Files   | Permanent            | Paper      | On-site/Off-site |          |
|   | Photo Files (priests, parishes, institutions, general)  | Permanent            | Paper/elec | On-site/Off-site |          |
|   | Clergy Card Files   | Permanent            | Paper      | On-site/Off-site |          |



| <b>Record Group</b>                   | <b>Type of Record</b>   | <b>Time</b>      | <b>Medium</b> | <b>Retained</b>  | <b>Disposal</b> |
|---------------------------------------|---|------------------|---------------|------------------|-----------------|
|                                       | Clergy Information Files  | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Baptism Record Index Files  | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Official Catholic Directories   | Permanent        | Paper         | On-site/Off-site |                 |
|                                       | Former Bishops' Files   | Permanent        | Paper         | On-site/Off-site |                 |
|                                       | Annuario Pontificio Directories   | Permanent        | Paper         | On-site/Off-site |                 |
|                                       | Parish Boundaries, Decrees and Maps   | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Historical Material (clippings, photos, booklets, etc. related to diocese and parishes) | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Diocesan Directories (file copies)  | Permanent        | Paper/elec    | On-site/Off-site |                 |
| <b><u>Publications</u></b>            |   |                  |               |                  |                 |
|                                       | Diocesan/Parish Histories   | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Diocesan/Parish Anniversary Books   | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Newsletters (diocesan, parish, affiliated organizations)                                | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Parish Directories  | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Parish Bulletins  | Permanent        | Paper/elec    | On-site/Off-site |                 |
| <b><u>Bishop's Office</u></b>         |   |                  |               |                  |                 |
|                                       | Bishop's Calendar   | One year         | Paper         | On-site/Off-site | Archives        |
|                                       | General Correspondence  | Perm → file      | Paper         | On-site/Off-site | Archives        |
|                                       | Holy See/Nuncio Correspondence  | Perm → file      | Paper         | On-site/Off-site |                 |
|                                       | Official Diocesan Correspondence  | Perm → file      | Paper         | On-site/Off-site |                 |
|                                       | USCCB Correspondence  | Perm → file      | Paper         | On-site/Off-site |                 |
| <b><u>Catholic Schools Office</u></b> |   |                  |               |                  |                 |
| General                               | Standardized Test Results   | 10 years         | Paper         | On-site/Off-site |                 |
|                                       | Curriculum Standards  | Until Superseded | Paper/elec    | On-site/Off-site |                 |
|                                       | School Calendar   | Current Year     | Paper/elec    | On-site/Off-site |                 |
|                                       | Crisis Management   | 1 Year           | Paper         | On-site/Off-site |                 |
|                                       | DEET Financial Assistance Requests  | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Enrollment Data   |                  | Paper/elec    | On-site/Off-site |                 |
|                                       | Civil Rights/Title IX Reports   | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | SEVIS/I-20 Foreign Student Program  | 3 Years          | Paper/elec    | On-site/Off-site |                 |
|                                       | Diocesan School Board Minutes   | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | Diocesan School Board By-Laws   | Until Superseded | Paper/elec    | On-site/Off-site |                 |
|                                       | Federal Program Requirements  | 5 Years          | Paper/elec    | On-site/Off-site |                 |
|                                       | Articles of Incorporations/Trusts   | Permanent        | Paper/elec    | On-site/Off-site |                 |
|                                       | NCEA Reports  | Permanent        | Paper/elec    | On-site/Off-site |                 |

| Record Group                        | Type of Record                                     | Time                       | Medium     | Retained                | Disposal |
|-------------------------------------|--|----------------------------|------------|-------------------------|----------|
| AHERA                               | School Management Plans                            | Permanent                  | Paper      | On-site/Off-site/school |          |
|                                     | Periodic Surveillance Reports                      | Permanent                  | Paper      | On-site/Off-site/school |          |
|                                     | Abatement Documents & Manifests                    | Permanent                  | Paper      | On-site/Off-site/school |          |
| TCCED                               | School Annual Report for Continued Accreditation   | Permanent                  | Paper      | On-site/Off-site/school |          |
|                                     | School Self-Study Document                         | Permanent                  | Paper      | On-site/Off-site/school |          |
|                                     | VT Consensus Report/Notification of Status         | Permanent                  | Paper      | On-site/Off-site/school |          |
|                                     | School Required Actions                            | Permanent                  | Paper      | On-site/Off-site/school |          |
|                                     | Interim Reports                                    | Permanent                  | Paper      | On-site/Off-site/school |          |
|                                     | Guide to Quality and Effectiveness Manual          | Until superseded + 5 years | Paper/elec | On-site/Off-site/school |          |
|                                     | TCCED Health Manual                                | Until superseded           | Paper/elec | On-site/Off-site/school |          |
|                                     | Individual Deficiency Removal Plans/Verification   | Termination + 5 years      | Paper      | On-site/Off-site/school |          |
| Education Personnel                 | Certificates and Licenses                          | Termination + 4 years      | Paper      | On-site/Off-site/school |          |
|                                     | Employee Service Record (including wage & salary)  | Permanent                  | Paper/elec | On-site/Off-site/school |          |
|                                     | Official Teacher Service Record                    | Permanent                  | Paper/elec | On-site/Off-site/school |          |
|                                     | Employment Applications (non-hires)                | 1 year from Receipt        | Paper/elec | On-site                 |          |
|                                     | Official Transcripts                               | Termination + 4 years      | Paper      | On-site/Off-site/school |          |
|                                     | Employment Contracts                               | Last eff. date + 4 years   | Paper      | On-site/Off-site/school |          |
|                                     | Grievance Records (not EEOC)                       | 2 years                    | Paper      | On-site/Off-site/school |          |
|                                     | Training and Educational Attainment Records        | Termination + 4 years      | Paper/elec | On-site/Off-site/school |          |
|                                     | CPE Course Rosters                                 | Termination + 4 Years      | Paper/elec | On-site                 |          |
| <b><u>Catechetical Services</u></b> |  |                            |            |                         |          |
|                                     | Catechetical Student Database                      | Death of student           | Electronic | On-site/Off-site        |          |
|                                     | Contracts with Educational Institutions            | Termination + 7 years      | Paper      | On-site/Off-site        |          |
|                                     | Course Evaluation                                  | 3 years                    | Paper      | On-site/Off-site        |          |
|                                     | Diocesan Ministry Day Program Booklet              | Permanent                  | Paper      | On-site/Off-site        |          |
|                                     | Handbooks and Manuals                              | 3 years                    | Paper/elec | On-site/Off-site        |          |
|                                     | Institutes (Christ the Servant and John Paul II)   | Permanent                  | Paper/elec | On-site/Off-site        |          |
|                                     | Parish Catechetical Profile                        | 5 years                    | Paper      | On-site/Off-site        |          |
|                                     | Renew/Why Catholic? Training Material              | 7 years                    | Paper/elec | On-site/Off-site        |          |
|                                     | TCC-RE Annual Reports                              | Permanent                  | Electronic | On-site/Off-site        |          |
|                                     | TCC-RE Diocesan Reports                            | 1 year                     | Electronic | On-site/Off-site        |          |
|                                     | Religious Education Reports (for diocesan offices) | Permanent                  | Paper/elec | On-site/Off-site        |          |

| Record Group                           | Type of Record                               | Time                     | Medium     | Retained         | Disposal |
|--|--|--------------------------|------------|------------------|----------|
| <b><u>Chancellor</u></b>               |  |                          |            |                  |          |
|  | Claimant Files                               | Settlement + 10 Years    | Paper      | On-site/Off-site |          |
|  | Ordination Records                           | Permanent                | Paper/elec | On-site/Off-site |          |
|  | Settlement Files                             | Permanent                | Paper      | On-site/Off-site |          |
|  | Clergy Assignment Letters (See Priest files) | Permanent → Priests File | Paper      | On-site/Off-site |          |
| <b><u>Communications</u></b>           |  |                          |            |                  |          |
|  | News Media Clippings                         | Permanent                | Paper/Elec | On-site/Off-site |          |
|  | Employee Performance Reviews                 | 3 years                  | Paper      | On-site/Off-site |          |
|  | Diocesan News Releases                       | 5 years                  | Electronic | On-site/Off-site |          |
|  | Pastoral Center News                         | Permanent                | Electronic | On-site/Off-site |          |
|  | Clergy Newsletter                            | Permanent                | Electronic | On-site/Off-site |          |
| <b><u>Newspaper</u></b>                |  |                          |            |                  |          |
|  | Newspaper Back Issues                        | Permanent                | Paper/elec | On-site/Off-site |          |
|  | Photos                                       | Permanent                | Paper/elec | On-site/Off-site |          |
|  | Subscription Database                        | Permanent                | Paper/elec | On-site/Off-site |          |
|  | Website                                      | Permanent                | Electronic | On-site/Off-site |          |
|  | Freelancer Information                       | Permanent                | Electronic | On-site/Off-site |          |
|  | Advertising Contracts                        | Permanent                | Paper/elec | On-site/Off-site |          |
| <b><u>Financial and Accounting</u></b> |  |                          |            |                  |          |
| Risk Management                        | Incident Reports (accidents/injury)          | 7 years                  | Paper/elec | On-site/Off-site |          |
|  | Employee Medical Complaints                  | 7 years                  | Paper/elec | On-site/Off-site |          |
|  | Employee Medical Records                     | 7 years                  | Paper/elec | On-site/Off-site |          |
|  | Environmental Test Records/Reports           | Permanent                | Paper/elec | On-site/Off-site |          |
|  | Hazardous Exposure Records                   | Permanent                | Paper/elec | On-site/Off-site |          |
|  | Toxic Substance Exposure Reports             | Permanent                | Paper/elec | On-site/Off-site |          |
|  | Workers Compensation Records                 | 12 years                 | Paper/elec | On-site/Off-site |          |
| Payroll                                | Permanent Earnings and Records               | Termination + 7 years    | Paper/elec | On-site/Off-site |          |
|  | Attendance Records                           | Termination + 7 years    | Paper/elec | On-site/Off-site |          |
|  | Employee Contracts                           | Termination + 7 years    | Paper/elec | On-site/Off-site |          |
|  | Employee Deduction Authorization             | Termination + 7 years    | Paper/elec | On-site/Off-site |          |
|  | Employee Salary Schedules                    | Termination + 7 years    | Paper/elec | On-site/Off-site |          |
|  | Labor Contracts                              | Termination + 7 years    | Paper/elec | On-site/Off-site |          |
|  | W-2 Years Forms                              | Filing + 7 years         | Paper/elec | On-site/Off-site |          |

| Record Group             | Type of Record                                       | Time                 | Medium     | Retained         | Disposal |
|--------------------------|--|----------------------|------------|------------------|----------|
|                          | W-4 Years Forms                                      | Filing + 7 years     | Paper/elec | On-site/Off-site |          |
|                          | Time Cards   | Filing + 3 years     | Paper/elec | On-site/Off-site |          |
|                          | Time Records   | Filing + 3 years     | Paper/elec | On-site/Off-site |          |
| Banking                  | Bank Deposits  | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Bank Statements                                      | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Cancelled Checks                                     | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Check Registers/Stubs                                | 7 years              | Paper/elec | On-site/Off-site |          |
| General                  | Audit Reports  | Permanent            | Paper/elec | On-site/Off-site |          |
|                          | Balance Sheets, Annual                               | Permanent            | Paper/elec | On-site/Off-site |          |
|                          | Balance Sheets, Monthly/Quarterly                    | 1 year               | Paper/elec | On-site/Off-site |          |
|                          | Budgets, Approved, Revised                           | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Financial Reports, Annual                            | Permanent            | Paper/elec | On-site/Off-site |          |
|                          | Financial Reports, Monthly                           | 1 year               | Paper/elec | On-site/Off-site |          |
|                          | Financial Statements                                 | Permanent            | Paper/elec | On-site/Off-site |          |
| Investment/<br>Insurance | Certificates of Deposit, Cancelled                   | Redemption + 3 years | Paper/elec | On-site/Off-site |          |
|                          | Insurance Policies                                   | Permanent            | Paper/elec | On-site/Off-site |          |
|                          | Mortgage Records                                     | Permanent            | Paper/elec | On-site/Off-site |          |
|                          | Letters of Credit                                    | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Securities Sales                                     | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Stock Investment                                     | Sale + 7 years       | Paper/elec | On-site/Off-site |          |
| Accounting               | Accounts Payable, Invoices                           | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Accounts Payable, Ledgers                            | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Accounts Receivable, Ledgers                         | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Credit Card Statements/Charge Slips                  | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Invoices and Paid Bills, Major Building Construction | Permanent            | Paper/elec | On-site/Off-site |          |
|                          | Invoices and Paid Bills, General Accounts            | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Cash Books   | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Cash Journals  | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Cash Journal, Receipts on Offerings and Pledges      | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Receipts   | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Mortgage Payments                                    | 7 years              | Paper/elec | On-site/Off-site |          |
|                          | Chart of Accounts                                    | 7 years              | Paper/elec | On-site/Off-site |          |

| <b>Record Group</b> | <b>Type of Record</b>  | <b>Time</b>                | <b>Medium</b> | <b>Retained</b>  | <b>Disposal</b> |
|---------------------|--|----------------------------|---------------|------------------|-----------------|
| Other Records       | General Ledger, Annual   | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Journals, General and Specific Funds   | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Journal Entry Sheets   | 7 years                    | Paper/elec    | On-site/Off-site |                 |
|                     | Ledgers, Subsidiary  | 7 years                    | Paper/elec    | On-site/Off-site |                 |
|                     | Payroll Journals   | 7 years                    | Paper/elec    | On-site/Off-site |                 |
|                     | Payroll Registers (summary schedule of earnings, deductions & accrued leave)     | 7 years                    | Paper/elec    | On-site/Off-site |                 |
|                     | Pension Records  | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Pledge Registers/Ledgers   | 3 years                    | Paper/elec    | On-site/Off-site |                 |
|                     | Permanently Restricted Gift Documents  | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Temporarily Restricted Gift Documents  | 3 years after restrictions | Paper/elec    | On-site/Off-site |                 |
| Tax Records         | Employment Taxes (Contributions and payments including withholding & FICA)       | File + 7 years             | Paper/elec    | On-site/Off-site |                 |
|                     | W-2 Years Forms  | File + 7 years             | Paper/elec    | On-site/Off-site |                 |
|                     | W-4 Years Forms  | File + 7 years             | Paper/elec    | On-site/Off-site |                 |
|                     | IRS Exemption Determination Letters (other than OCD listed organizations)        | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Form 990   | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | IRS Exemption Determination Letters (income, excise, property, sales, use, etc.) | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Form 641   | Permanent                  | Paper/elec    | On-site/Off-site |                 |
| Property Records    | Architectural Records, Blueprints, Building Designs, Specifications              | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Architectural Drawings   | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Deeds Files  | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Mortgage Documents   | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Property Appraisals  | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Real Estate Surveys/Plots, Plans   | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Title Search Papers and Certificates   | Permanent                  | Paper/elec    | On-site/Off-site |                 |
| Cemetery Records    | Account Cards (record of lot ownership and payments)                             | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Annual Report  | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Bank Statements  | 7 years                    | Paper/elec    | On-site/Off-site |                 |
|                     | Board Minutes  | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Burial Cards (record of interred's name, date of burial, etc.)                   | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Burial Records (record of interred's name, date of burial, etc.)                 | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Contracts Documenting Lot Ownership  | Permanent                  | Paper/elec    | On-site/Off-site |                 |
|                     | Correspondence   | BANR                       | Paper/elec    | On-site/Off-site |                 |

| Record Group                    | Type of Record  | Time                  | Medium     | Retained         | Disposal |
|---------------------------------|---|-----------------------|------------|------------------|----------|
|                                 | General Ledger  | Permanent             | Paper/elec | On-site/Off-site |          |
|                                 | Lot Maps  | Permanent             | Paper/elec | On-site/Off-site |          |
| <b><u>Human Resources</u></b>   |   |                       |            |                  |          |
| Administrative Records          | Employee Policy Manual                                      | Superseded + 4 Years  | Paper/elec | On-site/Off-site |          |
|                                 | Job Descriptions  | Superseded + 4 Years  | Paper/elec | On-site/Off-site |          |
|                                 | Organizational Chart  | While Current         | Paper/elec | On-site/Off-site |          |
|                                 | I-9 Years Audit   | Permanent             | Electronic | On-site/Off-site |          |
|                                 | Rejected Applications/Resumes                               | 1 Year after Receipt  | Paper/elec | On-site/Off-site |          |
| Personnel Records               | Employee Application  | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Resume  | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Employee Contracts/Offer Letters                            | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Salary Information  | Termination + 4 years | Paper/elec | On-site/Off-site |          |
|                                 | Attendance Records (jury, PTO, STD, LTD, FMLA, Bereavement) | Termination + 4 years | Paper/elec | On-site/Off-site |          |
|                                 | Eligibility Verification Form I-9 Years                     | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Performance Reviews   | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Write-Ups   | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Promotions/Transfers  | Termination + 4 years | Paper      | On-site/Off-site |          |
| Benefit Records                 | Open Enrollment   | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | New Hire  | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Life Event  | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Cont. of Benefits   | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Term. of Benefits   | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Disability Records STD/LTD                                  | Termination + 4 years | Paper/elec | On-site/Off-site |          |
|                                 | FMLA  | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | 403B Retirement Plan  | Termination + 4 years | Paper      | On-site/Off-site |          |
|                                 | Life Insurance Policies                                     | Termination + 4 years | Electronic | On-site/Off-site |          |
|                                 | Benefit Plan Description                                    | Rollout + 4 years     | Electronic | On-site/Off-site |          |
|                                 | Benefit Plan Annual Reports                                 | 6 years               | Electronic | On-site/Off-site |          |
|                                 | Personnel File  | Termination + 4 years | Paper      | On-site/Off-site |          |
| <b><u>Pastoral Planning</u></b> |   |                       |            |                  |          |
|                                 | Ad Limina Reports (Quinquennial Report)                     | Permanent             | Paper      | On-site/Off-site |          |
|                                 | Annual Vatican Report                                       | 5 Years               | Paper      | On-site/Off-site |          |
|                                 | Official Catholic Directory Report                          | 5 Years               | Paper      | On-site/Off-site |          |

| <b>Record Group</b>            | <b>Type of Record</b>                              | <b>Time</b>                   | <b>Medium</b> | <b>Retained</b>  | <b>Disposal</b> |
|--------------------------------|--|-------------------------------|---------------|------------------|-----------------|
|                                | Official Catholic Directory Entity Financials      | Current + 1 Year              | Paper         | On-site/Off-site |                 |
|                                | May and October Mass Counts                        | Permanent                     | Paper         | On-site/Off-site |                 |
|                                | Census Records (Parish)                            | Permanent                     | Paper/elec    | On-site/Off-site |                 |
| <b><u>Safe Environment</u></b> |  |                               |               |                  |                 |
|                                | Application  | Permanent                     | Paper         | On-site/Off-site |                 |
|                                | Screening Form                                     | Permanent                     | Paper/elec    | On-site/Off-site |                 |
|                                | Interviews   | Permanent                     | Paper         | On-site/Off-site |                 |
|                                | References   | Permanent                     | Paper/elec    | On-site/Off-site |                 |
|                                | Criminal Background Check                          | Permanent                     | Paper/elec    | On-site/Off-site |                 |
|                                | Training Records                                   | Permanent                     | Paper/elec    | On-site/Off-site |                 |
|                                | Policy Acknowledgment                              | Permanent                     | Paper/elec    | On-site/Off-site |                 |
|                                | Computer/Internal Policy                           | Permanent                     | Paper/elec    | On-site/Off-site |                 |
|                                | CPS Notifications                                  | Permanent                     | Paper/elec    | On-site/Off-site |                 |
|                                | Good Standing Records                              | Current + 1 Year              | Paper/elec    | On-site/Off-site |                 |
|                                | Non-Parish Organization Files                      | ACT + 3 Years                 | Paper/elec    | On-site/Off-site |                 |
|                                | Parish/School Audits                               | Permanent                     | Paper/elec    | On-site/Off-site |                 |
|                                | USCCB Charter Compliance Audit                     | Permanent                     | Paper/elec    | On-site/Off-site |                 |
| <b><u>Tribunal</u></b>         |  |                               |               |                  |                 |
|                                | Prenuptial Files                                   | 6 years paper/then electronic | Paper/elec    | On-site/Off-site |                 |
|                                | Nulity File Decision                               | Permanent                     | Paper         | On-site/Off-site |                 |
|                                | Nulity File Acta (other than decisions)            | Permanent                     | Paper         | On-site/Off-site |                 |
|                                | Canonical Affairs Committee Records                | 5 Years                       | Paper/elec    | On-site/Off-site |                 |
| <b><u>Vicar for Clergy</u></b> |  |                               |               |                  |                 |
|                                | Priests' Personnel Files                           | Permanent                     | Paper         | On-site/Off-site |                 |
|                                | Deacons' Personnel Files                           | Permanent                     | Paper         | On-site/Off-site |                 |
|                                | Clergy Rescript Files                              | Permanent                     | Paper         | On-site/Off-site |                 |
| <b><u>Youth Ministry</u></b>   |  |                               |               |                  |                 |
|                                | Waiver of Liability Forms                          | 7 years                       | Paper         | On-site/Off-site |                 |
|                                | Medical Release Forms                              | 7 years                       | Paper         | On-site/Off-site |                 |
|                                | Code of Conduct Forms                              | 7 years                       | Paper         | On-site/Off-site |                 |
|                                | Incident Report Forms                              | 7 years after resolution      | Paper         | On-site/Off-site |                 |
|                                | Youth, Young Adult & Campus Ministry Event Records | Permanent                     | Paper         | On-site/Off-site |                 |

## V. Parish Financial Management

There are more than 17,500 parishes in the United States with a vast amount of church assets that are entrusted to them. Strong systems of internal controls are needed to reduce the risk of fraud, misuse, waste or embezzlement. An effective internal control environment consists of written policies that are communicated regularly, well-documented procedures that are operating effectively, proper and frequent training of personnel, and effective monitoring of systems and procedures, with appropriate feedback. The existence and effectiveness of parish internal controls should be evaluated periodically.

Each diocese should consider implementing the financial management practices outlined herein to enhance its internal control environment. The Committee on Budget and Finance of the USCCB has endorsed these recommendations. These recommendations are designed to improve existing diocesan policies and procedures relative to financial management at the parish level and, therefore, should be viewed in the context of enhancements to, and/or a re-doubling of, existing efforts.

In the foreword to *Diocesan Internal Controls*, which was created by the United States Conference of Catholic Bishops' Accounting Practices Committee and published by the USCCB Committee on Budget and Finance in 1995, Archbishop Murphy, then-Treasurer, notes that "Canon 1284 states that all administrators are to perform their duties with the diligence of a good householder." While the parish pastor/administrator is the administrator of the parish and its property, it is the responsibility of the diocesan bishop "to exercise careful vigilance over the administration of all the goods which belong to the public juridic persons subject to him, without prejudice to legitimate titles which attribute more significant rights to him" (c. 1276 §1). Furthermore, the diocesan bishop is "to take care of the ordering of the entire matter of the administration of ecclesiastical goods by issuing special instructions within the limits of universal and particular law" (c. 1276 §2). The executive summary of that document points out: "Although the bishop will not become too involved in the details of the internal control system, he is the only person who has the power to ensure that each area of a diocese carries out its responsibility for the system. The proper tone must be set at the top of the organization, and for a diocese, that is the bishop." As such, there must be effective oversight by the bishop for compliance with all diocesan policies in each area of the diocese, and each of the following recommendations are made within that overarching mindset.

1. A properly functioning parish finance council is integral to good parish financial management, is required by canon law (c. 537), and a key element of a parish internal control system. To that end, and similar to the USCCB resolution entitled *Diocesan Financial Reporting*, each parish should send a letter to the diocesan bishop annually containing:
  - a. The names and professional titles of the members of the parish finance council.
  - b. The dates on which the parish finance council has met during the preceding fiscal year and since the end of the fiscal year.
  - c. The date(s) on which the approved (i.e. by the parish finance council) parish financial statements/budgets were made available to the parishioners during the



preceding fiscal year and since the end of the fiscal year. A copy of said published financial statements/budgets should be provided to the bishop.

- d. A statement signed by the parish pastor and the finance council members that they have met, developed, and discussed the financial statements and budget of the parish.
2. Thorough diocesan training should be provided by the diocese to parish finance council members relative to their roles and responsibilities.
  3. Diocesan policies addressing conflicts of interest, protection of whistleblowers, and fraud (including prosecution in all cases) should be regularly communicated by the diocese to all parishes.
  4. All parishes should complete an annual internal control questionnaire, and a proper review and follow-up made by qualified diocesan personnel.
    - a. The diocesan recommended internal controls should focus on providing recommendations that create strong internal control framework over assigning tasks to specific roles at the parish. There is a wide disparity of staffing levels across parishes in the United States and within each diocese. As a result, in some instances, it may not be practical or appropriate for a parish to implement all recommended internal controls developed by the diocese. However, parishes should work to achieve the underlying spirit of diocesan recommended internal controls, with a focus on key controls, using alternative methods that are achievable by the parish. For example, to ensure segregation of duties over review of bank reconciliations, diocesan control recommendations should advise that qualified individuals separate from the preparer review all bank reconciliations in a timely manner, rather than requiring the chair of the Finance Council review all bank reconciliations.
  5. Parish financial manuals should be developed by dioceses, containing best practices, similar to *Diocesan Financial Issues* which has been developed for dioceses.
  6. Standard parish accounting policies and financial reporting standards should be developed by the diocese, including a standard chart of accounts for all parishes and schools.
  7. Financial training should be integrated into current seminarian programs such that students will be better prepared to handle these eventualities.

The following tools have been developed to assist dioceses in implementing the above recommendations:

- a. Sample parish reporting form to be used for certification of the parish finance council's activities (Sample A)
- b. Sample agenda for parish finance council training (Sample B)
- c. An example of parish finance council guidelines (Sample C)

- d. Sample parish internal control questionnaire (Sample D)
- e. Sample parish accounting policies and financial reporting standards (Sample E)
- f. Sample Diocesan Decree on Parish Finance Councils (Sample F)

## Sample A: Parish Reporting Form

### *Parish Letterhead*

Dear Bishop:

Enclosed are the financial statements that were made available to parishioners for the fiscal period ended \_\_\_\_\_. Please accept this statement as the annual certification concerning financial management of the parish for the current fiscal period. This is to certify to the following:

1. That the annual budget was made available to parishioners on \_\_\_\_\_ (date);
2. That periodic financial statements (including, but not limited to a Statement of Financial Position and Statement of Activities) were made available to parishioners, as follows:

Date of Financial Statements

Date Issued to Parishioners

- 
- 
- 
- 

3. That the finance council regularly reviews and discusses the budget and periodic financial statements. Meetings of the finance council during the above period, and since the end of the period, were held on the following dates:

- 
- 
- 
- 
-

The above is hereby attested to by the Pastor and the members of the Parish Finance Council:

| <u>Printed Name</u> | <u>Occupation</u> | <u>Signature</u> |
|---------------------|-------------------|------------------|
| _____               | _____             | _____            |
| _____               | _____             | _____            |
| _____               | _____             | _____            |
| _____               | _____             | _____            |
| _____               | _____             | _____            |
| _____               | _____             | _____            |
| _____               | _____             | _____            |
| _____               | _____             | _____            |
| _____               | _____             | _____            |
| _____               | _____             | _____            |

*Insert diocesan-specific requirements for certification here.*

Sincerely yours,

Pastor

cc: Diocesan Chief Financial Officer

## Sample B: Parish Finance Council Training

### Introduction

The Parish Finance Council (the “Council”) is integral to good parish financial management. The Council is a consultative body that assists the pastor in the financial administration of the parish. Canon law mandates that all parishes have a Finance Council:

In each parish there is to be a finance council which is governed, in addition to universal law, by norms issued by the diocesan bishop and in which the Christian faithful, selected according to these same norms, are to assist the pastor in the administration of the goods of the parish, without prejudice to the prescript of Canon 532 (c. 537).

To be effective, the Parish Finance Council should meet regularly (no less than quarterly) with specific agendas and should have access to all relevant financial information of the parish. The Council should consist of no less than three members (excluding pastor and staff) who are chosen based on demonstrable skills or expertise in management, finance and accounting.

The Parish Finance Council assists with the financial management of the parish. Major responsibilities of the Parish Finance Council include input to, and review of the parish annual budget and periodic financial statements; review of internal controls and procedures; and planning for the temporal needs of the parish.

Each diocese should consider developing a Parish Finance Council charter containing guidelines for the proper functioning of the Council, an example of which is attached as Sample C – Parish Finance Council Guidelines. Some of these items may be defined as local norms issued by the diocesan bishop, an example of which is attached as Sample F. In addition, each diocese should consider providing periodic training for Parish Finance Council members relative to their roles and responsibilities. Suggested topics for training include:

1. Review of the Parish Finance Council Guidelines: roles & responsibilities
  - a. Decree on Parish Finance Councils
  - b. Consultative nature of the council
  - c. Recommended areas for consultation
  - d. Membership
    - i. Representation and background
    - ii. Number of members
    - iii. Officers
    - iv. Conflicts of interest
    - v. Role of parish employees
    - vi. Terms

- e. Meeting protocol
    - i. Scheduling meetings
    - ii. Agendas
    - iii. Minutes
    - iv. Confidentiality
    - v. Record Retention
  - f. Subcommittees
  - g. Relationship to other parish groups/councils
  - h. Checklist of major activities
2. Financial inter-relationship between the Parish Finance Council and the diocesan Central Administrative Office:

*Review and discussion of:*

- Services provided by the Central Office
- Assessments
- Diocesan/Special collections

3. Diocesan-issued financial policies & guidelines for parishes

*Review and discussion of:*

- Financial reporting requirements of the diocese
- Clergy remuneration policy
- Other significant policies

4. Internal control considerations

- Diocesan internal control questionnaire (copy provided)

5. Not-for-profit accounting

- Restricted vs. unrestricted donations
- Reporting for programs
- Accounting Guidelines specific to the diocese

6. Legal and regulatory compliance issues

## Sample C: Parish Finance Council Guidelines

*The Archdiocese of Chicago is acknowledged, and their effort in developing the initial draft of this Sample Parish Finance Council Charter is gratefully appreciated.*

This document is intended as an overview of the responsibilities and roles of Parish Finance Councils as defined by Canon Law and best practices of parish administration. An active and well-formed Parish Finance Council is an important and necessary support to the parish administrator in fulfilling his duty of being a good steward of parish resources. A Parish Finance Council supports good management of a parish and accountability to the diocese and to the parishioners. Each individual diocese is encouraged to review this document and the best practices contained herein and modify the document to conform it to the specific norms and particular law of that diocese. For simplicity within this document, references to a “pastor” should be understood to mean a pastor or parish administrator.

### PARISH FINANCE COUNCIL GUIDELINES

#### INTRODUCTION AND BACKGROUND

Parish Finance Councils assist the pastor in the administration of parish temporal matters. An active, well-formed Parish Finance Council is a key element for promoting the financial health of a parish, assuring accountability and assisting the pastor with his temporal responsibilities.

In the administration of temporal goods of the parish, Canon 532 defines the role of the pastor as the authoritative representative of the parish. Canon 532 says,

“The pastor represents the parish in all juridic affairs in accord with the norm of law; he is to see to it that the goods of the parish are administered in accord with the norms of canons 1281-1288.”<sup>1</sup>

Canon 537 introduces the Parish Finance Council as a **mandated** body having an advisory and consultative role with the pastor. Canon 537 says,

“Each parish is to have a finance council which is regulated by universal law as well as by norms issued by the diocesan bishop; in this council the Christian faithful, selected according to the same norms, aid the pastor in the administration of parish goods with due regard for the prescription of Canon 532.”

Therefore, while Canon Law vests much authority in the pastor, it also places an expectation on him to be a good steward of the resources entrusted to him and fulfill his office with the diligence of a good housekeeper. In addition to specifically requiring the pastor to seek counsel from his finance council, Canon Law also suggests that good stewardship requires the inclusion of the Christian faithful and utilization of their gifts in the administration of the resources of the Church and specifies that this expectation for good stewardship is to be further defined by the bishop through the establishment of particular norms which mandate how a pastor is required to utilize his Parish Finance Council, and how the finance council is expected to operate. Additionally,

depending on the legal structure of a parish (either canonically or civilly), its corporate statutes may define additional roles and responsibilities for the Parish Finance Council.

## **CONSULTATIVE BODY TO PASTOR**

The Finance Council works closely with the pastor, who is accountable to the diocesan bishop for the administration and stewardship of the temporal goods of the parish. The pastor, according to Canon Law, has among his responsibilities, the responsibility for parish financial and temporal management. The Parish Finance Council does not have decision making authority, consultation is at the heart of the decision-making process – sharing information, listening, contributing to the discussion, and promoting consensus.

Note: the full texts of Canons 1281-1288 may be found in Appendix A to this document.

Canon law states that the pastor is obligated to consult the Finance Council on certain matters. Although the pastor is not obliged to follow the recommendations of the Finance Council, the pastor should not act against such advice, especially when there is consensus, unless there is an overriding reason. In other words, the prudent pastor would not ignore the advice of the Finance Council unless there was a serious reason to do so. When acting contrary to its recommendations the pastor should provide an explanation to the Finance Council regarding the reasons for his decision.

In order to be effective in their responsibilities as members of the Parish Finance Council, members should have a love for the Church and its mission and develop a thorough understanding of the parish's mission, goals, people and other resources. The members should have knowledge of diocesan statutes and policies regarding temporal issues and other financial matters. It is the pastor's responsibility to give the members appropriate background and enrichment as well as appropriate access to financial data and supporting information.

## **Recommended Areas for Finance Council Consultation**

1. The advice of the Finance Council should be sought both for acts of ordinary administration and acts of extraordinary administration. However, the degree of consultation varies. For certain actions of day-to-day administration, the pastor does not need any specific authorization to carry out such acts but may find it helpful to seek advice of the Parish Finance Council even in these matters. For example, while the purchase of ordinary amounts of office supplies is within the pastor's authority, the Finance Council may provide useful advice on strategies that reduce the cost of such recurring purchases.
2. Diocesan norms require the pastor to consult with the Parish Finance Council at some level of financial commitment. For example, the pastor must consult with the Parish Finance Council regarding any commitment of parish resources over some fixed dollar amount such as \$10,000 or \$25,000. Alternatively, this threshold may be tied to the level of parish income, such as any commitment more than 1% of parish revenue. Commitments would include, but not be limited to, the initiation or modification of purchases, sales, leases, gifts, loans to others, and borrowings.



3. A parish will also need to seek written approval of the diocesan bishop prior to performing extraordinary acts of administration and must consult with his Finance Council prior to seeking approval of his bishop (c. 1281§1). Extraordinary acts of administration are defined by local norms and sometimes by the particular statutes of the parish. Extraordinary acts taken without such approval of the diocesan bishop are invalid acts and may also be invalid from a civil law standpoint. Examples of actions that some dioceses consider to be extraordinary acts of administration include: instances where the expenditure is greater than a fixed dollar amount such as \$20,000 or \$40,000 as determined in a particular diocese and involves a contract (employment, construction/repair, equipment, consulting, or services such as landscaping or cleaning), the acquisition or alienation of real property, the entering of a lease, the collateralization or mortgaging of real property, the sale of religious artifacts that would be considered as part of a parish's patrimony (e.g. stained glass windows) and other matters.
4. The advice of the Finance Council should be sought in the management of parish funds and banking arrangements. A limited number of bank accounts should be established and procedures for approving new accounts should be in place. The Finance Council should be consulted before a new bank account is opened. This also applies to bank accounts for auxiliary groups.
5. The Finance Council should review the parish annual budget and parish annual report. They should ordinarily be involved in the preparation of both reports, particularly the budget report. After review, the chairperson of the Finance Council is to co-sign each report before it is submitted to the diocesan bishop indicating consultation with the Finance Council.
6. Annually, along with the parish annual report, each parish is required to send a letter to the diocesan bishop containing:
  - a. The names and professional titles of the members of the Parish Finance Council.
  - b. The dates on which the Parish Finance Council met during the fiscal year for which the report was prepared, along with the dates of all meetings since fiscal year end.
  - c. The date(s) on which the approved (i.e. by the Parish Finance Council) parish financial statements/budgets were made available to parishioners during the preceding fiscal year and since the end of the fiscal year. A copy of said published financial statements/budgets should be provided to the bishop.
  - d. A statement signed by the pastor or parish administrator and the Parish Finance Council members that they have met, developed, and discussed the financial statements and budget of the parish.
7. The Finance Council should provide assistance in the formulation and communication of the Annual Financial Report to the parish community, as required by Canon 1287 §2. The Annual Financial Report to the parish community often includes more than just financial information (e.g. description of key issues, programs and events, statistics related to church attendance, sacraments, school and religious education enrollment, etc.). Additionally, many parishes find it helpful to provide parishioners with semi-annual or even quarterly

updates on the parish's financial condition. Understandable, regular and complete communication to parishioners is a key responsibility of the parish administrator and an important area for the Parish Finance Council to assist. Communication keeps parishioners informed of the parish's condition, its priorities, its needs, and progress on previously announced initiatives.

8. The Finance Council should review any indebtedness of the parish and assist the pastor in fulfilling his obligations under Canon 1284 §5, i.e. to “pay the interest on a loan or mortgage when it is due and take care that the capital debt itself is repaid in due time.” Planning for debt repayment should be an integral part of the budget process (in some cases local norms require the Finance Council chairperson to co-sign, with the pastor, any parish loan to acknowledge that the loan has been discussed with the Finance Council).
9. Regularly review periodic (at least quarterly) financial reports – balance sheet, income statements, comparisons to budget as well as prior year results and cash flow analysis.
10. Detail of budget to actual comparisons should be reviewed by individual program category, such as the elementary school and religious education. Significant variances from budgeted figures should be investigated and explained.
11. Review of internal control and procedures:
  - a. If written procedures do not exist, participate in the development of written procedures for cash receipts, cash disbursements, and administration of bank accounts, petty cash, and payroll.
  - b. Review the financial reports for parish general operations, parish school(s) and other parish organizations or programs with bank accounts or revenue collection responsibilities, to determine that proper accounting practices and internal control procedures are in place.
  - c. Alternatively, after consultation with the diocesan finance office, the parish may engage a CPA firm to perform an audit, a review, or agreed upon procedures.
12. Review the activities of any parish auxiliary groups and verify cash balances of bank accounts. Annually meet with auxiliary groups to review the reporting of past year's activities and a review of the budget for the coming year. Assess the accounting practices and internal control procedures in use to ensure compliance with diocesan policies. Review the activities of the auxiliary groups to assure that they are not jeopardizing the tax-exempt status of the parish.
13. Consult on the construction or renovation of parish facilities, the sale or purchase of parish property, and lease agreements. The Finance Council assists the pastor in planning for repair, replacement, or service of property and equipment to ensure that the parish buildings and property are adequately maintained. Review maintenance and utility costs seeking to minimize costs through preventative maintenance, energy conservation, and the implementation of risk management programs and recommendations.

14. Assess effectiveness of existing fund-raising programs and recommend new programs or changes to existing programs if revenues are insufficient. Support parish and diocesan stewardship programs.
15. Review of fundraising activities, such as raffles, bingo, and concession sales for acquisition of required licenses, support documentation for tax filings, actual filings of tax returns and general compliance with federal, state, and local laws.
16. Provide advice on matters requiring proxies by the parish civil corporation when it is incorporated separately.
17. Become knowledgeable on diocesan fiscal policies and norms to provide advice on implementation. Evaluate compliance with diocesan fiscal policies and assist the pastor in meeting these obligations.
18. Provide advice on what the parish needs to do to comply with diocesan policies and USCCB recommendations with respect to conflicts of interest, protection of whistleblowers and fraud detection, reporting and prevention.
19. Provide advice on how to use undesignated bequests or other unbudgeted revenue.
20. Provide advice on hiring and evaluating a business manager or anyone providing business services to the parish. Provide advice on training that might be helpful for parish staff.
21. Where possible, help the pastor establish and manage a parish endowment program. Particularly, help ensure that the purpose of the endowment is well-defined considering the long-term needs and life of the parish and that any restricted gifts are first reviewed to ensure that the parish can accept the restriction and, once accepted, that the funds are spent consistent with the donor restriction(s). Similarly, provide advice and oversight if an endowment already exists. Acceptance of an endowment may be considered an act of extraordinary administration, requiring the written permission of the bishop in addition to the approval of the pastor.

## **MEMBERSHIP**

The Parish Finance Council is about the life of a community of faith and, as such, its members should be members of that community of faith. As in other matters, the Pastor may use his discretion in the selection of qualified members from the parish community.

### **1. Representation**

- a. Members should be drawn from the parish community and reflect its diversity. This requirement may be waived if special expertise is sought. Where appropriate, outside advice and counsel can also be engaged to obtain needed specific expertise.
- b. Members of the Parish Finance Council should be chosen based on demonstrable skills or expertise in management and/or finance. Skill sets to consider include

business, law, accounting, and communications. Additionally, persons with professional knowledge and experience in engineering, construction, maintenance, and purchasing could also make a significant contribution and should be recruited when available. Expertise can vary widely and include a business executive, accountant, lawyer, and small business owner (any business, even a small neighborhood business). The unique talents within the parish community should be sought. A parish Time, Talent, and Treasure survey may be helpful in identifying parishioners having the desired skills and willingness to serve.

## **2. Number of Members**

- a. Membership should consist of no less than three members.
- b. A quorum shall consist of the majority of members.
- c. It is recommended that the Parish Finance Council have an odd number of members and that, except for unusual circumstances, membership be capped at no more than nine voting members.
- d. It may be helpful to form subcommittees.

## **3. Officers**

- a. The officers of the Parish Finance Council shall be a Chairperson and a Secretary.
- b. The pastor shall appoint the Chairperson after the members have gone through a period of discernment.
- c. The Chairperson will preside in a parliamentary manner at all meetings and, in consultation with the pastor or Parochial Administrator, will be responsible for selecting the hour and location of meetings, preparing the meeting agenda, and any other duties so assigned by the Pastor.

## **4. Conflicts of Interest/Preclusion to Membership**

- a. Parish Finance Council members owe the parish a duty of loyalty. The duty of loyalty requires a Parish Finance Council member to act in the interest of the parish rather than in the personal interest of the member or some other person or organization. In particular, the duty of loyalty requires a Parish Finance Council member to avoid conflicts of interest that are detrimental to the parish.
- b. Any person who may have a conflict of interest in view of other services, either paid or unpaid, rendered to the parish by the Parish Finance Council member, the member's family or the member's business is ineligible to serve as a member of the Parish Finance Council.
- c. On an annual basis the Parish Finance Council members should disclose in writing any known financial interest that the individual, or a member of the individual's family, has in any business entity that transacts business with the parish.
- d. No parish employee or member of the family of an employee or relative of the pastor may serve on the finance council.
- e. Members of the Parish Finance Council may serve in other volunteer service roles in the parish such as other committees or boards if, in the judgment of the pastor,

such dual service will not create conflict of interest situations. The role of the Parish Finance Council must never be impaired.

- f. No member should serve on the Parish Finance Council at the same time as a closely related person (e.g. husband and wife, mother and son).

## **5. Role of Parish Employees**

Parish employees are not members of the Parish Finance Council; they are staff and support the Parish Finance Council. Parish employees should be available to answer questions regarding parish programs, accounting, financial reporting, and internal controls. The Finance Council should be provided relevant and timely information including financial reports (balance sheet, income statement, budget to actual comparisons, loan balance payments and interest payments, investment of surplus funds, and status of fundraising drives) to review.

The Parish Business Manager should attend meetings in a consultative capacity. Likewise, when parish buildings and grounds are to be discussed, inviting staff responsible for these areas can enhance the discussion. While staff members may present proposals, answer questions, and explain details, they must remain aware of and allow the Council to discuss and come to a consensus.

## **6. Acknowledgment of Members**

Acknowledge members' contributions to the Finance Council and subcommittees at meetings, in the minutes, in the bulletin and in other appropriate ways.

## **7. Terms**

- a. Members are to be appointed by the pastor for fixed terms to be determined at the local level and may be reappointed or terminated in this role by the pastor at the pastor's sole discretion. It is suggested that reappointments are limited to a specific period of time. It may be helpful to stagger the terms so that there is continuity of service and no disruption to the function of the Finance Council. For example, a parish may adopt a term of three years, renewable once.
- b. When a pastorate becomes vacant, it is recommended that the Parish Finance Council remain in place to assist the administrator and to provide continuity in a transition. After a suitable period of transition with a new pastor, the new pastor can determine whether to ask the council members to complete their respective terms or to ask some or all of the members to resign so that new members can be recruited to the Parish Finance Council.

## **MEETING PROTOCOLS**

In striving for openness and accountability in its practices, meeting minutes summarizing the items discussed and the decisions reached should be recorded. Prepared agendas, distributed in advance, will keep meetings focused.

Plan meetings in advance and create an annual schedule of meeting dates and times. This will increase participation by members.

### **1. Schedule Meetings**

Schedule meeting times at least once a quarter, or more frequently if required. Some parishes use a format of the finance council meeting every other month with subcommittees meeting during the off months. When the finance council is operating in a healthy environment, their work can encompass 12 meetings per year. Meeting times and dates should be predictable, such as a day and week of each month. Since the purpose of the Parish Finance Council is to provide advice and support to the pastor, the pastor should be present at the Parish Finance Council meetings.

Formulate a communication method among officers to deal with Parish Finance Council matters between meetings.

### **2. Use of Agendas and Review Materials**

Meeting agendas should be prepared in advance of the meeting by consultation between the Pastor and Parish Finance Council Chair. The agenda should list the major items for discussion. Supplying information in advance to members will lead to more productive meetings.

### **3. Recording of Meeting Minutes**

Minutes should be recorded by the Parish Finance Council Secretary and archived as part of the parish permanent record.

### **4. Confidentiality**

Members should maintain confidentiality on those matters designated as confidential. Materials such as agendas, meeting minutes, and review materials should not be disclosed to others if designated as confidential.

Parish Finance Council meetings are typically not open to the parish community. Reports to the community will be shared once decisions are finalized. Communication with the parish should also occur at the onset of studying an issue to solicit needs and concerns, gifts and resources of the parish community. The primary purpose of the Parish Finance Council is to provide open and honest advice to the pastor, if the meetings occurred in a public forum, the discussion may be too limited. The Finance Council should advise the pastor on the best ways to keep the parish informed and involved in key issues and decisions facing the parish.

### **5. Record Retention**

The parish should retain meeting minutes, agendas, handouts, reports, and materials reviewed during the meeting for future reference by either internal or external parties.

## **SUBCOMMITTEES**

Some parishes may prefer to divide the Finance Council into subcommittees to deal with specific responsibilities and duties. The magnitude and complexity of the different subcommittees depends upon the size, resources, obligations, and needs of each particular parish. The Finance Council coordinates the work of these subcommittees, often by following priorities established by the Parish Pastoral Council.

The work of the subcommittees may encompass the following:

### **1. Budget Subcommittee**

- a. To assist the pastor and parish staff in the preparation, presentation, and review of an annual budget for both operating and capital expenditures based upon the goals and objectives determined by the Parish Pastoral Council. If a Budget Subcommittee is utilized, the final proposed budget should be presented to the entire council for review, before submission to the diocese or publication to parishioners.
- b. To assist other programs and ministries in preparing and submitting their annual budgets to the parish.
- c. To study parish revenue and make recommendations to the Parish Pastoral Council for maintaining and increasing revenues in order to meet parish objectives and priorities.
- d. To periodically (e.g. monthly or quarterly) review income and expenditures and make recommendations as necessary to see that expenses are within set limits. Monitor parish contribution trends.
- e. To provide parishioners with periodic (e.g. semi-annual or annual), comprehensive written reports on the parish's financial position, including a statement of activity and balance sheet accounts. Consider oral reports to parishioners to elaborate on key results and issues.
- f. To work with the elementary school and the religious education program regarding the budget, review internal controls of the business office, and prepare recommendations regarding subsidy. The same applies if supporting a regional school or consolidated school and may involve communication with other Parish Finance Councils or with a School Finance Council.
- g. To review periodic financial audits of the parish performed by an independent auditor and provide advice on how to address and correct identified weaknesses.
- h. Assist in communicating results of audits to parishioners.
- i. Conduct self-administered audits of internal controls and procedures. Particularly focus on areas involving cash receipts and any disbursements. Review procedures used for gathering, counting and recording Sunday collections and tuition and

control of bank accounts. Confirm duties are adequately segregated. Share findings with appropriate diocesan personnel.

- j. To ensure the consistent use of tamper-evident bank deposit bags along with a robust collection and counting procedure for offertory and any significant event or activity handling cash.
- k. To ensure that bank reconciliations are regularly completed very soon after each bank statement is received and that the reconciliations are checked by someone other than the person performing the reconciliation.
- l. To educate parishioners about stewardship and the need for parish involvement and support. If a parish has a separate stewardship committee this responsibility would fall to that committee.
- m. To review cost-cutting measures when necessary.

## **2. Facilities and Maintenance Subcommittee**

- a. Advise the Pastor regarding the results of quarterly inspection of all parish facilities.
- b. Recommend repairs or replacements based on priorities established by these inspections.
- c. Develop a detailed inventory of all parish assets in accordance with Canon 1283 §2 and update the inventory on an annual basis.
- d. Assist in the development of guidelines concerning use of parish facilities.
- e. Assist in the development of parish energy conservation programs.
- f. Develop teams of parishioners who will donate time and talents for parish maintenance tasks, taking note of the extent to which such work is allowed to be performed by volunteers under the guidelines of the diocesan risk management and insurance programs.
- g. Review the parish's risk management and loss prevention reports in order to ensure corrective action is taken where necessary.
- h. Ensure that the safety and security of the parish campus is addressed and reviewed regularly.

## **3. Financial Planning and Development Subcommittee**

- a. To provide long-range planning for both the financial and physical needs of the parish.
- b. To work closely with the budget and maintenance subcommittees, the Parish Pastoral Council, and other parish organizations to adequately plan and identify for the long range financial and physical needs of the parish.

## **RELATIONSHIP TO PASTORAL COUNCIL**

Since the Parish Finance Council relates to the administrative responsibilities of the pastor, it should not be a part of the Parish Pastoral Council structure. However, an officer from the Parish Finance Council may serve as an ex-officio member of the Parish Pastoral Council. Communication between the two councils is essential to share information regarding the parish finances in order to implement the pastoral plans and priorities.



An appropriate means of communication should be developed between the Parish Finance Council and the Parish Pastoral Council to ensure that the Parish Finance Council does not enter into areas of policy and mission, which are the prerogative of the Parish Pastoral Council. The Parish Finance Council advises on the adequacy of resources to accomplish the mission and specific ministries of the parish.

The Parish Finance Council reviews a draft of the parish annual calendar prepared by the Parish Pastoral Council.

## **RELATIONSHIP TO OTHER PARISH GROUPS/COUNCILS**

Although there is no formal reporting process between the Parish Finance Council and other parish groups/councils, the Finance Council should interact with parish groups/councils to study, create, and revise plans for the effective management and use of parish resources.

## **A CHECKLIST OF MAJOR ACTIVITIES**

The Parish Finance Council should establish an annual plan of its activities. Such a checklist could include the following activities:

### **1. Parish Annual Report**

- a. Review completed report prior to submission to the diocesan bishop. The report should be complete within 90 days of the end of the fiscal year.
- b. Coordinate communication to parish community of the financial situation of the parish. Consider using printed material, oral presentations, and parish hall meetings. Report should be presented to the parish as soon as possible, but no later than 5-months after the end of the fiscal year.

### **2. Parish Budget Report**

- a. Project and plan resources to meet specified goals.
- b. All individual program budgets are reviewed: church, elementary school, religious education, and auxiliary groups.
- c. Share proposed budget with the Parish Pastoral Council and the general parish.
- d. Complete and submit to diocesan bishop as required.

### **3. Financial Review**

- a. Financial report and significant financial facts should be prepared for every meeting.
- b. Budget amounts are compared to the actual income and expenditures to monitor results in comparison to budget projections.
- c. Year over year trend reports for programs, revenues, and expenses are analyzed to plan corrective action.

- d. At least annually, a representative from the Finance Council should review the general ledger detail and reconciliation of cash and investment accounts.

#### 4. Accounting/Internal Control Systems/Best Practices

- a. Review accounting system to determine if it produces current and accurate financial records.
- b. Ensure that appropriate risk management practices are in place.
- c. Identify all parish bank accounts, not just known operating accounts. Confirm that these account balances are reflected in the financial statements. Determine if the number of accounts can be reduced to ease administration.
- d. Review current bank account signature cards and account reconcilements for all parish accounts on a regular basis.
- e. Review the separation of duties, to the extent possible, of personnel involved in the finances of the parish.
- f. Review any statements received for any parish account related to a credit or debit card, store account, purchase order, purchasing card or other similar instrument. Verify that purchases had the necessary approvals and were for a parish (not personal) purpose.

#### 5. Auxiliary Groups

- a. Review budget and upcoming activities for the next year.
- b. Review revenue and expenses along with bank account reconcilements.
- c. Meet with the groups to acknowledge their contribution of time, talent, and treasure. Reinforce financial accountability of all groups to the parish.

#### 6. Compliance Oversight

- a. Taxable Activities: review support documentation and tax filings for payroll taxes (including W-2's), bingo, pull-tabs, and concession sales.
- b. Licensing Activities: review support documentation and filings for bingo, pull-tabs, carnivals, raffles and other events that may be restricted by the local municipality.
- c. Payments for Services Provided to Parish: confirm that IRS Form 1099 reports are completed and filed for independent contractors.
- d. Deductions from parish employee pay: confirm that payroll deductions are submitted on a timely basis to the benefit providers.
- e. Confirm that all compensation to employees and contractors, including bonuses or gifts, is reflected appropriately on the respective Form W-2 (for employees) or Form 1099 (for independent contractors).

## *Appendix A*

### References – Canons 1281-1288

Canon 1281 §1 – With due regard for the prescriptions of their statutes, administrators invalidly posit acts which go beyond the limits and procedures of ordinary administration unless they first obtain written authority from the ordinary.

§2 – The acts which go beyond the limits and procedures of ordinary administration are to be defined in the statutes; if, however, the statutes do not mention such acts, it is within the competence of the diocesan bishop to determine such acts for persons subject to him after he has heard the finance council.

§3 – Unless and to the extent that it is to its own advantage, a juridic person is not held to answer for acts invalidly posited by its administrators. A juridic person, however, is responsible for acts illegitimately but validly posited by its administrators with due regard for the right to sue or to have recourse against administrators who have damaged it.

Canon 1282 – All clerics or lay persons who through a legitimate title take part in the administration of ecclesiastical goods are bound to fulfill their duties in the name of the Church and in accord with the norm of law.

Canon 1283 – Before administrators take office:

1. they must take an oath before the ordinary or his delegate that they will be efficient and faithful administrators;
2. they are to prepare, sign and subsequently renew an accurate and detailed inventory of immovable goods, movable goods, either precious or of significant cultural value, or other goods along with a description and appraisal of them;
3. one copy of this inventory is to be kept in the archives of the administration; the other, in the curial archives; any change whatever which the patrimony may undergo is to be noted on each copy.

Canon 1284 §1 – All administrators are bound to fulfill their office with the diligence of a good housekeeper.

§2 – For this reason they must:

1. take care that none of the goods entrusted to their care is in any way lost or damaged and take out insurance policies for this purpose, insofar as such is necessary;
2. take care that the ownership of ecclesiastical goods is safeguarded through civilly valid methods;
3. observe the prescriptions of both canon and civil law or those imposed by the founder, donor or legitimate authority; they must especially be on guard lest the Church be harmed through the non-observance of civil laws;

4. accurately collect the revenues and income of goods when they are legally due, safeguard them once collected and apply them according to the intention of the founder or according to legitimate norms;
5. pay the interest on a loan or mortgage when it is due and take care that the capital debt itself is repaid in due time;
6. with the consent of the ordinary invest the money which is left over after expenses and which can be profitably allocated for the goals of the juridic person;
7. keep well-ordered books of receipts and expenditures;
8. draw up a report on their administration at the end of each year;
9. duly arrange and keep in a suitable and safe archive the documents and deeds upon which are based the rights of the Church or the institution to its goods; deposit authentic copies of them in the archive of the curia when it can be done conveniently.

§3 – It is strongly recommended that administrators prepare annual budgets of receipts and expenditures; however, it is left to particular law to issue regulations concerning such budgets and to determine more precisely how they are to be presented.

Canon 1285 – Within the limits of ordinary administration only, it is permissible for administrators to make donations for purposes of piety or Christian charity from movable goods which do not pertain to the stable patrimony.

Canon 1286 – Administrators of goods:

1. are to observe meticulously the civil laws pertaining to labor and social policy according to Church principles in the employment of workers;
2. are to pay employees a just and decent wage so that they may provide appropriately for their needs and those of their family.

Canon 1287 §1 – Both clerical and lay administrators of any ecclesiastical goods whatsoever which have not been legitimately exempted from the governing power of the diocesan bishop are bound by their office to present the local ordinary with an annual report, which in turn he is to present to the finance council for its consideration; any contrary custom is reprobated.

§2 – Administrators are to render an account to the faithful concerning the goods offered by the faithful to the Church, according to norms to be determined by particular law.

Canon 1288 – Administrators are neither to initiate nor to contest a lawsuit on behalf of a public juridic person in civil court unless they obtain the written permission of their own ordinary.

Definition: A juridic person is an artificial person constituted by competent ecclesiastical authority for an apostolic purpose, with a capacity for continuous existence and with canonical rights and duties like those of a natural person. Like a civil-law corporation, it is a legal construct which can and must be conceived of apart from the natural persons who constitute it, administer it, or for whose benefit it exists. Of its nature, a juridic person is perpetual and, once established, it can outlast all natural persons or material goods which formed it.

## *Appendix B*

### **RESOURCES and REFERENCE INFORMATION**

Besides these brief guidelines, there are many other materials available on church finances, much of it can be found on the internet. Some of the links you might find helpful are listed below.

#### Archdiocese of Chicago

- The Archdiocese of Chicago Policies & Procedures, Book V, “The Temporal Goods of the Church.” Access at <https://www.archchicago.org/documents/70111/70567/Book+5.pdf/7355468d-6c31-4a8d-8694-2f1e37dd4ecb>
- The Archdiocese of Chicago Policies & Procedures, Book II, “The People of God.” Access at <https://www.archchicago.org/documents/70111/70567/Book+2.pdf/cce478a4-c393-4cdb-90cc-e2e978d6299e>
- “Best Practices,” issued annually by the Department of Financial Services. Access at [www.archchicago.org/departments/financial\\_services/](http://www.archchicago.org/departments/financial_services/)
- “Archdiocese of Chicago: Construction Guidelines, revised 2005.” Published by the Archdiocesan Office of Facilities and Construction. Access at [www.archchicago.org](http://www.archchicago.org). Select departments, facilities and construction, general information, and finally construction/mechanical guidelines.

#### Catholic Finance Corporation

- Various policies and guidelines on parish finances and parish capital projects can be found at [www.catholicfinance.org](http://www.catholicfinance.org) especially under the ‘Resources’ tab.

#### Archdiocese of St. Louis

- A Financial Management and Control Manual for Parishes may be found at [www.archstl.org/sharedaccounting](http://www.archstl.org/sharedaccounting). This manual provides tips on finance councils, budgeting, financial reporting, and contains an internal controls questionnaire.

Church Finance Handbook, Edited by Kevin E. McKenna, Lawrence A. DiNardo, Joseph W. Pokusa, Canon Law Society of America, 1999.

#### United States Conference of Catholic Bishops (USCCB):

- “Diocesan Financial Management,” access at [www.usccb.org/about/financial-reporting](http://www.usccb.org/about/financial-reporting)
- “Diocesan Internal Controls: A Framework,” access at [www.usccb.org/about/financial-reporting](http://www.usccb.org/about/financial-reporting). While written for dioceses, these documents give a helpful framework on issues like reporting, internal controls, conflicts of interest and other important topics.

#### National Leadership Roundtable

<http://www.theleadershiproundtable.org/TLR/new-events/news/CCUSA07092012.htm>

## Sample D: Internal Control Questionnaire

Parish \_\_\_\_\_ School \_\_\_\_\_

City, State \_\_\_\_\_ For the year ended \_\_\_\_\_

This questionnaire is to be completed by each parish and school annually. Each question must be answered, and “no” answers must be explained in the comment section next to the question. If you are in doubt as to the meaning of a question, please contact the Diocesan Finance Office for assistance. This completed questionnaire must be submitted to the Diocesan Finance Office within 120 days of the end of the fiscal year, with the required acknowledgment signatures affixed.

(X) appropriate box Yes No Comment

### GENERAL

Does the parish have a Finance Council, established and operating in accordance with Canon Law, and the policies issued by the diocese? \_\_\_\_\_

Do you have a copy of the current Diocesan Financial Policies and Procedures? \_\_\_\_\_

Have the Pastor, Business Manager and at least one Finance Council member read the Diocesan Financial Policies and Procedures? \_\_\_\_\_

Is the parish in compliance with every policy as included in the current Diocesan Financial Policies and Procedures? \_\_\_\_\_

Is access to the general ledger and supporting subsidiary ledgers restricted to authorized personnel? \_\_\_\_\_

Are subsidiary ledgers maintained and reconciled to the general ledger on a monthly basis? \_\_\_\_\_

### FINANCIAL REPORTING

Has the budget been submitted at the beginning of the fiscal year in accordance with diocesan policy? \_\_\_\_\_

Have interim financial reports been submitted in accordance with diocesan policy during the fiscal year? \_\_\_\_\_

Have year-end financial reports been submitted \_\_\_\_\_

in accordance with diocesan policy? \_\_\_\_\_

Has the parish/school given the parishioners a complete financial report for the year? \_\_\_\_\_

Does the Finance Council review budget vs. actual variances on a regular basis and make budget adjustments as necessary? \_\_\_\_\_

Does the Finance Council review and approve interim and year-end financial statements on a timely basis? \_\_\_\_\_

Have all auxiliary groups been informed of diocesan and parish financial policies, and are they in compliance with them? \_\_\_\_\_

ACCOUNTING SYSTEMS

Do you have written procedures for the following accounting systems:

Cash receipts; cash disbursements; Personnel; Management; Payroll; Purchasing; Mass Stipends and Stole Fees? \_\_\_\_\_

BANK ACCOUNTS

Are bank accounts established, maintained and reported in accordance with diocesan financial policies? \_\_\_\_\_

Is the pastor an authorized signer on all bank accounts, including all auxiliary activity bank accounts? \_\_\_\_\_

Are all auxiliary activity bank statements received directly at the parish and reviewed by parish personnel? \_\_\_\_\_

Are all authorized signers on bank accounts in accordance with diocesan policy? \_\_\_\_\_

Are unopened, monthly bank statements delivered directly to the pastor, or his designee (Parochial Vicar or someone who is recording receipts and disbursements in the general ledger, and without access to check stock)? Is the statement opened and its contents reviewed by this person? \_\_\_\_\_

If bank statements are obtained online, are they downloaded by someone who is independent of recording cash receipts and disbursements and without access to check stock? \_\_\_\_\_

Are monthly bank reconciliations performed for all bank accounts, by someone who is independent of recording cash transactions, and are all reconciling differences resolved on a timely basis? \_\_\_\_\_

Are bank reconciliations reviewed by someone other than the preparer on a periodic basis? \_\_\_\_\_

On a test basis, are endorsements on cleared disbursement checks compared to the payee on the front of the check? \_\_\_\_\_

Are disbursement checks indicated as outstanding for more than 60 days investigated and resolved? \_\_\_\_\_

Does the Finance Council approve the opening and closing of all bank accounts? \_\_\_\_\_

Does someone other than the Bookkeeper review the monthly activity in the savings accounts with the diocese, and compare such activity to the activity posted in the general ledger? \_\_\_\_\_

Are funds received for Mass stipends recorded separately from other funds and a record kept of all Masses said in accordance with Canonical and diocesan requirements? \_\_\_\_\_

Are funds in excess of a 60-day operating requirement transferred to the diocesan Savings & Loan Program for investment? \_\_\_\_\_

CASH RECEIPTS

Are responsibilities for collection and deposit preparation functions segregated from those for recording cash receipts and general ledger entries? \_\_\_\_\_

Is the parish/school in compliance with diocesan policies with respect to cash receipts? \_\_\_\_\_



Has the parish established offertory count procedures in accordance with diocesan guidelines and are these procedures being followed?

\_\_\_\_\_

Does the parish/school consistently utilize tamper-evident deposit bags for the offertory and significant fundraising events?

\_\_\_\_\_

Is an envelope process for offertory in place and are periodic statements sent to parishioners giving them a record of their contributions to the parish?

\_\_\_\_\_

If a parishioner disputes their offertory statement, is the dispute resolved by someone other than personnel who handle and record cash receipts?

\_\_\_\_\_

Are all cash receipts deposited and recorded in the general ledger in the proper account on a timely basis (preferably daily)?

\_\_\_\_\_

Is all cash received deposited intact and no funds removed from the deposit?

\_\_\_\_\_

Is a subsidiary record of all accounts receivable kept, outstanding amounts followed up on and is the record reconciled to the general ledger on a monthly basis?

\_\_\_\_\_

Is a restrictive endorsement placed upon each incoming check when it is received?

\_\_\_\_\_

Are records of cash received, including offertory, compared to bank validated deposit slips on a daily basis?

\_\_\_\_\_

Are "NSF" checks followed-up immediately, resolved and adjusted as necessary?

\_\_\_\_\_

Are restricted donations recorded as restricted, and used only for the restricted purpose imposed by the donor?  
Is a record kept of the use of the restricted funds?

\_\_\_\_\_

Are endowed funds received recorded as endowment, and is only the investment income expended for ministry use?

\_\_\_\_\_

Are all bequests and trusts where the parish/school is a beneficiary handled in accordance with Canonical and diocesan requirements for the acceptance and receipt of such gifts?

\_\_\_\_

CASH DISBURSEMENTS

Is the parish/school in compliance with diocesan policies with respect to cash disbursements?

\_\_\_\_

Do procedures exist to ensure that disbursements are made only for budgeted matters, or have specific Finance Council approval and to ensure that all disbursements are approved?

\_\_\_\_

Is cash disbursed only upon receipt of properly approved original vendor invoices or properly approved check requests?

\_\_\_\_

Do check signers review support documents before signing checks?

\_\_\_\_

Do procedures exist to ensure that all disbursements are properly classified in the general ledger?

\_\_\_\_

Are unissued, blank checks under tight control and accounted for?

\_\_\_\_

Is the drawing of checks to cash or bearer prohibited?

\_\_\_\_

Is the use of facsimile signature stamps prohibited?

\_\_\_\_

Are credit cards issued and used only in accordance with diocesan policy?

\_\_\_\_

Is the use of debit cards prohibited?

\_\_\_\_

Are all expenses paid when due, and are all vendor discounts taken?

\_\_\_\_

If a discretionary account exists, is the Parish Finance Council aware of its purpose, and is the activity reported within the parish financial reports?

\_\_\_\_

Are “voided” checks destroyed by someone independent of the cash disbursement recording function, and is the voided check recorded as voided immediately?

\_\_\_\_\_

Have funds collected for National and Special Collections been remitted to the diocese within 30 days of the collections?

\_\_\_\_\_

PERSONNEL AND PAYROLL

Is the parish/school in compliance with diocesan policy with respect to personnel management and payroll issues, including USCCB and diocesan policy with respect to Safe Environment Protection?

\_\_\_\_\_

Are complete personnel files maintained for all employees?

\_\_\_\_\_

Are all employees properly classified as “exempt” or “nonexempt”?

\_\_\_\_\_

Are all payments to individuals, other than to Religious, and other than for properly accounted for employee expense reimbursements, reported on IRS Form W-2?

\_\_\_\_\_

Are the required tax withholdings made from individuals paychecks and remitted to the taxing authority in accordance with their rules and regulations?

\_\_\_\_\_

Are all payments made to and for Religious who are subject to policy and IRS regulations?

\_\_\_\_\_

Is IRS Form 1099 issued to independent contractors in accordance with IRS regulations?

\_\_\_\_\_

Are all payroll tax returns filed, and payroll taxes remitted in accordance with IRS, State and Local regulations on a timely basis?

\_\_\_\_\_

Are all diocesan clergy recognized and reported as employees for Federal Income Tax purposes but as Self-Employed individuals for Social Security purposes?

\_\_\_\_\_

Are clergy Mass stipends and stole fees reported to the IRS as income in accordance with diocesan policy?

\_\_\_\_\_

Are the eligibility requirements for all diocesan employee benefit plans carefully observed with respect to each employee so that no one will be improperly included or excluded?

\_\_\_\_\_

Are withholdings from checks to employees for contributory participations in diocesan employee benefit plans remitted to the plans on a timely basis?

\_\_\_\_\_

## Acknowledgment

We, the undersigned, acknowledge the following concerning this questionnaire:

1. We are familiar with these internal controls as recommended by the diocese.
2. Where we have answered “no” to a control question, we have explained above why it was not practical or appropriate to follow the internal control, and that we have implemented an alternative control procedure which conforms as closely as possible to the spirit of the control procedure as established by the diocese.
3. We have met to review and discuss all of the above internal controls and represent that they are functioning as required except as indicated otherwise.
4. We are not aware of any parish or school checking, savings or other accounts that have been omitted from the accounting records and our financial reports.

### SIGNATURES:

---

Pastor

---

Principal

---

Business/Office Manager

---

Bookkeeper

## **Sample E: Parish Accounting Policies & Financial Reporting Standards**

### **Objectives**

The primary objectives of parish accounting and financial reporting are as follows:

- To accurately and completely record, summarize and report the financial activity of the parish on a timely basis;
- To summarize financial transactions in standard financial reports that accurately reflect the financial condition of the parish and which are issued on a timely basis following each month-end;
- To provide a “benchmark” in conjunction with the financial statements in the form of a budget so that readers of the statements have a basis of comparison to assess financial performance.

### **Accounting Policies**

Financial activity is to be recorded primarily using the accrual basis of accounting, according to the following guidelines:

#### Receipts/Revenue

Revenue is to be recorded when earned. Generally, that is when funds are received. However, there can be instances where this is not the case, including:

- Advance payments: receipts representing deposits for future services to be rendered by the parish, such as the purchase of columbarium niches and cemetery plots, and tuition payments received prior to the period in which the educational activities will take place, are to be recorded as a liability (unearned income) and reclassified to income when the revenue is earned.
- Custodial receipts: receipts over which the parish has no discretion as to their use represent custodial transactions and are to be recorded as a liability (custodial obligations) until paid. This includes receipts from national and diocesan collections.
- Pledges: GAAP (Generally Accepted Accounting Principles) specify that an unconditional promise to give should be recorded as revenue upon receipt of the pledge if it is deemed collectible. However, for consistency of reporting across the diocese, it has been determined that parishes should only recognize revenue on pledges when they are collected.

#### Expenses/Liabilities

- Expenses are to be recorded when incurred (upon receipt of merchandise/service and the supporting invoice) and recorded as a liability (accounts payable). When teacher salaries are paid over the course of the school year and following summer, deferred salaries, taxes and benefits are to be expensed and recorded as a liability (accrued salaries, taxes and

benefits) over the course of the school year. Upon payment of the deferred salaries, taxes and benefits, the accrual is to be charged (eliminated).

- Expenses Paid in Advance: expenditures representing deposits for merchandise on order and services under contract are to be recorded as a prepaid asset. Upon receipt of the merchandise and completion of services, the appropriate expense account is to be debited and the prepaid asset account credited.

### Reimbursable Expenditures

- Payments that will be reimbursed are to be recorded to accounts receivable until reimbursement is received. This includes sales taxes paid to a vendor that are eligible for refund from the state Department of Revenue.

### Capital Assets

- Property and equipment is recorded at cost when purchased and at estimated fair value when received via donation. Expenditures for fixed assets with a cost >\$2,500 and a useful life of more than one year are to be capitalized and reported as an asset on the balance sheet. Donations of fixed assets with a fair market value >\$2,500 and a useful life of more than one year are to be recorded by debiting the fixed asset account and crediting the in-kind donations account. To determine whether an expenditure is a capital item or should be recorded as a repair, consider whether the expenditure extends the asset's life. For example, replacing the entire roof on a building extends the life of the building and, therefore, represents a capital asset, while replacing a portion of the shingles damaged by a storm is a repair. Similarly, repaving a parking lot extends the life of the lot and, therefore, represents a capital asset, while filling pot holes in the lot is a repair.

### Debt

- The principal amount of all loans payable is to be recorded as a liability (notes payable) and reported on the balance sheet. The principal portion of payments is to be recorded to the notes payable account and the interest portion is to be recorded to the interest expense account.

### Net Assets

- Net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets consist of:
  - Without Donor Restrictions
  - With Donor Restrictions

## Financial Reporting

Reporting to the parish – a financial report is to be made to the parish council at least annually. In addition, a year-end financial report is to be presented to the entire parish community. At a minimum, this report should consist of a summary level Statement of Activities and a summary level Statement of Financial Position, and consideration should be given to presenting a summary level Statement of Cash Flows. The report should normally be made available to parishioners within three (3) months after the end of the fiscal year. In addition, the annual budget is to be presented to the entire parish community within 60 days after the beginning of the fiscal year.

The following standard reports are to be issued to the pastor, Finance Council and appropriate managers at the close of each month:

1. Statement of Activities by Cost Center – this report summarizes income statement activity by cost center, listing the totals for all cost centers. The standard column headings are:
  - Current Month Actual
  - Year-to-Date Actual (from July of the current fiscal year thru the current accounting month)
  - Annual Budget
  - Annual Budget Remaining (variance of the annual budget from the YTD actual. Positive numbers are favorable variances, while numbers in brackets are unfavorable)
  - Year-to-Date as a % of Annual Budget
  
2. Statement of Activities by Account (all Cost Centers Combined) – this report summarizes income statement activity by natural account classification (e.g. all office supplies in one line, regardless of the cost center). The standard column headings are:
  - Current Month Actual
  - Year-to-Date Actual (from July of the current fiscal year thru the current accounting month)
  - Annual Budget
  - Annual Budget Remaining (variance of the annual budget from the YTD actual. Positive numbers are favorable variances, while numbers in brackets are unfavorable)
  - Year-to-Date as a % of Annual Budget
  
3. Statement of Financial Position – this is a balance sheet listing all active main accounts. The standard column headings are:
  - Current Period Balance (this is the balance as of the last day of the current accounting month)
  - Prior Year Balance (this is the balance from the previous year, as of the same month as the current accounting month)



4. Restricted Accounts – this is a roll-forward of restricted and endowment gifts showing the balances at the beginning of the year, monthly debits and credits, year-to-date debits and credits, and the ending year-to-date balances. The standard column headings are:
  - Beginning Balance (balance at the beginning of the fiscal year)
  - Month Credits (additions in the current accounting month)
  - Month Debits (reductions in the current accounting month)
  - YTD Credits (additions from beginning of the fiscal year through the current accounting month)
  - YTD Debits (reductions from beginning of the fiscal year through the current accounting month)
  - Ending balance (balance as of the last day of the current accounting month)

## **Budgeting**

Prior to the beginning of the fiscal year a financial budget for the upcoming fiscal year is to be prepared. The finance council should participate in developing the annual budget, based on goals set by the pastor with input from parish commissions and department heads. The finance council should recommend the final budget for approval by the parish council and pastor. They should also participate in the communication of the annual budget to the parish community.

The budget is the plan of revenues and expenditures for the upcoming year. It is to be prepared in accordance with the chart of accounts. A line-item amount is to be budgeted for each revenue and expenditure account. During the fiscal year, the pastor and finance council should review actual revenues and expenditures against budgeted amounts on a regular basis. Any material variance should be investigated and resolved as soon as possible; unfavorable actual-to-budget variances should be addressed by implementing offsetting measures.

## **Sample Parish Cash and Banking Guidelines**

### Offertory Collection Procedures

After the offertory collection, baskets from the collection are to be combined by at least two ushers. The funds may be brought to the front of the church for the remainder of the service, or they may be secured for counting immediately. Funds collected should remain intact until deposited at the bank; cash/check/envelopes should never be removed from the collection for any purpose. If the funds are placed at the front of the church for the remainder of the service, they should be removed from the altar by two ushers immediately following the end of the Mass or service. If the collection is not counted during/immediately after Mass, provision should be made by the office staff to issue tamper evident bags for each Mass. The office staff is to maintain a master log of all tamper evident bags. Upon issuing the bags for the weekend Masses, the bag numbers issues should be recorded on the master log. The master log should be attached to the bags being issued. The log and the bags for the upcoming weekend should be stored in a secure area, to which the ushers have access. A copy of the log should be made after the weekend issue is recorded. The copy should be retained in the parish office, in the event the original is misplaced or mishandled. Immediately following the collection or immediately following Mass (if the funds are brought to the altar during

the offertory procession), two ushers should place the funds into a tamper evident bag. The seal tag should be removed from the bag, attached to log and recorded as used on the log. The log should be signed and dated by all the ushers handling the funds (at least two). The sealed used bags are to be transported by two ushers and deposited in the parish safe, preferably a drop safe. At the conclusion of the last service for the weekend, the log should be attached to the bag and dropped into the safe. No funds are to be left unsecured in the church. The funds should subsequently be retrieved from the safe by at least two unrelated persons and counted and recorded by at least two designated, unrelated persons. Parish staff and clergy should not be part of the count team.

### Bank Account Signatories

The Pastor/Administrator or person with the duly authorized Power of Attorney is required to be the authorized signor on all parish and related entity bank accounts. Signing authority can be given to the Parochial Vicar to assist when the Pastor is temporarily unavailable. In no instance should a signature stamp or pre-signed check be used.

### Bank Account Reporting

All bank accounts that use the parish tax ID should be included on the general ledger of the parish. This is the case even when the parish provides no funds to the organization (e.g. a fundraising group or program). Groups, organizations and clubs that utilize the parish federal identification number should account for all cash receipts and disbursements on the parish general ledger.

### Auxiliary Organization Using the Parish Tax ID

Auxiliary organizations are accountable to the Pastor and therefore monthly activity must be reported to the business manager and the Pastor. The Pastor should be the signatory and the receiver of the monthly bank statements for any accounts held by these organizations. Certain national organizations, such as the St. Vincent de Paul Society, have their own tax ID number, so these requirements would not apply to them.

## Sample F: Sample Decree on Parish Finance Councils

Dear Brothers and Sisters in Christ:

Flowing from our rebirth in Christ through the waters of baptism, we are all called to contribute and to build up the Body of Christ (cf. c. 208), to promote the growth of the Church (cf. c. 210) through apostolic action (cf. c. 216) and to bring the message of salvation to "all people of all times and all places." (cf. c. 211) We do this by lives lived in conformity with the Gospel message and by the generous sharing of our time, talent and treasure as good stewards of God's manifold gifts.

Since our financial treasure plays such an important role in providing the Church with those material resources for divine worship, for catechesis and sacramental preparation, for ministry to youth, the elderly, the poor and countless other apostolic and charitable works (cf. c. 222), it is essential that the Christian faithful share their knowledge and competence in financial and administrative matters with their pastors for the good of the Church. (cf. c. 212 §3).

Therefore, in compliance with Canon 537 of the Code of Canon Law, which states that "in each parish there is to be a finance committee to help the parish priest in the administration of the goods of the parish" and in virtue of my legislative authority in accord with Canon 391 §2 of the same Code of Canon Law, I hereby decree the following norms as particular law for the Diocese of \_\_\_\_\_:

1. Each parish, mission and inter-parochial school of the Diocese of \_\_\_\_\_ is to have its own finance council. Parishes and missions are subject to the norm of Canon 537 of the Code of Canon Law; inter-parochial schools are subject to the norm of Canon 1280 of the same Code. The bylaws of these entities are to be submitted to the vicar general for his "visum est" by January 1, 2011. The finance council is to provide the pastor (administrator) with sage wisdom and necessary assistance in the administration of the goods of the parish (mission, school) in accord with Canons 1281-1288, while keeping in mind that the pastor is the representative of the parish in such matters (cf. 532).
2. The finance council is a consultative body over which the pastor presides either directly or through a delegate, named as chairperson. The finance council bylaws should determine the chairperson's duties in accord with diocesan policy published in Financial Guidelines and Policies – Parishes, Schools and Early Childhood Centers, Appendix II.
3. Excluding the pastor, each finance council must be composed of:
  - a. At least 3 members for parishes with fewer than 500 families
  - b. At least 5 members for parishes between 501 and 1,500 families
  - c. At least 7 members for parishes over 1,500 families
  - d. For inter-parochial schools, a minimum of two consultants to assist the administrator in the administration of the material goods of the school [cf. c. 1280].
4. Members of the finance council must possess outstanding integrity and be committed to the furtherance of the Church's mission, be qualified in finances, and/or business, and not employees of the parish or school.

- a. Members of a parish finance council must be registered members of the parish.
  - b. Members of a school finance council may be parents of a child attending the school or an alumnus(a) or another qualified adult appointed at the discretion of the school pastor.
5. Terms of office, as determined in the finance council bylaws, should not be less than two years nor more than four years. A member may be reappointed but must not serve more than 8 continuous years. Members' terms must be staggered so as to provide continuity.
6. Each parish finance council must meet at least 4 times a year. Finance council bylaws may require more frequent meetings. Parishes designated as Financially Challenged must meet monthly until the Financially Challenged designation is lifted.
7. The parish finance council must be consulted in the preparation of the annual budget of the parish and, if applicable, the parish school. In parishes and/or schools designated as Financially Challenged, the finance council must approve the budget before being accepted by the diocesan finance office for its review.
8. In addition to the annual budget, the parish finance council is to provide advice and assistance to the pastor concerning the following matters:
  - a. Quarterly and annual financial reports to the bishop;
  - b. Financial accountings to parishioners at least once per fiscal year;
  - c. Short- and long-term financial planning;
  - d. Educating the faithful of the parish in the area of financial stewardship, in order to increase financial support of the parish;
  - e. The incurring and repayment of debt;
  - f. The resolution of unpaid debts and budget deficits;
  - g. Personnel administration, especially staffing needs, salary scales, tax compliance and reporting, personnel policies;
  - h. Federal, state and local regulatory matters;
  - i. Acquisitions and sales of land;
  - j. Expenditures or projects in excess of \$25,000;
  - k. Leases or other contractual arrangements that last more than one year.

The pastor of a parish or mission must consult the parish finance council before submitting:

- l. The annual governance certification letter; and
- m. The internal control questionnaire to the diocesan bishop

The signatures of the finance council members on these documents are indicative of consultation, not approbation.

9. Before petitioning the bishop in writing for his approval for an act of extraordinary administration, namely a single act, or an aggregate of acts so intimately connected that they are essentially one, which incurs an expense or indebtedness in excess of \$40,000, a

pastor must consult the parish finance council. Their signatures on the petition to perform an act of extraordinary administration are indicative of consultation, not approbation.

However, before accepting a petition to perform an act of extraordinary administration which is in excess of 20% of a parish's annual offertory, the bishop, exercising his pastoral office (cf. c. 381) and ever mindful of the intentions of the donor(s) (cf. c. 1300), may require a pastor, not only to consult the finance council, but the parish pastoral council as well, even obtaining the latter's consent by majority vote (cf. c. 127) before beginning his review of the petition for approval.

10. A printed record of each finance council meeting must be kept. In order to keep members of the parish informed, it is recommended that a summary of each parish finance council meeting be published either in the parish bulletin or on the parish website.
11. For a just cause, a pastor, with the written consent of his finance council, may petition the vicar general of the diocese in writing to be dispensed from a particular norm of this decree for a period of time. Such dispensation from the vicar general must be in writing and witnessed by the chancellor or vice-chancellor.

These norms, herein decreed as particular law for the Diocese of \_\_\_\_\_ shall be binding for all parishes and missions in the Diocese of \_\_\_\_\_, and all diocesan inter-parochial schools, effective \_\_\_\_\_. By this decree, all policies contained in Financial Guidelines and Policy Manual for Parishes, Schools and Early Childhood Centers for the Diocese of \_\_\_\_\_, which are not contrary to the norms prescribed above, are raised to the status of particular law for all Christ's faithful and institutions in and out of the Diocese of \_\_\_\_\_.

Given at \_\_\_\_\_, \_\_\_\_\_ on this \_\_\_\_\_ day of \_\_\_\_\_ in the year of our Lord 20\_\_\_\_\_.

\_\_\_\_\_  
Bishop \_\_\_\_\_

Diocese of \_\_\_\_\_

\_\_\_\_\_  
Chancellor / Notary

## VI. Compensation of Priests and the Dual Tax Status of Priests

The IRS expects that ministers, including priests, are ordinarily classified as employees for income tax purposes but self-employed for Social Security and Medicare tax purposes. A reference that is helpful with tax treatment of clergy specific issues is Scott A. Hoselton's *Income Tax for Priests Only*, published by Shepherds Advisor. No denomination has been successful in defending the self-employment status position for clergy, although certain individual clergy have successfully maintained self-employment status.

From the middle to late 1990s, when the IRS audited priests who filed their tax returns as self-employed for income tax purposes, it typically reclassified them from self-employed status to employee status.

In determining the employee or independent contractor status of taxpayers, the IRS now uses the three-category approach (behavioral contract, financial control and the relationship of the parties) to determine the amount of control exercised over the priest's duties (see Chapter IX: Compensation of Lay Employees and Diocesan Deacons of the Church for a more detailed discussion of the three categories and IRS Publication 15-A: Employer's Supplemental Tax Guide). An IRS analysis of the three categories as they pertain to priests would most likely result in a determination that the priest is an employee, as did the twenty-factor analysis under Rev. Rul. 87-41.

Priests who file their tax returns based on Form W-2 file as *employees*. This means that they report their unreimbursed business expenses on Form 2106, *Unreimbursed Employee Business Expenses*, (or the simpler Form 2106-EZ) and then transfer those expenses to Schedule A, *Itemized Deductions*. Common expenses include meals, entertainment, transportation and travel. It should be noted that the deductible portion of both meals and entertainment is 50% of the total. Generally speaking for priests, the standard deduction is greater than allowable itemized deductions, in which case there would be no tax benefit to filing either Form 2106 or Schedule A. The standard deduction amount is adjusted for inflation each year and implicitly encompasses tax deductions not common to priests (e.g. real estate taxes and mortgage interest).

If the diocese adopts an accountable business expense reimbursement plan, the reimbursements paid to the priest are not taxable. To be an accountable plan, the expenses must be related to the priest's responsibilities, the priest must adequately account for the expenses and all excess reimbursements must be returned (IRS Publication 463). If the diocese adopts a non-accountable reimbursement plan, the reimbursement is added to wages as taxable income reported on Form W-2 and the priest may claim the expenses on Form 2106 as explained above.

In very limited cases, a few priests may be permitted to file their tax returns based on Form 1099-MISC filed as bona fide *independent contractors*. This means that they report all income and related expenses on Schedule C. Under this tax status, priests receive full, dollar-for-dollar deduction offset against their income for ministry-related expenses.

## **Other Clergy Tax Considerations**

### **Tax-free Housing**

Housing provided to priests may qualify as an income tax-free benefit. However, it is subject to self-employment tax and, as such, is to be reported on Form 1040, Schedule SE. Determining the value of housing provided can vary depending on the location of the housing, whether or not it is in a parish rectory, the level of privacy, etc. The IRS suggests that the value of the housing be determined by reference to comparable data. For a discussion of housing allowances for both active and retired priests, please see Chapter VII: Compensation of Diocesan Priests: Pension and Other Post-Retirement Benefits.

### **Tax-free Board**

Meals provided to priests are an income tax-free benefit, under the following conditions:

1. The meals are consumed on the parish premises.
2. The meals are provided for convenience of the parish (i.e. the priest is “on call”).
3. The meals are required as part of the priest’s working conditions.

Meals that do not meet all of the above requirements do not qualify as a tax-free benefit. If the priest is provided with a food allowance or reimbursement for food purchases or restaurant meals, it may represent taxable income to the priest unless it qualifies as a business (church) expense under an accountable reimbursement plan.

The value of meals provided to priests is subject to self-employment tax and, as such are to be included on Form 1040, Schedule SE.

### **Stipends, Mass Fees, Allowances**

The IRS considers Mass Stipends, Fees, Stole Fees and Honoraria as payments for services rendered and, thus, represent earnings subject to both federal income tax and Social Security/Self-Employment tax. When such payments are issued by the employer, they should be included on the priest’s Form W-2.

Allowances paid to a priest (auto, clothing, etc.) represent earnings subject to federal income tax and Social Security/Self-Employment tax. Any amounts paid to cover a priest’s self-employment or income taxes are taxable income for both taxes. Allowances paid to a priest are to be included on the priest’s Form W-2.

Where the allowance is meant to be a reimbursement for parish-related business expenses and not taxable income, an accountable business expense reimbursement plan should be considered.

## **Professional Fees**

Professional income is earned when a priest is paid to perform services outside his normally assigned duties. Professional income is usually derived from a particular skill or discipline which the priest acquired through extended education.

Common examples include Canon Law specialists, psychologists, licensed counselors and the like. These priests typically have a regular salary from their parishes, but they are called upon from time to time for their expertise, and they are paid additional income for this work. If this income is related to their employer it is W-2 earnings. If it is paid by someone other than the employer, it is paid on an “outside contractor” basis and reported on a Form 1099. This income, net of any direct expenses incurred to derive the income, constitute earnings subject to Federal income tax and Social Security tax.

## **Income Tax Withholding**

Priests are exempt from all federal payroll withholding requirements. However, a priest may elect to have federal income tax withheld from his pay. He may elect to have sufficient amounts withheld only as federal income tax to cover both federal income taxes and Social Security/Self-Employment tax. As discussed above, the priest is considered self-employed for Social Security purposes; therefore, Social Security (FICA) and Medicare taxes should never be withheld from his pay. State and local withholding requirements for priests may vary by state and locality.

## **Clergy Exemption for 403(b) or 401(k) Contributions**

Contributions by priests to a Church sponsored 403(b) or 401(k) plan are excluded from net earnings for self-employment purposes. Therefore, when priests calculate their income subject to self-employment tax, they should exclude the amounts contributed to their 403(b) or 401(k) plan via payroll deduction.



## **VII. Compensation of Diocesan Priests: Pension and Other Post-Retirement Benefits**

### **Introduction**

Canon law stipulates that the diocesan bishop must provide suitable support and housing for all diocesan clergy upon their retirement from active service (CIC cc. 281 and 384). In the United States, the USCCB has promulgated a set of norms in light of this provision of canon law. In adhering to these norms, dioceses have developed various approaches to providing for the well-being of its retired priests. Many dioceses have adopted defined benefit plans to provide pension benefits for retired priests. In some cases, dioceses sponsor tax-sheltered annuity plans or other forms of defined contribution plans.

Most retired clergy are eligible for Medicare benefits. Currently, Parts A (hospital inpatient and limited long-term care), B (physician and outpatient) and D (pharmacy) programs are available. Persons need to pay close attention to enrollment requirements for these benefits, especially Part D, as timing affects the participant's cost. Dioceses may provide other post-retirement benefits, such as supplemental medical and dental benefits, long-term care, and housing allowances. As medical programs evolve and as federal healthcare requirements change, it is important to adjust payments accordingly.

The accounting treatment for pension and post-retirement benefit plans is specified in the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) topic sections 712, Non-retirement Post-Employment Benefits; section 715, Compensation – Retirement Benefits; and section 958-715, Not-for-Profit Entities Compensation – Retirement Benefits.

These pronouncements apply to all entities issuing financial statements in conformity with generally accepted accounting principles (GAAP), including the Catholic Church. These pronouncements apply to lay employee plans as well as diocesan clergy plans. Accounting guidance is periodically revised; diocesan staff should consult with professionals as changes are effective.

### **Accounting Treatment**

The regular, systematic practice of providing certain benefits to retired priests (such as monthly pension payments, payments of premiums for Medicare supplemental insurance policies, payment of medical and dental bills, housing subsidies, etc.) is evidence of a defined benefit pension plan or a post-retirement benefit plan, whether or not a written plan document exists. The benefits may be in the form of either a reimbursement to the retiree or direct payment to a provider. Under these circumstances, benefits are viewed as deferred compensation arrangements whereby the diocese agrees to pay future benefits in exchange for current services. Therefore, the expected cost of providing pension and other post-retirement benefits to priests is to be recognized over their years of active service in the diocese. The obligation of the diocese for pension and other post-retirement benefits is to be accrued in accordance with sound actuarial principles and the terms of the plan.

Benefits that are provided on a case-by-case basis, without any consistency or expectation thereof, represent discretionary payments and may be accounted to on a pay-as-you go (expensed when incurred) basis.

It is recommended that retired priests' benefits be formalized in a written plan document. This provides clarity to the priests and eliminates misunderstandings as to exactly what benefits they can expect. When developing or changing a plan document, legal counsel should be consulted. The plan document should include eligibility requirements, funding sources and benefits. The tax treatment for benefits should be well documented and followed consistently.

ASC 715, Compensation – Retirement Benefits applies to all not-for-profit organizations with single-employer, multiple-employer and multi-employer defined benefit pension, health or other postretirement plans. Organizations with single-employer and multiple-employer plans are required to: (1) report the funded status of its plans, measured as the difference between the fair value of the plan assets and the benefit obligation, directly on its balance sheet (recognition provisions), (2) align the measurement date for plan assets and benefit obligations with the organization's fiscal year-end (measurement date provisions) and (3) provide certain disclosures in the organization's financial statements. Organizations with multi-employer plans are not required to report the funded status of the plans on their balance sheet; however, there are required disclosures to be made in the organization's financial statements.

ASC 715, Compensation – Retirement Benefits is a complex topic, and the circumstances of each plan need to be considered in its full implementation. Since these circumstances can vary widely from plan to plan, it would be prudent for dioceses to seek professional advice with respect to their own particular situations.

Employers are required to provide significant disclosures about the assets in postretirement benefits plans (e.g. fair value of plan assets, concentrations and categories of plan assets, etc.), (ASC 715-20-50-5; 958-715-50-1). The content and presentation of these disclosures changes periodically and current guidance should be reviewed when financial statements and footnotes are prepared.

An analysis of payments made to, or on behalf of, retired priests should be conducted to determine whether – despite the absence of a written plan – there is a pattern of payments that represent a systematic practice of providing benefits that should be accounted for in accordance with relevant accounting pronouncements.

## **Plan Funding**

The method of funding these benefit plans is varied and often complex. Many dioceses rely on special assessments, special collections, fund-raising campaigns, or a combination of these and other methods. Some dioceses cover pension and other post-retirement benefits on a pay-as-you go basis, while other pre-fund these obligations. Best practices suggest that careful consideration must be given to establishing a Trust to account for and report the operating activities of these programs.

Consideration should be given to pre-funding pension and post-retirement benefit plans. Insufficient liquid assets may result in the diocese's inability to meet its obligation to retired priests. If funds are not segregated for these purposes, usually in a trust, the assets may be subject to creditor claims. Trusts should not be over funded; a funding policy should be developed, approved by competent authority and followed consistently.

Only assets that are segregated and legally restricted for pension and post-retirement benefits qualify as plan assets under the provisions of GAAP. Assets that are not segregated in a trust or otherwise effectively restricted so that they cannot be used by the diocese for other purposes do not qualify as plan assets.

Healthcare costs and life expectancies are continuing to increase each year. The issue of recognizing and funding these future obligations is more critical today than ever. When pension and post-retirement plans are pre-funded, assets should be appropriately invested to generate a return on investment while maintaining the corpus of the fund and providing sufficient.

### **Status of Priests' Retirement Plans**

Consultation with diocesan legal counsel or pension counsel is necessary to determine whether a diocesan retirement plan (for lay employees or priests) meets the requirements of the Internal Revenue Code (IRC) either as a qualified defined benefit or defined contribution plan or as a section 403(b) tax-deferred annuity, and whether the plan qualifies as a "church plan" under section 414(e) of the Code. Although qualified church plans are not subject to ERISA (Employee Retirement Income Security Act) vesting, participation and funding rules and are not required to file the annual Form 5500, such plans must nonetheless comply with numerous technical requirements, including certain pre-ERISA standards. Because pension legislation is amended frequently, periodic compliance reviews of all diocesan retirement plans are advisable.

### **Housing Allowance Designation**

IRC section 107 provides an exclusion from gross income for a parsonage (housing) allowance provided to clergy (active as well as retired). This includes the rental value of a home furnished to him as part of compensation or a housing allowance, to the extent that the payment is used to rent or provide a home. In order to qualify under IRC section 107, the trustees of the priests' retirement plan, or the bishop, must designate a portion of each payment as a housing allowance excludable under IRC section 107 prior to the beginning of each year.

The amount excludable from gross income as a housing allowance is limited to the least of the following three options:

- The amount actually used to provide a home (including rent, furnishings, repairs, insurance, taxes, utilities – but not food or entertainment)
- The amount officially designated as a housing allowance
- The fair rental value of the home, including furnishings, utilities, garage, etc.

The sum of all pension payments issued in a calendar year are to be reported as the gross distribution amount on form 1099-R. If the diocese has properly designated all, or a portion of the pension payments as a housing allowance, the taxable portion of the total payments cannot be determined by the diocese, since the amount excludable from income as a housing allowance has to be determined by the taxpayer based on the three options shown above. Therefore, the taxable amount on form 1099-R should be left blank and the box – taxable amount not determined checked.

The exclusion from income for federal income tax purposes applies to both active and retired clergy. The exclusion from income for Self-Employment tax purposes applies only to retired clergy.

### **Guidelines for the Retirement of Bishops**

In November 2010 the USCCB approved “Guidelines for the Provision of Sustenance to Bishops *“Emeriti.”* The following summarizes these guidelines:

1. Beginning January 1, 2011, the stipend recommended for all bishops in retirement will be a minimum of \$1,900.00 per month, to be adjusted annually according to the local cost of living index. If pension benefits granted to a Bishop *Emeritus* already provide the minimum amount recommended for the stipend, no additional funds need to be given. If, on the other hand, pension benefits do not meet the minimum recommended amount, additional funds should be supplied to reach the recommended minimum level. If pension benefits granted to retired priests of the diocese exceed the minimum recommended for the Bishop *Emeritus*, the greater amount should be considered appropriate for the Bishop *Emeritus*.
2. In addition to the monthly stipend, it is also recommended that in fraternal charity and solicitude each diocese also provide the following:
  - a. Appropriate housing and board – if he so desires, and unless the Holy See has provided otherwise, appropriate housing and board within the diocese where the Bishop *Emeritus* last served, including the use of a private chapel and housekeeping assistance. It is recommended by the Congregation for Bishops that the official residence provided by the diocese be reserved for the presiding Diocesan Bishop. The diocese is obligated to provide a Bishop *Emeritus* with appropriate housing and board even should he choose to reside outside of the diocese.
  - b. Health and welfare benefits, including major medical and the full cost of medical and hospital care. This includes any applicable coverage for home health care, assisted living facilities or long-term care facilities.
  - c. An office with secretarial assistance commensurate with need.
  - d. Suitable funeral and burial.

It is recommended that each diocese also provide the following benefits:

- a. Transportation including an insured automobile for his use.

- b. Travel expenses (i.e. transportation, lodging, food, etc.) to allow the Bishop *Emeritus* to attend:
  - i. Provincial meetings and workshops
  - ii. Regional meetings, workshops and retreats
  - iii. Meetings of the USCCB
  - iv. *Ad limina* visits to the Holy See
  - v. Ecumenical councils, Synods of Bishops, and meetings of the Roman Curia to which the Bishop *Emeritus* is associated
  - vi. Episcopal installations
3. The sustenance of a Bishop *Emeritus* who is a member of an institute of consecrated life or a society of apostolic life is to be provided by the diocese in which he last served, unless the institute or society wishes to provide such support.
4. If it seems advisable in order to seek some degree of uniformity, the dioceses of a given region or province, in a spirit of subsidiarity, should take upon themselves the responsibility to interpret and implement these guidelines, taking into account the local economy. Only in this way can the differing living costs in the various regions of the country be factored into the consideration of retirement benefits.

## VIII. Compensation of Religious

Members of religious orders who provide services to a diocesan employer (defined here to include the diocese and any affiliated entities listed in *The Official Catholic Directory* [OCD], (i.e. the Kennedy Directory) are subject to distinct tax and reporting rules, primarily as a result of their vow of poverty.

### Employment Classification

Status as a member of a religious order does not automatically determine employment classification. Rather, classification of a religious as an employee of a diocesan employer or as an independent contractor should be made by applying the common law tests as interpreted by the Internal Revenue Service (IRS) (See Chapter IX: Compensation of Lay Employees and Diocesan Deacons of the Church).

### Taxation of Compensation

No individual religious is “tax-exempt.” Tax exemption applies, if at all, to a religious order that qualifies as tax exempt under section 501(c)(3) of the Internal Revenue Code. Further, status as a member of a religious order does not automatically immunize from federal income and employment taxation the compensation paid to a religious who is performing services for a diocesan employer. Rather, the taxability of such compensation (including employee fringe benefits, if any) provided by the diocesan employer, is determined in accordance with the principles set forth in Revenue Ruling (Rev. Rul.) 77-290, 1977-2 C.B. 26.

### Rev. Rul. 77-290

Under Rev. Rul. 77-290, a member of a religious order providing services to a diocesan employer will be considered *for tax purposes* to be an agent of his or her order and will not be liable individually for federal income or employment taxes (FICA or Medicare) on compensation paid by the diocesan employer, *provided* three criteria are met: (1) the religious must be subject to a vow of poverty; (2) the religious must be providing services for a diocesan employer listed in the OCD at the direction of his or her ecclesiastical superiors; and (3) the religious must remit the full amount of compensation to his or her religious order, which must be exempt from federal income tax under section 501(c)(3) of the Code. *If any Rev. Rul. 77-290 criterion fails to be met, the religious is taxable individually on compensation received.*

Rev. Rul. 77-290 does not purport to determine the employment status of a religious providing service for a diocesan employer, and does not preclude classification of a religious as an employee of a diocesan employer or the provision of customary employee benefits to religious who are employees. Rev. Rul. 77-290 presumes that the religious are employees of the entities described therein, since neither FICA nor income tax withholding would be an issue in the absence of status as an employee.

## **Verifying Rev. Rul. 77-290 Requirements**

It is incumbent on the diocesan employer to determine whether a member of a religious order meets all three criteria of Rev. Rul. 77-290 before suspending its general withholding and reporting obligations under the Internal Revenue Code. The diocesan employer should verify that the individual is a member of a Section 501(c)(3) religious order subject to a vow of poverty recognized by the Church and that the individual's services have been authorized by his or her religious superior. These first two issues can be resolved in any reasonable manner, e.g. by correspondence with the member's religious superior.

Section 501(c)(3) status should be verified by reference to the current OCD. The diocesan employer should also verify that the full amount of compensation paid to the religious will be remitted to the religious order. This can be accomplished in one of several ways, listed below in order of preference: (1) by direct deposit to a bank account bearing the name and employer identification number ("EIN") of the religious order; (2) by check payable to the religious order; or (3) by check payable jointly to the religious order and the individual religious.

As a general rule, compensation paid directly to an individual religious will be treated as taxable to the individual religious. However, in limited circumstances, diocesan employers may be justified in treating such compensation as qualifying under Rev. Rul. 77-290. In these circumstances, the diocesan employer should determine that there exists a significant impediment to the payment of compensation to the religious order directly as outlined above. In addition, the diocesan employer should obtain appropriate written documentation from the superior of the religious order certifying that compensation paid directly to the individual religious will be remitted to the religious order in accordance with the requirements of Rev. Rul. 77-290. This supporting documentation should be updated annually.

**NOTE:** As religious increasingly come to the United States from congregations outside the country, special care must be taken to review and confirm payment for services to the criteria identified above. If the religious congregation is not exempt from taxes by inclusion in the OCD, any payment must usually be made under an ordinary and taxable employment relationship.

## **Reporting Compensation**

The manner of reporting compensation of religious performing services for diocesan employers depends on the taxability of that compensation. If the criteria of Rev. Rul. 77-290 are satisfied and compensation is not taxable to the individual religious, no reporting on Form W-2 or Form 1099 is required. Some diocesan employers may currently report compensation paid to nontaxable religious, generally in one of two ways: (1) issuance of a Form 1099 bearing the religious order or civil corporation's employer identification number (EIN); or (2) issuance of a Form W-2 bearing the Social Security number (SSN) of the religious employee. The first practice is problematic for the religious order and should not occur. The second practice is also problematic and may trigger IRS scrutiny. Although commercial payroll services may initially require issuance of a Form W-2 or Form 1099, with persistence and determination they can be persuaded to modify their computer programs to accommodate the special needs of diocesan employers with respect to Rev. Rul. 77-290.

If the criteria of Rev. Rul. 77-290 have not been satisfied, (e.g. if the diocesan employer has been unable to verify that the full amount of compensation will be remitted to the religious order) the compensation is taxable to the individual religious and should be reported in the ordinary course of employment. Thus, if the religious is taxable and is classified as an employee (see above) of the diocesan employer, compensation must be reported on Form W-2. If the religious is taxable and is classified as an independent contractor of the diocesan employer, compensation must be reported on Form 1099. No withholding is required with respect to independent contractors.

Reporting and tax withholding with respect to taxable religious will differ for religious priests and non-ordained religious. The compensation of a taxable religious priest who is performing ministerial services should be reported in the same manner as that of diocesan priest employees. Priests performing ministerial services are treated as self-employed for Social Security tax purposes even if they are classified as employees for income tax purposes. They are liable for SECA tax under Section 1402 of the Code. No FICA taxes should be withheld. The compensation of a taxable religious priest employee who is not performing ministerial services, or of a taxable non-ordained religious employee, should be reported in the same manner as that of diocesan lay employees, with income and FICA tax withheld.

### **When Medicare is Secondary Payer**

A member of a religious order whose members are required to take a vow of poverty is not considered to have current employment status with the religious order if the services he/she performs as a member of the order are considered employment by the order for Social Security purposes only. This applies where the religious order elected Social Security coverage for its members under section 3121(r) of the Internal Revenue Member of Religious Order Code. Thus, Medicare is primary payer to any group health coverage provided by the religious order.

This exception applies only to members of religious orders who have taken a vow of poverty. It does not apply to clergy or to any member of a religious order who has not taken a vow of poverty or to lay employees of the order. This exception applies not only to services performed for the order itself (such as administrative, housekeeping, and religious services), but also to services performed at the direction of the order for employers outside of the order provided that the outside employer does not provide the member of the religious order with its own group health plan coverage. A member of a religious order has current employment status with the outside employer as a result of providing services on behalf of the outside employer (an ongoing business relationship exists). If the outside employer provides group health plan coverage to the member of the religious order on the basis of that current employment status relationship, the usual Medicare Secondary Payer rules apply.

Medicare is the secondary payer to the group health plan of the outside employer if the outside employer has the requisite number of employees.



### **EXAMPLE 1**

Sister Mary Agnes is a member of a religious order where members are required to take a vow of poverty. Sister Mary Agnes was assigned to teach at a church school in the Diocese of the Metropolis. The diocese does not provide group health plan coverage to Sister Mary Agnes. The only group health coverage available to Sister Mary Agnes is provided by the religious order. Medicare is the primary payer for services provided to Sister Mary Agnes.

### **EXAMPLE 2**

Sister Mary Teresa is a member of a religious order whose members are required to take a vow of poverty. Sister Mary Teresa was assigned to teach at a church school in the Diocese of Smallville. On the basis of her teaching relationship with the Diocese of Smallville, the diocese provides group health plan coverage to Sister Mary Teresa. The group health plan provided by the Diocese of Smallville is the primary payer and Medicare is the secondary payer for services provided to Sister Mary Teresa.

Carriers should note that the exemption only applies to the working aged and disability provisions that base a group health plan's obligation to be a primary payer on a current employment status relationship. The exception does not apply to the End Stage Renal Disease (ESRD), Workers' Compensation or Liability and No-Fault provisions.

For further information, please refer to the Medicare Secondary Payer (MSP) Manual, published by the Center for Medicare and Medicaid Services, a Federal Agency within the U.S. Department of Health and Human Services.

# **IX. Compensation of Lay Employees and Diocesan Deacons of the Church**

## **Introduction**

Compensation issues related to Lay Employees and Deacons working for a diocese and/or its parishes are numerous and driven by significant federal, state and even local regulations.

This chapter provides a general overview of the following three topics:

- Compensation Defined
- Classification of Personnel as Employees or Independent Contractors
- Exempt vs. Non-Exempt Employees
- Taxation of Ordained Diocesan Deacons

Accordingly, this chapter does not address Lay Retirement Benefit Plans, other employee benefits, or numerous other matters impacting the compensation of Lay Employees and Deacons.

Perhaps the strongest recommendation coming out of this chapter is that dioceses have a good professional relationship with its auditors and attorneys. Some of the content of this chapter may not be equally applicable in every diocese. Since the auditors and the attorneys of each diocese are more acquainted with the specific circumstances of each client, they will often be in a better position to tie their recommendations to the specific circumstances of their clients. Rules from the IRS or the Department of Labor may be complex.

## **Compensation Defined**

In general, compensation includes any payment made by an employer to an employee for services rendered in the course of the employer's business.

## **Other Forms of Compensation**

All forms of payment to employees are compensation and are taxable income, other than reimbursements of expense. This includes stipends paid for various services, Christmas or Easter bonuses, etc. Accordingly, all payments to employees (other than expense reimbursements) should be paid through the payroll system and included in taxable income for the employee.

## **Classification: Employee or Independent Contractor**

The mission of the Church requires the efforts of the ordained, the religious and the laity. When the efforts result in paid compensation to lay people, it is important to record and report the compensation properly. At calendar year end, two methods are prescribed by the Internal Revenue Service (IRS) to report compensation: Form W-2 for employees and Form 1099 for independent contractors. Once a diocese determines the worker status of a lay worker, the reporting procedures

are quite clear. The challenge lies in the determination of worker status (employee vs. independent contractor).

Clearly a full-time lay worker with benefits (e.g. a maintenance worker, office assistant or school teacher) is an employee and thus the employer withholds federal, state and local taxes; withholds and matches Social Security (FICA) and Medicare taxes; and reports compensation and withholdings on Form W-2.

Of course, when a parish hires an outside service (which could conceivably be an individual sole proprietorship) to repair the parish boiler, the parish may properly treat the service as being provided by an independent contractor and issue a check for payment of that contractor's invoice with no withholding obligations. Prior to paying the first invoice the parish will require that the service provider complete Form W-9 to establish the provider's tax status. At the end of the calendar year the parish will issue a Form 1099 to that non-corporate independent contractor for services rendered in excess of \$600 per calendar year. In all cases legal firms should be issued a Form 1099 regardless of their tax status.

Diocesan personnel should be aware that payments to non-employees that are classified as "foreign persons," including payments for goods, reimbursements and services, should be supported by the proper tax form (e.g. Form 8283 for purposes of determining if an exemption from withholding taxes is warranted) and, if the individual is traveling to this country, proper immigration status should be confirmed prior to services being provided.

As a general rule, most individual workers that receive compensation (in whatever form) should be classified as employees. Additional tax, insurance and benefit-related risk may be incurred when employees are incorrectly identified as independent contractors. It is the diocesan entity that should make the classification decision based on its review of all the facts and circumstances; it is not up to the worker as to how he/she should be classified.

Dioceses should refer to **IRS Publication 15-A: Employer's Supplemental Tax Guide** for official guidance on these determinations ([www.irs.gov](http://www.irs.gov)). It is revised annually. State regulations may also affect the classification of employees.

The IRS has provided the following three-category approach to assist employers in determining proper worker classification.

A worker's status under the common law test is determined by applying relevant facts that fall into these three categories: behavioral control, financial control, and the type of relationship itself. In each case, it is very important to consider all the facts – no single fact provides the answer. This common law test applies for purposes of FICA, FUTA, Federal income tax withholding and the Railroad Retirement Tax Act, if there is no controlling statute.

1. ***Behavioral Control.*** Facts reviewed under the Behavioral Control analysis show whether an employer has a right to direct or control how the worker does the work. A worker is an employee when the business has the right to direct and control the worker. The employer

does not actually have to direct or control the way the work is done – as long as the employer has the right to direct and control the work.

For example:

- *Instructions* – if the worker receives extensive instructions on *how* work is to be done, this suggests that the worker may be an employee. Instructions can cover a wide range of topics, for example: how, when, or where to do the work, what tools or equipment to use, what assistants to hire to help with the work, and where to purchase supplies and services. If a worker receives less extensive instructions about *what* should be done, but not *how* it should be done, the worker may be an independent contractor. For instance, instructions about time and place may be less important than directions on *how* the work is performed.
- *Training* – if the worker is provided with training about required procedures and methods, this suggests that the employer wants the work done in a certain way, and the worker may be an employee.

2. ***Financial Control.*** Facts reviewed under the Financial Control analysis show whether there is a right to direct or control the business part of the work.

For example:

- *Significant Investment* – if the worker has a significant investment in his/her work, the worker may be an independent contractor. While there is no precise dollar test, the investment must have substance. However, a significant investment is not necessary to be an independent contractor.
  - *Expenses* – if the worker is not reimbursed for some or all business expenses, then the worker may be an independent contractor, especially if the worker's un-reimbursed business expenses are high.
  - *Opportunity for Profit or Loss* – if the worker can realize a profit or incur a loss, this suggests that the worker is in business for himself and that the worker may be an independent contractor.
  - *Multiple customers* – if the worker has multiple customers, the argument for independent contractor is strengthened. An employer/employee relationship is implied if the Diocese is the worker's only or primary customer.
3. ***Relationship of the Parties.*** These are facts that illustrate how the diocese and the worker perceive their relationship.

For example:

- *Employee Benefits* – if the worker receives benefits this is an indication that the worker is an employee. If the worker does not receive benefits, the worker could either be an employee or an independent contractor.
- *Written Contracts* – a written contract may show what both the worker and the business intend. This may be very significant if it is difficult, if not impossible, to determine status based on other facts. At the same time, a written contract in and of itself should not be the determining factor.
- *Permanency of the Relationship* – the expectation of a relationship to continue indefinitely, rather than for a specific project or time period, is generally considered as intent to create an employer-employee relationship.
- *Services Provided as Key Activity of the Business* – an employee, and not an independent contractor, performs services that are a key aspect of the regular business of the organization.

In uncertain cases, employers have the option of filing Form SS-8: a form designed by the IRS that asks questions about the three factors outlined above. The IRS is usually not quick in responding to a Form SS-8 inquiry. Further, if the employment status is so uncertain, it is likely that the IRS will rule in favor of employee status.

### **Exempt vs. Non-Exempt Employees**

This topic refers to whether an employee is exempt from the overtime rules or is subject to overtime rules (non-exempt). This determination of employee status can be subjective, although there are guidelines from the Department of Labor (DOL).

The overtime rules for non-exempt employees require that those employees be paid for overtime. However, the rules for determining overtime hours and the rates for those hours are complex. The DOL issued a rule updating the salary and compensation levels needed for certain classes of employees to be exempt with an effective date of December 1, 2016. A temporary injunction was issued in November 2016 and on August 31, 2017, a summary judgement (final ruling) was granted striking down the new rule. The DOL has published a Request for information defining and delimiting the exemptions for certain classes of employees. An increase in the exempt salary threshold may apply in the future, but, as of this writing, there are no revisions to the exemption thresholds.

Currently, the FLSA requires that most employees in the United States be paid at least the federal minimum wage for all hours worked and overtime pay at time and one-half the regular rate of pay for all hours worked over 40 hours in a workweek.

However, the FLSA provides an exemption from both minimum wage and overtime pay for employees employed as bona fide executive, administrative, professional outside sales employees and certain computer employees. To qualify for exemption, employees generally must meet

certain tests regarding their job duties and be paid on a salary basis at not less than \$455 per week. Job titles do not determine exempt status. For an exemption to apply, an employee's specific job duties and salary must meet all the requirements of the DOL's regulations.

The following are some categories of exemptions. Please review the DOL summary sheets available on its website for further discussion of the following. As well, be aware that the regulations can be complex and should be reviewed carefully, and that new case law is constantly refining how the following categories should be evaluated.

### Executive Exemption

To qualify for the executive employee exemption, all the following tests must be met:

- The employee must be compensated on a salary basis as defined in the regulations at a rate not less than \$455 per week;
- The employee's primary duty must be managing the enterprise, or managing a customarily recognized department or subdivision of the enterprise;
- The employee must customarily and regularly direct the work of at least two or more other full-time employees or their equivalent; and
- The employee must have the authority to hire or fire other employees, or the employee's suggestions and recommendations as to the hiring, firing, advancement, promotion or any other change of status of other employees must be given particular weight.

### Administrative Exemptions

To qualify for the administrative employee exemption, all the following tests must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$455 per week;
- The employee's primary duty must be the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers; and
- The employee's primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

### Professional Exemption (learned and creative)

To qualify for the learned professional employee exemption, all the following tests must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$455 per week;
- The employee's primary duty must be the performance of work requiring advanced knowledge, defined as work which is predominantly intellectual in character and which includes work requiring the consistent exercise of discretion and judgment;
- The advanced knowledge must be in a field of science or learning; and

- The advanced knowledge must be customarily acquired by a prolonged course of specialized intellectual instruction.

To qualify for the creative professional employee exemption, all the following tests must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$455 per week; and
- The employee's primary duty must be the performance of work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.

### Computer Employee Exemptions

To qualify for the computer employee exemption, the following tests must be met:

- The employee must be compensated **either** on a salary or fee basis (as defined in the regulations) at a rate not less than \$455 per week **or**, if compensated on an hourly basis, at a rate not less than \$27.63 an hour;
- The employee must be employed as a computer systems analyst, computer programmer, software engineer or other similarly skilled worker in the computer field performing the duties described below; and
- The employee's primary duty must consist of:
  - i. The application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software or system functional specifications;
  - ii. The design, development, documentation, analysis, creation, testing or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications;
  - iii. The design, documentation, testing, creation or modification of computer programs related to machine operating systems; or
  - iv. A combination of the aforementioned duties, the performance of which requires the same level of skills.

### Highly Compensated Employees

Highly compensated employees performing office or non-manual work and paid total annual compensation in excess of \$120,000 or more are exempt from the FLSA if they customarily and regularly perform at least one of the duties of an exempt executive, administrative or professional employee identified in the standard tests for exemption. This is a complex exemption that requires a thorough understanding of what constitutes compensation. Reference should also be made to Chapter XX: Income Tax, for additional discussion regarding "Excess Benefit Transactions" and the rebuttable presumption standards for lay employees.

## Outside Sales Exemption

The Outside Sales Exemption would not generally apply to parishes and schools. However, it could apply in entities such as radio and TV stations, cemeteries, etc.; where outside sales personnel may be employed. If this is the case, to qualify for the outside sales employee exemption, the following must be met:

- The employee's primary duty must be making sales (as defined in the FLSA), or obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer; and
- The employee must be customarily and regularly engaged away from the employer's place or places of business.

## **Exemption from Federal and State Unemployment Taxes**

Under federal law, an organization that is exempt from income tax under section 501(c)(3) of the Internal Revenue Code is also exempt from Federal Unemployment Tax (FUTA). Additionally, this exemption also applies in several states.

## **Taxation of Ordained Deacons**

When a deacon (whether transitional or permanent) begins working for a diocese, it is very important to determine if the deacon is a member of a religious institute. If he does belong to a religious institute, even if he is working for a diocese, his compensation is subject entirely to the provisions of the preceding chapter on the compensation of religious. What follows in this chapter pertains only to diocesan deacons.

## Permanent Deacons

Depending upon the facts and circumstances of their Church employment, permanent deacons will be classified either as lay employees or "ministers of the gospel" for tax purposes. This is not an option to be made at the discretion of the deacon or the Church employer. To be classified as a minister of the gospel under the Internal Revenue Code, the deacon must be "ordained, commissioned, or licensed" as a minister *and* must be performing the duties that are normally those of a minister of the gospel. All ordained permanent deacons meet the first requirement. However, all permanent deacons do not necessarily meet the second requirement. The specific job performed by a particular deacon must be analyzed to determine whether that job involves the performance of duties that are normally those of a minister of the gospel. Under IRS regulations, these will include "the ministration of sacerdotal functions and the conduct of religious worship, and the control, conduct, and maintenance of religious organizations (including the religious boards, societies, and other integral agencies of such organizations), under the authority of a religious body constituting a church or church denomination." Whether an activity constitutes a "sacerdotal function" depends on the tenets or practices of the particular church or denomination. Under canon law, deacons do not perform the same sacerdotal functions as priests but may nonetheless perform services normally done by those of a minister of the gospel within the meaning of the IRS regulations. It is recommended that decisions about the proper classifications of deacons for tax



purposes be made centrally by the diocese to ensure consistency of interpretation among deacons in similar job categories.

If a deacon qualifies as a minister of the gospel for tax purposes, he must be treated consistently as such for *all* tax purposes. Thus, such a deacon is eligible for the Section 107 housing allowance exclusion (assuming all other applicable requirements are met) and must also be treated as self-employed for social security purposes, being liable for SECA taxes. If a deacon does not qualify as a minister of the gospel for tax purposes (i.e. he is not performing duties that are normally those of a minister of the gospel), he must be treated in the same manner as lay employees for tax purposes.

### Transitional Deacons

When a seminarian is ordained to the diaconate, he should be treated in the same manner as an ordained permanent deacon for tax purposes. Thus, if he is assigned to a parish during the summer or for a year-long training assignment and is performing duties that are normally those of a minister of the gospel, he would be eligible for the Section 107 housing allowance exclusion and would be treated as self-employed for social security purposes and be liable for SECA taxes. If he is not performing duties that are normally those of a minister of the gospel, he would be treated in the same manner as lay employees for tax purposes.

An additional reference that is helpful with tax treatment of deacons is Scott A. Hoselton's *Tax Manual for Deacons*, published by Shepherds Advisor.

## **X. Diocesan Payments Associated with Priestly Formation**

### **Introduction**

The education and financial support of seminarians are provided by dioceses through various means. Education is typically provided through enrollment in a seminary, and financial support may be provided for tuition, books, room and board, travel, medical, and other living expenses. There are four general financial arrangements.

1. Costs incurred are the responsibility of the seminarian, and paid by him or his family, unless otherwise provided for below.
2. Costs paid by the diocese are either made directly to the seminarian or to the educational institution on the seminarian's behalf.
3. The diocese may provide a loan to the seminarian with a written and signed promissory note. The loan may provide for forgiveness of the debt if certain conditions are met.
4. The seminarian obtains an educational loan from a third-party lender, with a commitment from the diocese to repay the loan on the seminarian's behalf if certain conditions are met.

These four arrangements are not mutually exclusive; dioceses may use a combination of the above arrangements in providing for the various financial needs of the seminarian.

### **Accounting Treatment**

All costs paid by the diocese on behalf of the seminarian without any expectation of repayment (arrangement #2 above), are to be recorded as an expense in the period incurred. Tuition payments made in advance of the semester or school year are to be recorded as prepaid tuition and amortized over the period in which the instruction occurs.

Loans made by the diocese to the seminarian (arrangement #3 above) are to be recorded as such if, at the time of the loan, it is documented with a signed promissory note and there is a reasonable expectation of repayment or satisfaction of conditions stipulated for the forgiveness of the debt. A decision to recognize these payments as assets (loans/notes receivable) must be made in light of the diocese's past record of either collecting them or achieving the conditions stipulated for forgiveness. Loans to seminarians are to be reviewed regularly for collectability in the same manner as other loans and an allowance is to be provided (expense is to be recorded) in order to state the asset at its net realizable value whether for reasons of collectability or satisfaction or conditions stipulated for forgiveness. However, the reason would define the nature of the expense as either bad debt expense or a program expense.

In some cases, a loan is interest free or has a below-market interest rate. In this situation, a portion of the loan is to be recognized as interest, and the loan should be recorded at the present value of the future estimated cash flows.

To calculate the portion of the recorded loan which represents interest, calculate the present value of the loan, using an applicable interest rate even though it may differ from the stated rate. This process is called imputing interest, and the resulting difference between the amount of the loan

and the present value of the loan is to be recorded as a discount on the loan and as a program expense.

When determining an appropriate interest rate, to the extent possible, the diocese would consider market inputs relevant to the loan being made. These might include the time value of money, credit standing of the borrower, collateral, duration of the loan, restrictive covenants, and liquidity. In the absence of market inputs, the diocese would use its own assumptions about the assumptions that market participants would use under similar circumstances.

### Example

A diocese lends \$100,000 to a seminarian to cover the cost of his education. The note is noninterest bearing, is unsecured, and a balloon payment is due at the end of the 5-year term. The diocese determines that a market rate for a loan with the same terms and a borrower of equal credit worthiness as the seminarian is 15 percent. The present value of the contractual payments due under the loan is \$49,720. Using the interest method, the diocese would make the following entry:

|  |           |           |
|--|-----------|-----------|
| Loan receivable                                  | \$100,000 |           |
| Program Expense                                  | \$50,280  |           |
| Cash   |           | \$100,000 |
| Discount on loan receivable (a contra-asset a/c) |           | \$50,280  |

Use of the Interest Method while the loan is outstanding:

The discount on the loan is amortized as interest income over the life of the loan in such a way as to result in a constant rate of interest when applied to the amount outstanding at the beginning of any given period. The difference between the periodic interest cost calculated using the interest method and the nominal interest on the outstanding amount of the debt is the amount of periodic amortization. Continuing the example above, at the end of year 1, the diocese would make the following entry to amortize the discount and record the imputed interest income at 15 percent of the implied principal amount of the loan ( $\$49,720 \times 15\%$ ):

|  |          |         |
|--|----------|---------|
| Discount on loan receivable (a contra-asset a/c) | \$ 7,458 |         |
| Interest Income                                  |          | \$7,458 |

If a loan that is not impaired is forgiven and the diocese communicates to the borrower that the amount is forgiven, the diocese should recognize a program expense. In the case of loans that specify conditions for forgiveness, the outstanding loan balance is accounted for, as described above, as a loan receivable until all of the specific conditions are met. Once the conditions are met, the diocese should adjust the outstanding loan balance to zero with a corresponding adjustment made to program expense. Communication of the forgiveness to the borrower is key to the classification, because in accordance with FASB ASC 405-20-40-1, the debt is not extinguished until the debtor is legally released from being the primary obligor under the liability. In the absence of that communication, the diocese continues to act as a lender rather than a donor.

Commitments made by the diocese to repay loans on the seminarian's behalf (arrangement #4 above) are to be recorded as a liability when the conditions surrounding the commitment have

substantially been met. When the conditions surrounding the commitment have substantially been met, the expense and the corresponding accrual should be recorded at fair value. Consideration should be given to disclosing the value of conditional commitments in the footnotes to the financial statements.

### **Income Tax Considerations**

Arrangement #1. No tax consequences to the diocese.

Arrangement #2. Under Internal Revenue Code section 117, amounts paid by the diocese to or on behalf of a seminarian who is a degree candidate at an educational institution for tuition or amounts used for required books, supplies, fees and equipment are excludable from the seminarian's income for federal income tax purposes as well as FICA and FUTA taxes. The IRS has issued rules that classify tuition assistance and other related educational or support expenses. The IRS rules provide:

"Qualified Tuition Assistance," also known as scholarships, is excluded from taxable income only to the extent that:

- a. It is for tuition, fees, books, supplies and equipment required for instruction; and
- b. It is incurred by a seminarian who is a candidate for a degree. A candidate for a degree must:
  - i. Pursue a degree at a college or university; or
  - ii. Attend an educational institution that:
    - a. Provides a program that is for full credit toward a bachelor's or higher degree; or
    - b. Offers a program of training to prepare students for gainful employment in a recognized occupation.
    - c. Is authorized under federal or state law to provide such a program and is accredited by a nationally recognized accreditation agency.
    - d. No duties are required to be performed for the Diocese as a condition of receiving the scholarship grant.

"Non-Qualified Educational Assistance" expenses are taxable to a seminarian. Payments made on behalf of the seminarian that are subject to income taxation include but are not limited to the following:

- a. Room and Board
- b. Travel
- c. Medical insurance
- d. Equipment, supplies, books, not required for enrollment or attendance at an eligible educational institution;
- e. Stipend paid to seminarians

Items a through d above are reported to the seminarian on a Schedule A to be used by the seminarian for tax reporting purposes. Stipends (item e) are reported on Form 1099-Miscellaneous that is issued by the Diocesan Finance Office in January of each year (See Taxability of Other Benefits and Payments, below).

A recommended practice would be to provide each seminarian with an annual statement (known as Schedule A) that informs him of any taxable amounts provided by the diocese for each calendar year to assist the seminarian in preparing his own federal and state income tax returns. The statements should be delivered to the seminarian by January 31 of the year following the calendar year for which the taxable amounts were provided.

Arrangement #3. A bona fide loan made by the diocese to the seminarian does not represent taxable income to the seminarian. However, subsequent forgiveness of the loan will usually result in taxable income to the seminarian and should be reported as wages on Form W-2 (if the seminarian is an employee) or income on Form 1099-MISC, box 7 (if the seminarian is not an employee). It is recommended that any discharge of indebtedness be done gradually so that the seminarian's federal and state income tax liability associated with the discharge is spread over multiple years.

Arrangement #4. A commitment made by the diocese to repay a loan on a seminarian's behalf if certain conditions are met does not represent taxable income to the seminarian at the time the commitment is made. However, the diocese's subsequent repayment of such a loan on the seminarian's behalf will usually result in taxable income to the seminarian for the reasons described in the previous paragraph and should be reported as wages on Form W-2 (if the seminarian is an employee) or income on Form 1099-MISC (if the seminarian is not an employee).

### **Taxability of Other Benefits and Programs**

No simple rule exists regarding the taxability of other benefits for seminarians. However, their employment status appears to be that of either a non-employee student, or as an employee. Seminarians who provide various types of services and receive various payments and items of value, while at the seminary and while serving in the parishes should be classified as an employee at those entities. These payments could easily be classified as payments for services. In addition, dioceses and parishes often supervise the time, manner and methods by which services are performed as well as the training the seminarian receives. Seminarians often use tools and supplies provided by the diocese or parish. Seminarians are clearly not independent contractors engaged in these activities to make a profit, and they usually receive non-employee-type benefits such as health insurance. Given these circumstances, the tax relationship between the diocese and the seminarian appears to be either a student (non-employee) or in some cases an employee. Seminarians are usually not ordained unless they become a transitional deacon. Without meeting the requirements of Internal Revenue Code section 3401(9) and Treasury Regulation §1.1402(c)-5 which limit exemptions to "duly ordained, commissioned, or licensed ministers of a church," seminarians do not qualify to be treated as clergy. Thus, benefits such as room & board, personal travel expenses, medical insurance, out-of-pocket medical expenses, and living allowances or stipends, may be taxable to the seminarian if not exempt under another provision.

Please note that taxable education assistance expenses paid on your behalf are not subject to Social Security or Medicare withholding. Stipends, however, are subject to Social Security and Medicare tax on Form 1040SE.

## **Foreign Seminarians**

Foreign seminarians are required to follow the same process for scholarships and tax assistance as U.S. born citizens. A distinction exists between resident alien and nonresident alien seminarians. Resident alien seminarians already have a social security number and are treated like U.S. citizens for tax reporting purposes. Nonresident aliens have stringent reporting and work rules that must be followed as discussed below.

### **A. U.S. Citizen or Resident Alien**

The diocese is required to report to you the value of the taxable benefits it provides on Schedule A. However, you, as the recipient of these benefits, are required to file a tax return and report the taxable value of those benefits. U.S. citizen and resident alien seminarians report their taxable income on either Form 1040 or Form 1040-EZ. To assist you with your reporting obligations, the diocese will annually issue a statement to you indicating the value of the taxable benefits that you received. If you file Form 1040, you should report the value of the taxable benefits on line 7 and write the letters “SCH” (short for Scholarship) next to that line. If you file Form 1040EZ, you should report the value of the taxable benefits on line 1 and write the letters “SCH” next to it.

Please note that these taxable education expenses are not subject to social security or Medicare withholding. You need not report them on Schedule SE.

The diocese will also issue you a Form 1099-MISC for stipend income that you received. You must report both the stipend income and the value of the Non-Qualified taxable benefits that you receive on your tax returns.

Resident aliens and U.S. citizens are taxed on their worldwide income (not merely U.S. source income), which must be reported on their U.S. income tax returns, Form 1040 series. Resident aliens may claim the same deductions and credits as U.S. citizens, and are taxed at the same rates as U.S. citizens.

### **B. Nonresident Alien**

If you are a nonresident alien seminarian, it is your responsibility to obtain an individual tax identification number (ITIN) from the Internal Revenue Service using Form W-7 and to provide that individual tax identification number to the Vocations Office. The diocesan corporation’s vocations office and its finance office can assist you in filing for this identification number. Please contact the vocations office to request this assistance.

Nonresident alien seminarians are required to file Form 1040NR or Form 1040NR-EZ to report their U.S. source taxable income each year. You will receive a Form 1042-S from the diocesan corporation that will set forth the total value of your stipend income and the taxable benefits that were paid to you or on your behalf. The diocesan corporation is required to withhold taxes from

these amounts. To claim a treaty exemption from withholding at the time of payment with respect to either wages or independent contractor payments, you must submit Form 8233 to the withholding agent, the diocesan corporation. To claim a treaty exemption from withholding at the time of payment with respect to scholarship payments, you must submit Form W-8BEN to the withholding agent.

You are responsible for completing the correct tax forms and providing them to the diocesan corporation. In addition, you must always advise the vocations office of any change in your tax status, change of address, and change in your visa status.

Please note that the United States Citizenship and Immigration Services (“CIS”) now requires all non-citizens to report a change of address (Form AR-11) within 10 days of the address change. Failure to do so may subject the individual to criminal penalties and removal from the United States.

### **Nonresident Alien Seminarian Visa Status (Short Overview)**

The first step that any foreign seminarian takes to enter the diocese is through the United States Citizenship and Immigration Services (“CIS”). This process includes obtaining approval from the diocese and the bishop, and from one of the specific seminaries that are authorized to enroll foreign students.

CIS regulations require that all schools that are duly authorized to enroll foreign students must have a designated school official (“DSO”) who is authorized to annotate the Form I-20 A-B. While the scope of the foreign student visa process is beyond the scope of this memorandum, it is important to note that this annotation becomes significant for employment matters as they relate to F-1 visas. Generally speaking, students holding F-1 visas are prohibited from working in the United States; however, there are certain exceptions to this rule.

A nonresident alien may be permitted to participate in a curricular practical training program that is an integral part of an established curriculum. Curricular practical training includes work/study programs, internships, and cooperative practical training programs that are an integral part of the established curriculum at his seminary. If a nonresident alien seminarian is paid for curricular practical training performed in a parish, his wages would be considered effectively connected with a trade or business in the U.S. and he would be taxed at the same rates that apply to U.S. citizens and resident aliens. If the seminarian is an employee, his wages would be reported on Form W-2, but no FICA taxes would be withheld from wages paid to nonresident alien seminarians by parishes as part of their curricular practical training. If the seminarian is an independent contractor, his payments would be reported on Form 1042-S.

### **Taking non-Degree Program Courses**

Students who are taking college preparatory courses or studying English as a second language in preparation for becoming a seminarian will be taxed on the full value of the education assistance (including tuition and the cost of required supplies and books) provided to them by the diocese because these students are not pursuing a degree. These programs include language studies that a seminarian may wish to pursue for ministerial purposes; he should let the Vocation Director know. This is subject to the approval of the Vocation Director.

There is the Institute for Priestly Formation (I.P.F.) the diocese will pay the full cost of the summer spiritual program if a seminarian is assigned to participate by the bishop.

### **Nonresident Alien Change in Status**

Upon completion of their studies, seminarians who have been ordained to the diaconate (transitional) and ultimately to the priesthood are considered ministers of religion. Once their studies are complete and by virtue of their religious vocation, seminarians on an F-1 visa may apply to the CIS to change their student status to the R visa nonimmigrant category as ministers of religion.

This is an important step for two reasons:

1. Once in the R visa nonimmigrant category, they can begin accumulating the requisite 2-year experience needed to adjust status to permanent residents, assuming that the diocese sponsors them. Specialized immigration counseling should be obtained to determine the proper time to seek a change in immigration visa status.
2. As an ordained minister, their tax reporting status changes to a “dual-taxpayer” status (see Chapter VI: Compensation of Priests and the Dual Tax Status of Priests).



## **XI. Deposit and Loan Programs**

Many dioceses, through their Administrative Offices or a separate legal entity, accept deposits from parishes, schools, agencies and/or other ecclesiastical entities within the diocese. In turn, these funds are loaned to parishes and potentially other entities within the diocesan community, with excess funds being invested. Names for this may vary (deposit and loan fund, capital revolving fund, savings and loan program, etc.); but for the purposes of this chapter, this activity will be termed “deposit and loan fund” and/or “the Program.” In the majority of instances, the Program will be (1) one where the Administrator acts as a principal paying a return to depositors and charges interest to borrowers (diocesan program), (2) an investment and lending program that operates for the mutual benefit (mutual program) of the parishes and other participating agencies/entities of the diocese (the participants bear the loan and investment risks and proceeds), or (3) one where an option is given to the depositors to participate in a type (1) or type (2) arrangement (hybrid program).

Deposit rates should be reviewed (and adjusted as appropriate) on a periodic basis to remain attractive to depositors.

Loan rates should be reviewed (and adjusted as appropriate) on a periodic basis. Market rates and other diocesan program rates may be used as benchmarks.

### **Civil Structure**

The civil structure of the Program may vary from diocese to diocese depending upon the policies, diocesan civil structure, applicable state laws, regulatory considerations, canonical determinations, and other financial and operating considerations of the diocese. Examples of such structures would be as a separate Trust or as a separate Corporation. While some dioceses elect to include the Program as a Fund within the existing civil structure of the diocese, best practices suggest that careful consideration must be given to establishing either a Trust or Corporation to account for and report the operating activities of these programs. When a separate entity is established and the program is administered by staff of the diocese (as opposed to employees of the separate entity), best practices include the adoption of a Financial Services Agreement between the two entities. This document specifies services to be provided by both parties, compensation for the performance of services and appropriate indemnification language.

### **Risk & Return Considerations**

The financial risks and returns of a Program can either inure to the benefit of the sponsor (diocese, separate trust, corporation, etc.) of the Program (diocesan program) or to the depositors participating in the Program (mutual program). When designing the Program, an important consideration should be determining who will benefit from income and losses of the Program.

## **Advantages for Borrowers**

The deposit and loan funds generally operate on a revolving basis where cash from parishes and others are accumulated and loaned out at an interest rate that may be less than that commercially available. Loan origination points, application charges, loan servicing fees, and the establishment of financial debt covenants are either non-existent or generally less than what commercial banking terms would be. Likewise, the internal loan documentation may be less rigorous for both parishes and dioceses.

In addition, dioceses are often in a more flexible position in regard to defaults.

## **Advantages to Depositors**

The Program generally pays an attractive yield on deposits in the fund and conditions on withdrawals of funds may not be as restrictive as a typical financial institution. In addition, it may be reassuring to a parish community, including its pastor and the parish finance council, that their cash funds are maintained within a diocesan Program.

## **Establishment of the Program**

Diocesan entities with cash in excess of day-to-day operating requirements should be encouraged or required, according to the respective diocesan policy, to place their surplus cash or a portion thereof in the Program. The Program will promulgate a governing document that defines the Program's purpose, provides for accountability and transparency and identifies all entities within the diocese eligible to participate in the Program.

## **Operating, Investment and Lending Policies**

In addition to a governing document, the following policies should be established:

1. Loan/underwriting policy
2. Deposit policy/agreement
3. Investment policy statement

The Program should be operated in a prudent manner. That includes the distribution of periodic statements of account to both the depositors and the borrowers.

The Program's investment approach must be carefully evaluated and monitored. The investment asset allocation and the nature of the investments themselves should be designed to "match" the liquidity needs of the Program's depositors. Generally, the investment approach should be conservative.

Loans should be (1) evaluated and approved based on financial projections furnished by prospective borrowers; (2) evidenced by formal promissory notes indicating repayment schedules and interest rates, signed by proper ecclesial authority – including the acknowledgement of the respective parish finance council representatives; and (3) regularly reviewed. The Program should

utilize a standard promissory note that can be modified for certain borrower's needs and/or specific terms and conditions. The promissory note should reference conformity to both Canon Law and the governing laws of the state in which the diocese operates. Because the amounts loaned under the note are the patrimonies of other parishes and/or agencies within the territory of the diocese, consideration should be given to disclosing this in the note and have the borrower acknowledge that such funds have been made available to it in a spirit of mutual assistance. Finally, the borrower should also acknowledge its legal and moral responsibility to repay the promissory note in a timely and responsible manner. A sample promissory note is included later in this chapter. Consideration should be given to identifying collateral for the loan, such as real estate that may be available for sale.

The regular review of the lending arrangement and of the credit status of the borrowers will usually include monitoring of the borrower's financial condition, budgets and capital purchases. The liquidity of the Program is important for operational purposes. Formal cash projections should be prepared using loan repayment schedules and anticipated loans, deposits, and withdrawals. Projections should be updated frequently and reviewed according to prescribed policy.

Under certain conditions the loan may be classified as a programmatic loan. The primary criteria for classification as a programmatic loan is that the determination to enter into the loan agreement is to further the mission of the diocese with minimal, if any, consideration given to the production of income. Programmatic loans may bear interest at or below the market rate. The discount associated with programmatic loans bearing a below-market interest rate should be recognized as a contribution expense and by establishing a valuation allowance. The valuation allowance should be amortized as interest income over the life of the note. If a programmatic loan that is not impaired is forgiven and the forgiveness is communicated to the borrower entity, the forgiveness should also be recognized as a contribution expense.

### **Allowance for Loan Losses**

Provision should be made for loans that will be uncollectible in the ordinary course of operations. An allowance should be established and loans should be written off when they are determined to be uncollectible. The approval for the write-off of loans as uncollectible should be substantiated. Reference should be made to Topic 310 of the Accounting Standards Codification, Receivables, and specific disclosures about the credit quality of financing receivables and the allowance for loan losses. Pursuant to Accounting Standards Update No. 2010-20, the diocese should make financial reporting disclosures to facilitate the users' evaluation of the loans within the Program, including:

- The nature of credit risk inherent in the Program's portfolio of financing receivables
- How that risk is analyzed and assessed in arriving at the allowance for loan losses
- The changes and reasons for those changes in the allowance for loan losses

At a minimum, all loans should be reviewed on an annual basis for collectability and allowances adjusted accordingly. Policies should be adopted that ensure consistency in loan collectability reviews.

### **Financial Reporting**

For financial reporting purposes, the recipients and users of the reports and the civil structure of the Program should be considered in determining the form and content of the report. These considerations would include, but not be limited to, those of “control” and “financial interest.”

In a diocesan program, the Administrator of these funds should include the operation of the Program in its combined financial statements, and the footnotes to the financial statements should clearly state the Program’s purpose and its relationship to the diocese. The diocese may want to consider creating a separate financial report for the Program which can be presented to its depositors.

If the Program is a separate legal entity, a complete set of financial statements should be prepared in accordance with Generally Accepted Accounting Principles on an annual basis. It is recommended that the management or administrator of the Program consider having these statements audited independently by a CPA firm.

### **Oversight**

It is recommended that the Program has an Administrative Committee, Board of Trustees, or Board of Directors, whose role is to meet on a periodic basis and:

- Review the financial position of the Program
- Review the loan portfolio and loan risk
- Approve significant loans
- Provide guidance on investment of deposits, loan rates, and deposit rates

**SAMPLE PROMISSORY NOTE – This is a sample document and should be reviewed by diocesan counsel and tailored to the specific requirements of the Diocesan Deposit and Loan Program**

**Promissory Note**

\$

(Date)

For value received, \_\_\_\_\_, (Name of the parish, school or agency) – (City), a separate juridic person under the 1983 Code of Canon Law of the Roman Catholic Church and a \_\_\_\_\_, (parish, school or agency) within the Diocese of \_\_\_\_\_ (“the Borrower”), promises to pay to the order of (insert name of the Program, the Trust or legal entity) (the “Trust” or the “Lender”), the lessor of \$ \_\_\_\_\_ or so much thereof as may have actually been advanced under the terms of this Note together with any interest accrued and unpaid until all amounts owing under this Note are paid in full. The parties acknowledge that the Lender has executed this Note to allow the Borrower to draw funds for the exclusive use of funding construction costs related to the “\_\_\_\_\_” (the Project). The parties further acknowledge that the loan proceeds are being used for the specified purposes only.

Borrower agrees to abide by the promises and agreements entered into under this Agreement.

Terms and Conditions:

1. Borrower is required to repay this Note in \_\_\_\_\_ years from the date of the Project completion (Date of Completion). The Date of Completion shall be defined as the earlier of (i) 30 days after the Borrower is issued a certificate of occupancy, if applicable or (ii) 30 days after the advancement of all the proceeds under the Note. Monthly payments, which include both principal and interest (the Payment) will be established based on a prepared amortization schedule which will be calculated based on the outstanding balance due on the Note and the Lender’s lending rate upon Date of Completion. Each payment of principal and interest shall be paid by the Borrower on the first of the month pursuant to the prepared amortization schedule, without any right of set-off or counterclaim to: (insert name and address of the Program, the Trust or legal entity). The initial payment shall be due on the first day of the month following the Date of Completion. If any payment under this Note becomes due and payable on a day other than a business day, the payment shall be due on the next succeeding business day, provided, however, that if the date for any payment of interest is extended as provided hereunder or by operation of law or otherwise, interest shall continue to accrue and be payable at the then applicable rate during such extension. Any payments required for any other fees, charges or miscellaneous payments will be invoiced to the Borrower and are due within 30 days after receipt.
  - a. Amortization Reset – The principal amortization schedule for this Note, as set forth in section 1 above, may be adjusted one time during the term of the Note as the Borrower and the Lender shall agree (“the Amortization Reset”) in the event that (i) the Borrower prepays the principal amount owing with respect to any such Note in an aggregate amount equal to at least \$50,000 (the “Prepayment Increment”) and

(ii) such Prepayment Increment is made during the first twelve months from the Date of Completion (“the Reset Period”). At such time as a Prepayment Increment has been made with respect to the Note, then within the first 15 business days of the next succeeding calendar quarter, upon the written request of the Borrower, the Lender shall affect the Amortization Reset at the prevailing interest rate at that time, as described in section 3 below, and over the remaining term of the Note.

2. No additional advances will be made under the terms of this Note after the Date of Completion regardless of whether or not the full amount of the Note has been drawn.
3. This Note has a variable interest rate feature. The interest rate on this Note may change from time to time if the rate identified below changes. Interest shall be computed on the basis of 365 days per year. Interest on this Note shall be calculated and payable at a variable rate equal to the Prime Rate (“Prime Rate”) as published in the Wall Street Journal. The current Prime Rate on this Note would be \_\_. \_\_% per annum, assuming advances were made concurrent with the date of this Note. Interest rate changes on this Note will occur the first day of the month following the day that the Prime Rate changes. Interest shall accrue on each advance under this Note on the date such advance is loaned to Borrower. The Borrower should be aware that it may have a balloon payment due upon the maturity date of this Note due to the fluctuations in the interest over the term on the Note.
4. This Note allows for the prepayment of principal and interest amounts due hereunder, without a penalty.
  - a. However, the Payment, as defined within this Note, must be made on time on the first of *each* month, regardless of prepayments until the outstanding principal, together with all accrued interest, is paid in full.
  - b. Prepayments will not be considered in the determination of the Note’s past-due status or delinquency.
  - c. The Borrower is past-due if the monthly Payment is made after the scheduled date (the first of each month) and delinquent if the monthly Payment is not made.
5. Upon Default, as defined herein, the interest rate on this Note shall be increased to the interest rate in effect at the time of Default, plus two percent (2%).
6. All pledge payments or contributions received by Borrower for the Project are to be sent to (insert name of the Program, the Trust or legal name of entity) and deposited into Borrower’s designated savings account until Borrower directs that they be used to make construction payments, scheduled Payments and/or to make Prepayment Increments until the outstanding principal together with all accrued interest is paid in full.
7. Lender reserves the right, at its sole discretion, to assign or sell all or any part of the outstanding indebtedness under this Note to a commercial lending institution of Lender’s choosing at any time.

8. The terms and conditions of this Note are governed by the particular laws of the Diocese of \_\_\_\_\_.

### Covenants

Until the Note is paid in full, together with any and all accrued and unpaid interest thereon and all other amounts due hereunder (other fees, charges or miscellaneous payments as defined below) are paid and satisfied in full, and this Promissory Note has been terminated, the Borrower covenants and agrees that it will:

1. Use all loan proceeds solely for the Borrower's funding toward the Project.
2. Promptly inform lender in writing of (i) all adverse changes in the financial condition of the Borrower; and (ii) any and all matters affecting the Borrower that could materially affect the Borrower's financial condition.
3. The Borrower recognizes its obligations to repay the indebtedness referenced herein and commits that such repayment obligation shall always hold a preeminent position in current and future budgeting and planning. Borrower also recognizes that it may need to reduce its future operating budgets in order to accommodate the debt service of this Note.
4. Borrower must continually re-evaluate its ten (10) year forecast, provided to (insert the name of the Program, the Trust or legal name of entity) dated as of \_\_\_\_\_, to ensure that it can balance its operating budget, (i.e. revenues must exceed or equal expenditures, including debt and interest payments).
5. Borrower must encourage parishioners to remain faithful to their offertory donations during the pledge payment period.
6. Borrower covenants and agrees that it will not incur any additional indebtedness until the Note has been paid in full without the prior written approval of the (insert name of the Program, the Trust or legal name of entity). A violation of this covenant shall be deemed an event of default under the terms of the Note.
7. Perform and comply with all terms, conditions and provisions set forth under the Note, and promptly notify Lender of the occurrence or imminent occurrence of any event or circumstance that may constitute a Default under this Note and/or the other obligations of Borrower.
8. (Add other relevant covenants as necessary. May want to consider reporting requirements during the construction period and while the loan is outstanding).

## Events of Default and Lender Remedies

1. If any one or more of the following events occur and be continuing, it shall constitute a “Default” by Borrower:
  - a. Non-payment. Borrower shall fail to pay the principal and interest hereunder when due (whether as stated or at maturity, by acceleration or otherwise), within five (5) business days after the principal or interest shall become due and payable, or shall fail to pay any other fees, charges or miscellaneous payments payable hereunder within 30 days after such other fees are invoiced; and fails to notify the Lender (or respective entity managing the Program) prior to the end of such five or thirty day period or such earlier time as the payment at issue is otherwise due, that Borrower is unable to meet its repayment obligation(s) hereunder; or,
  - b. Compliance. Borrower shall fail to comply with the Covenants and any other terms and conditions of this Note, or fails to comply with the terms and conditions of any other agreement between Borrower and Lender; or
  - c. Material adverse change in financial condition. Any material adverse change in Borrower’s financial condition, either as disclosed to Lender by Borrower or as determined by Lender in review of Borrower’s routine financial reports and other information.
  
2. Remedies in the Event of Borrower Default.
  - a. Other Action as Warranted. Lender may take such action as may be lawful and, in Lender’s sole discretion, is deemed warranted with respect to the outstanding obligations of Borrower to Lender hereunder, including the acceleration of the indebtedness, and Lender shall be entitled to all such remedies as legal and equitable principles allow.
  - b. (In the case of a material default during the construction phase, diocese may want to have the right to take over the administration of the project and charge an appropriate project management fee).

## Representations, Warranties and Other

1. The Borrower acknowledges that the amounts provided under this Note are the patrimonies of other parishes and organizations within the territory of the Diocese of \_\_\_\_\_ that have been generously made available to it in a spirit of unity and mutual assistance. The Borrower also acknowledges its legal and moral responsibility to repay this Note in a timely and responsible manner and pledges to do the same.
  
2. The Borrower agrees not to assign any of the Borrower’s rights or obligations described in this Note without the prior written consent of Lender, which consent may be withheld by Lender in its sole discretion. The Borrower agrees that Lender is entitled to assign some or all of its rights and remedies described in this Note with appropriate notice to Borrower but that no consent from the Borrower is required.



3. The Borrower agrees to make payment to Lender at any address designated by Lender and in lawful United States currency. The Borrower waives presentment, demand for payment, notice of dishonor and protest and further waives any right to require Lender to proceed against anyone else before proceeding against the Borrower. This Note shall be binding upon the heirs, successors and assigns of the Borrower and Lender. This Note represents the complete and integrated understanding between the Borrower and Lender regarding the terms hereof and may not be modified, amended or waived except by a written instrument duly executed by both parties.
4. Borrower hereby represents and warrants that this Note constitutes the legal, valid and binding obligation of Borrower enforceable in accordance with its terms, except to the extent that enforceability may be limited by applicable bankruptcy, insolvency or other similar laws of general application relating to or affecting the enforcement of creditor's rights from time to time in effect.
5. To the extent permitted by law, the Borrower agrees to pay Lender's reasonable attorney's fees and other costs incurred in collecting any amount due or enforcing any right or remedy under this Note, including audit or internal investigation fees incurred should there be a material adverse change in the Borrower's financial condition.
6. This Note shall be governed in all respects by the laws of the State of \_\_\_\_\_ and the Code of Canon Law of the Roman Catholic Church.

**BORROWER:**

(Name of the Parish, School or Agency), a \_\_\_\_\_ (Parish, School or Agency) of the Diocese of \_\_\_\_\_

By: \_\_\_\_\_  
 \_\_\_\_\_  
 Name and Title

Witnessed and approved by the \_\_\_\_\_ (Name of appropriate body and Parish, School or Agency)

By: \_\_\_\_\_ (Name of Chairperson), Chairperson of  
 \_\_\_\_\_ (Name of appropriate body and Parish, School or Agency)

**APPROVED:**

(Name of Program)

By: \_\_\_\_\_  
 \_\_\_\_\_  
 Name and Title

**SAMPLE DEPOSIT AGREEMENT – This is a sample document and should be reviewed by diocesan counsel and tailored to the specific requirements of the Diocesan Deposit and Loan program and any applicable state laws. Consideration should be given to create a similar document for other investment programs.**

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Name of Program  
**Deposit Account Agreement  
Terms and Conditions**

1. **INTRODUCTION** – The (Name of Program) (“the Program”) is only available to entities of the Diocese of \_\_\_\_\_. This Agreement governs the use of the Program’s services by \_\_\_\_\_ (Name of Parish, School or Agency) hereafter referred to as “Depositor.” Use of services is expressly conditioned on acceptance of this Agreement as indicated by the execution of this Agreement by an authorized signer. By using the services of the Program, you acknowledge that you have read and agree to abide by the terms and conditions of this Agreement, which will be binding upon Depositor.
2. **DEPOSITS** – Depositor may make deposits to its account(s) with the Program by mailing a check to the Pastoral Center Finance Office, along with a letter of transmittal indicating the account number to which the funds are to be deposited or instructions to open a new account.
3. **WITHDRAWALS** – Depositor may make withdrawals from its account by providing written notice 5 days in advance in any amount up to the balance in the account less the minimum required balance if the Depositor desires to remain in the Program.
4. **MINIMUM REQUIRED BALANCES** – The minimum required balance for the Program is \$100.
5. **TERM** – Funds on deposit in the Program are not subject to a minimum investment period.
6. **AUTHORIZED SIGNATURES** – The parish priests are the authorized signers for parish accounts, including parish schools. The principal and superintendent of schools are authorized signers for non-parish schools. Agency directors are the authorized signers for agencies. In lieu of the above, upon written request by an authorized signer, the diocesan bishop, vicar general or chief financial officer may sign on behalf of authorized signer. The Program will only honor requests from an authorized signer for withdrawals or other transactions related to your account. Requests for withdrawals must be in writing and must contain a handwritten signature – copies, facsimiles, or signatures that appear to be made by machine or stamp, or otherwise, will not be honored.
7. **STATEMENTS** – Account statement(s) will be mailed or made available on a quarterly basis and will include the amount of interest earned, if any, for the statement period.

- 8. INTEREST CALCULATION** – Interest will be calculated and credited to Depositor’s account(s) on a monthly basis based upon the number of days funds are on deposit using the interest rate, which is \_\_\_\_\_, with a minimum interest rate of \_\_\_\_\_.
- 9. OWNERSHIP OF FUNDS ON DEPOSIT** – Funds on deposit are held by the Program in trust for the Depositor, which is the owner of the funds on deposit. Furthermore, the Canonical Pastor/Administrator duly appointed by the Bishop of \_\_\_\_\_ is the administrator of the assets of the parish/juridic person according to the internal law and rules of the Roman Catholic Church. No funds placed with the Program become funds of the Program or of the Diocese of \_\_\_\_\_ solely by virtue of their placement, but rather retain their character as property of the Depositor along with any interest earned credited to the account(s) of Depositor. While the funds may be commingled to achieve investment management and other benefits, the Program will maintain its records in such a manner as to clearly delineate the actual ownership of the funds being held in trust.
- 10. ACKNOWLEDGEMENT** – By execution of this agreement you acknowledge that you are informed that monies deposited into the Program are commingled with funds of other Diocesan Parish, Schools or Agencies for investment purposes; that they may be loaned to eligible depositors at their request and with the approval of the diocesan bishop or his designee; and that these terms and conditions apply to current and future funds on deposit with the Program.
- 11. AMENDMENT** – The Program may amend terms of this agreement upon 30 days advance notice.

IN WITNESS WHEREOF, the parties have caused this agreement to be signed this \_\_\_\_\_ day of \_\_\_\_\_, 20\_\_\_\_\_.

DEPOSITOR

(NAME OF PROGRAM)

(NAME OF PARISH, SCHOOL OR AGENCY)

BY: \_\_\_\_\_

BY: \_\_\_\_\_

\_\_\_\_\_  
Name and Title

\_\_\_\_\_  
Name and Title

## **XII. Investments**

All institutions with investments should develop written investment policies governing significant investment criteria for each class of funds being invested. An Investment Committee is also a best practice. Among the matters which should be included in the investment policy are the following:

- Investment objective – a statement addressing the time horizon of the investment or fund, the use of sound investment practices that emphasize time horizon and the overall expectation of return on investment, and the acceptable level of risk.
- The Investment Committee:
  - Membership: number, term and qualifications of members and appointment authority.
  - Responsibilities:
    - to serve as faithful stewards in safeguarding the assets of the diocese
    - to serve as faithful stewards with respect to those assets deposited by participating institutions
    - recommend investment policy, guidelines, asset allocation to the diocese
    - to select and review the Investment Managers, Investment Consultant and Custodians for recommendations to the diocese
    - to recommend changes in the investment policy and fund design, and to implement the approved policy, and hold investment managers accountable
- Responsibilities of the Investment Managers – to manage the funds in a manner consistent with the investment objectives, guidelines and constraints outlined in the investment policy and in accordance with State and Federal law. This includes fiduciary responsibilities, security selection/asset allocation, and proxy voting.
- Responsibilities of the Investment Consultant: The Investment Committee may recommend the engagement of an independent investment consulting firm to assist them in the attainment of the Investment Fund’s objectives and monitor compliance with the stated investment policies. The Consultant’s responsibilities include assisting the Investment Committee with all aspects on the Investment Fund including establishing investment policies, asset allocation, manager selection (monitoring, reviewing, implementing, evaluating, etc.), preparing and presenting quarterly investment review reports, communicating investment policies and objectives to the managers, assisting with special tasks, and more.
- Responsibilities of the Board or Council: Explain the responsibilities of the Board or Council (if it is ultimately responsible for making the decisions that affect the Investment Fund’s Policy and Objectives). The Board or Council makes recommendations to the Diocese and must act as faithful stewards, prudently, avoid self-dealing and conflicts of interest, and for the best long-term interest of the Fund.
- Responsibilities of the Custodian: The custodians are responsible for the safekeeping of the assets. Their duties and responsibilities include all normal custodial functions

(security safekeeping, collection of income, settlement of trades, providing monthly reports detailing investment holdings and all transactions, establishing and maintaining an account(s) for Investment Managers, etc.) and preparing additional reports as requested.

- Socially responsible guidelines – guidelines for a socially responsible investment policy should be developed and implemented and should be modeled on the guidelines published on the website of the USCCB.

Matters that should be considered in preparing written investment policies include:

1. The purposes and the priorities for investing the funds,
2. Liquidity needs of the funds,
3. Risk Tolerance,
4. Asset Allocation,
5. Criteria for Investment Manager selection,
6. Spending need or Return objective of Fund,
7. Quality Minimums,
8. Benchmarks for each strategy,
9. Prohibited investments,
10. Investment style preferences,
11. Conflict of Interest statement, and
12. Regulatory requirements imposed by ERISA or any other applicable body.

Please see Foundations and Endowment Chapter references to UPMIFA Statutes. Institutions increasingly make use of alternative investments such as hedge funds, private equity funds, real estate funds, venture capital funds, etc. to increase both yield and diversification of investments. Prior to investing in such alternatives, institutions should recognize that these investments require more thorough due diligence, audit preparation and sometimes more administrative staff responsibility. Institutions should investigate if there will be problems with valuation, excessive risk, liquidity, taxation of unrelated business income, etc. They also should be aware that it may be difficult to determine if Social Responsibility guidelines are being observed by alternative investment funds.

The AICPA has published a Practice Aid entitled “Alternative Investments – Audit Considerations” that explores many of the issues with regard to alternative investments. It may also be a good idea to consult with outside auditors prior to utilizing alternative investment vehicles.

The Financial Accounting Standards Board (FASB) has issued pronouncements concerning fair value measurements that apply to accounting for investments. This guidance is contained in FASB Codification Section 820, *Fair Value Measurements and Disclosures*, and is effective for years beginning after November 15, 2008.

The Statement defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. Where applicable, the Statement simplifies and codifies related guidance within GAAP.

The Statement does not expand the use of fair value measurements but increases the consistency and comparability of fair value measurements. It retains the exchange price notion of fair value and clarifies that the exchange price is the price in an orderly transaction between market participants. The expanded disclosures focus on the inputs used to measure fair value and for recurring fair value measurements using significant unobservable inputs. To increase consistency and comparability in fair value measurements and relate disclosures, the Statement establishes a fair value hierarchy, which prioritizes into three broad levels the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable, either directly or indirectly. In 2015 Accounting Standards Update No. 2015-07, May 2015- Fair value Measurement, the following references the guidance, Investments valued using the practical expedient are categories within fair value hierarchy on a basis of whether the investment is redeemable at NAV or at NAV at a future date. See Subtopic 820-10-15-4 through 820-10-35-59 and 820-10-50-6A.

The Statement also encourages entities to combine the fair value information disclosed under the Statement with the fair value information disclosed under other accounting pronouncements.

## **XIII. Property and Equipment**

### **Recognition of Fixed Assets**

Fixed assets are property, plant, and equipment that typically consist of long-lived tangible assets that are not expected to be sold or consumed in less than one year. Common fixed assets include, but are not limited to: land, buildings, machinery (boilers, organs, etc.) and furniture and fixtures (desks, chairs, etc.). Every diocese should establish a fixed asset policy to determine which expenditures should be capitalized and which expenditures should be expensed. Capitalized fixed assets should be recorded to the balance sheet and depreciated throughout the expected useful life of the asset. Expenditures that are not capitalized should be recognized as an expense on the income statement during the period the expenditure is incurred.

The fixed asset policy should state a reasonable minimum amount for an expenditure to be classified as a fixed asset. For example, a fixed asset policy states that any equipment less than a specified dollar amount should be expensed. In this instance if the total cost to replace a boiler in a rectory is less than the minimum amount the diocese should expense the total cost. Conversely, if the replacement cost of the boiler was more than the minimum the boiler would be capitalized. The diocese should also note in the fixed asset policy that items purchased individually may fall below the minimum but exceed the minimum when purchased in aggregate. For example, a desk would fall below the minimum threshold. However, if the diocese purchased 75 desks at a certain price per unit at the same time the total expended would exceed the minimum and should be capitalized as a fixed asset. Care should be taken to write off any remaining book value on an asset that is replaced.

The fixed asset policy should address the difference between repairs & maintenance and capital improvements. Repairs and maintenance to existing structures or equipment should only be capitalized if the expenditure extends the expected useful life of the asset. For example, a repair to a small section of a church roof exceeds the minimum capitalization threshold but does not extend the useful life of the asset. In this instance, the repair should be expensed in the year in which the expenditure is incurred. Conversely, if a completely new roof is installed it would extend the useful life of the structure and the costs to replace the roof should be capitalized.

Depreciation is the recognition of the cost of the fixed asset on the income statement spread over the expected useful life of the asset. The diocese's fixed asset policy should establish a consistent, systematic depreciation methodology. For expediency, the fixed asset policy may state general guidelines for the expected useful life on equipment. Depreciation expense should be recorded opposite an "accumulated depreciation" contra account on the balance sheet. There are several types of depreciation methods that can be used by a diocese, but typically, not-for-profit organizations depreciate assets on a straight-line basis over its useful life. Straight line depreciation is calculated by the total acquisition cost of the asset, less salvage value, divided by the expected useful life. For example, the depreciation expense for a new vehicle purchased for \$5,000 with no expected salvage value and a 5-year expected useful life would be \$1,000 per year.

The diocese should start depreciation when the fixed asset is available and ready for use. This is particularly relevant for significant construction projects that may take several years. Costs related

to construction should be capitalized when incurred but not depreciated until the asset is available and ready to be used. The criterion to start depreciation, however, does not necessarily mean a project is fully completed. For example, construction of a new parish center has been ongoing for two years. The hall portion of the center is ready and available for use but the library and classroom portions are still under construction. In this instance the costs related to the construction of the hall should be depreciated in the current year. The costs incurred for the library and classroom portions of the building should be depreciated when those parts of the project are available and ready for use.

All fixed assets, except land and property held for sale, should be depreciated in accordance with the diocese's fixed asset policy. Property classified as held for sale should be recorded at the lower of its carrying amount or fair value less cost to sell (FASB Codification 360-10-55-43) and should only be classified as held for sale when the criteria outlined in FASB Codification 360-10-45-9 have been met.

Organizations that have not capitalized fixed assets previously should do so retroactively. If historical costs are not available for assets already in service, another reasonable basis can be used to value such assets. Other bases might be cost-based appraisals, insurance appraisals, replacement cost values, or property tax appraisals adjusted for market value. An alternative basis should be used only if historical cost information is unavailable and only to establish the initial value at the date of recording. Subsequent purchases should be recorded at cost and donated assets at market value.

Any fixed asset, purchased or donated, greater than or equal to the minimum capitalization amount, should be categorized as a fixed asset and depreciated over its useful life. If a purchased or donated fixed asset is less than the minimum amount, it should be expensed in the period obtained rather than capitalized.

### **Carrying Value of Fixed Assets**

Generally, fixed assets should be carried at the acquisition cost less accumulated depreciation. A diocese, however, is required to recognize an impairment loss if the carrying value of the fixed asset is no longer recoverable. For example, if a building is destroyed by a fire the diocese should write off the carrying value of the structure and record an impairment loss in the year in which the loss occurs in accordance with FASB Codification 605-40-25-3. If the diocese rebuilds the structure the costs incurred to do so should be capitalized.

Many dioceses purchase property in advance for future growth and development. Care should be taken periodically to review and inventory such properties to determine the future suitability for needs within the diocese. Property so purchased and held should be carried at cost value with any necessary adjustment for retirements as required by FASB Codification Subtopic 958-360. Consideration of the possibility of property taxes being charged to the diocese should be given to any unoccupied properties. Despite the tax-exempt status of the diocese some towns and municipalities may charge property taxes on unoccupied properties.

Property acquired by contribution should be carried at fair value at the date of contribution, in accordance with FASB Codification 958-605-25-2. Should the future use of the property change,



the continuing value of the property should be reviewed. Property held that no longer meets its original intended use should be written down to the lower of its cost or net realizable value. Likewise, facilities that are closed and no longer serve their intended purpose should be considered for proper valuation in accordance with FASB Codification Section 958-360-35 and Section 360-10-35.

### **Net Asset Classification**

Fixed assets may represent a significant dollar amount in the total assets of a diocese. These assets do not reflect the same liquidity and values as do other more current assets. To differentiate the relative values of net assets held by a diocese, consideration should be given to a separate net asset classification for fixed assets on the balance sheet. Within the category of unrestricted net assets (what might have been more commonly called “fund balances” in the past); “Net Investment in Property and Equipment” could be further designated. This further distinguishes the amount of net assets that may be less liquid in the financial statement of the diocese.

Not-for-profit organizations may receive contributions of long-lived assets (such as property and equipment) or of cash and other assets restricted to the purchase of long-lived assets, for which donors have not expressly stipulated how or for how long the long-lived asset must be used by the organization or how to use any proceeds resulting from the assets’ disposals. Although not required, an organization may adopt an accounting policy of implying time restrictions on the use of such contributed assets that expire over the assets’ expected useful lives. If an organization adopts such a policy, the contributions received should be reported as restricted support that increases temporarily restricted net assets. Depreciation should be recorded over the assets’ useful lives, and net assets should be reclassified from temporarily restricted to unrestricted when (a) the asset is placed in service or (b) as depreciation is recognized over the assets’ useful life.

Alternatively, organizations may adopt a policy of not implying time restrictions on contributions of long-lived assets (or of other assets restricted to the purchase of long-lived assets) received without donor stipulations about how long the contributed assets must be used. If an organization adopts such a policy, contributions of long-lived assets with no donor-imposed time restrictions should be reported as unrestricted support. Contributions of cash and other assets restricted to the acquisition of long-lived assets should be reported as restricted support that increases temporarily restricted net assets; those restrictions expire when the long-lived assets are placed in service by the organization. A diocese should refer to current tax law for guidance concerning holding periods for donated fixed assets to assure that the donor’s tax deduction for the gift is not jeopardized. A diocese should also refer to its gift acceptance policy with respect to donations of long-lived assets.

## Oversight of Fixed Assets

Property should be classified as to its use, and management responsibilities should likewise be classified by use. Property of parishes and schools should be placed under the oversight of the individuals in charge of such institutions, and the requirements of Canon 1283 §2 and 1283 §3 should be considered when there is a change in administrators. Canon 1283 §2 and 1283 §3 call for an inventory to be made as administrators begin their function and for a copy of the inventory to be preserved at the location and for a copy to be sent to the archives of the curia. Typically, a pastor or principal will oversee property maintenance at a related facility. Recognizing the specialized skills needed to care for fixed assets, they may rely on the support and assistance of committees and volunteers to help maintain, advise and coordinate these activities.

Careful consideration should be given to the development/improvement of existing real estate for future needs within the diocese. Improvements to land should be considered along with the long-term nature of these assets and their expected long-term use.

A number of procedures should be followed to carefully institute and exercise oversight and stewardship responsibilities for fixed asset holdings. The first procedure is a complete inventory of fixed assets. This inventory should include the following:

- A complete legal description of each real estate parcel and related buildings and improvements
- A description of buildings and improvements on each real estate parcel and a detailed picture or drawing of such
- A description of the use of the property
- A description of the form of ownership of the property
- A description of any mortgages or encumbrances related to the property
- An identification of each parcel's property manager, if applicable

Other procedures should be established to provide for the physical safeguard of assets from theft, vandalism, or unauthorized disposition.

Procedures likewise should be established to provide for the ongoing maintenance of facilities. Maintenance should consist of both daily and routine activities, while a plan should be established for long-term improvements, such as roof replacement and major maintenance. Institutional budgets should include a capital budget as well as an operational budget. The capital budget should consider necessary long-term repairs and improvements to the facilities to keep them safe and operational.

Procedures should be established to ensure that adequate insurance is maintained to minimize liability with respect to use of facilities. Insurance coverage should be reviewed on an annual basis. Periodic insurance appraisals should be obtained to ensure that property insurance coverage is adequate.

## **Alienation and Acts of Ordinary and Extraordinary Administration**

Certain acts relating to temporal goods are more significant than others and require a more elaborate system of authorization. The *Code of Canon Law* clearly distinguishes acts of *administration* (whether ordinary or extraordinary) from acts of *alienation* of property, whereby a juridic person divests itself of all or part of its stable patrimony.

To place acts of ordinary administration of greater importance, a diocesan bishop, for validity, must first hear the finance council and college of consultors. A diocesan bishop's acts of extraordinary administration, as defined by the USCCB, require, for validity, the consent of the finance council and college of consultors. No permissions from outside the diocese are required for acts of ordinary or extraordinary administration.

Canon 1277 reads as follows:

The diocesan bishop must hear the finance council and college of consultors to place acts of administration that are more important in light of the economic condition of the diocese. In addition to the cases specially expressed in universal law or the charter of a foundation, however, he needs the consent of the finance council and of the college of consultors to place acts of extraordinary administration. It is for the conference of bishops to define which acts are to be considered of extraordinary administration.<sup>1,3</sup>

To place acts of extraordinary administration, as defined in the statutes of public juridic persons other than the diocese, administrators require, for validity, the consent of the Ordinary (see c. 1281).

Canons 1291 and 1292 §1, 2 and 3 deal with the validity of acts of alienation. In cases involving alienation of stable patrimony, permission from the Holy See might be required, depending on the value of the property to be alienated.

Canon 1291 reads as follows:

The permission of the authority competent according to the norm of law is required for the valid alienation of goods which constitute by legitimate designation the stable patrimony of a public juridic person and whose value exceeds the sum defined by law.<sup>1</sup>

A commentary on alienation reads as follows:

Since alienation is the transfer of ownership, there is no alienation if no transfer of ownership takes place. Mortgaging property is not an act of alienation. A mortgage gives rise to rights in regard to property and creates the potential of a future loss of ownership in the event of default in payments on the loan for which the mortgage serves as collateral, but there is no immediate transfer of ownership and, hence, no alienation. The same is true of assuming a mortgage when purchasing property which already has a mortgage on it. Granting a right of way or an easement to come across or otherwise use one's land, since it does not involve a transfer of ownership, is not an act of alienation (if the easement also

includes the right to remove minerals, timber, or other natural resources from the land, then, of course, the easement would entail alienation of such resources).

Canon 1292 §1 reads as follows:

Without prejudice to the prescript of Can. 638 §3, when the value of the goods whose alienation is proposed falls within the minimum and maximum amounts to be defined by the conference of bishops for its own region, the competent authority is determined by the statutes of juridic persons if they are not subject to the diocesan bishop; otherwise, the competent authority is the diocesan bishop with the consent of the finance council, the college of consultors and those concerned. The diocesan bishop himself also needs their consent to alienate the goods of the diocese.<sup>1</sup>

In March 2010, the United States Conference of Catholic Bishops promulgated the proscribed amounts in accord with Canon 1292 §1 (**Updated May 2011**):

The maximum limit for alienation and any transaction which, according to the norm of law, can worsen the patrimonial condition is \$7,500,000 for dioceses with Catholic populations of half a million persons or more. For other dioceses, the maximum limit is \$3,500,000 (cf. can. 1295).<sup>1</sup>

1. The minimum limit for alienation and any transaction that, according to the norm of law, can worsen the patrimonial condition is \$750,000 for dioceses with Catholic populations of half a million persons or more. For other dioceses, the minimum limit is \$250,000.<sup>1</sup>
2. For the alienation of property of other public juridic persons subject to the diocesan bishop, the maximum limit is \$3,500,000 and the minimum limit is \$25,000 or 10% of the prior year's ordinary annual income, whichever is higher.<sup>1</sup>

An accompanying memorandum from the USCCB President notes that “the approved sums are modestly lower than those that [were previously] in force. They are also no longer subject to an annual adjustment according to the Consumer Price Index.”

There have been further updates since December 1, 2011 to the proscribed amounts promulgated by the USCCB for Canon 1292 §1. Canon 1292 §2 and §3 read as follows:

The permission of the Holy See is also required for the valid alienation of goods whose value exceeds the maximum amount, goods given to the Church by vow, or goods precious for artistic or historical reasons (c. 1292 §2).<sup>1</sup>

If the asset to be alienated is divisible, the parts already alienated must be mentioned when seeking permission for the alienation; otherwise, the permission is invalid (c. 1292 §3).<sup>1</sup> Canons 1292 §4, 1293, and 1294 prescribe conditions for the liceity of acts of alienation as follows:

Those who by advice or consent must take part in alienating goods are not to offer advice or consent unless they have first been thoroughly informed both of the economic state of the juridic person whose goods are proposed for alienation and of previous alienations (c. 1292 §4).<sup>1</sup>

The alienation of goods whose value exceeds the defined minimum amount also requires the following:

- 1° A just cause, such as urgent necessity, evident advantage, piety, charity, or some other grave pastoral reason (c. 1293 §1).<sup>1</sup>
- 2° A written appraisal by experts of the asset to be alienated (c. 1293 §1).<sup>1</sup>

Other precautions prescribed by legitimate authority are also to be observed to avoid harm to the church (c. 1293 §2).<sup>1</sup>

An asset ordinarily must not be alienated for a price less than that indicated in the appraisal (c. 1294 §1).<sup>1</sup>

The money received from the alienation is either to be invested carefully for the advantage of the church or to be expended prudently according to the purposes of the alienation (c. 1294 §2).<sup>1</sup>

As a result of Canon 1295, the procedures for alienation must be applied not only to transactions where the stable patrimony of a public juridic person is alienated, but also to those transactions where the overall economic condition of a public juridic person is jeopardized or placed at risk.

The application of Canon 1295 is contingent on the level of risk and on the economic condition of the public juridic person. The Canon deals with such matters as the transfer of rights such as easements, mortgages, liens, and options as well as with incurring debt, including guarantees, surety and gift annuities, and the making of unsecured loans. The Canon encompasses accepting an obligation, giving up a right, assuming a debt, or being responsible for the liability of another.

For a greater discussion of alienation and ordinary and extraordinary acts of administration, suggested reading includes *The New Commentary on the Code of Canon Law* and the *Church Finance Handbook* (Kevin E. McKenna, Lawrence A. DiNardo, and Joseph W. Pokusa; Washington, D.C.: Canon Law Society of America, 1999).

## **Leasing**

Canon 1297, in part, reads as follows:

Attentive to local circumstances, it is for the conference of bishops to establish norms for the leasing of Church goods, especially regarding permission to be obtained from the competent ecclesiastical authority (c. 1297).<sup>1</sup>

Effective August 15, 2007, the following USCCB Complementary Norms for Canon 1297 became effective:

1. Prior to leasing of ecclesiastical goods owned by a diocese, the diocesan bishop must hear the finance council and the college of consultors, when the market value of the goods to be leased exceeds \$400,000.

2. Prior to leasing of ecclesiastical goods owned by a diocese, the diocesan bishop must obtain the consent of the finance council and the college of consultors when the market value of the property to be leased exceeds \$1,000,000 or the lease is to be for three years or longer.
3. The valid leasing of ecclesiastical goods owned by a parish or other public juridic person subject to the governance of the diocesan bishop requires consent of the diocesan bishop when the market value of the goods to be leased exceeds \$100,000 or the lease is to be for one year or longer.
4. The valid leasing of ecclesiastical goods owned by a pontifical institute of consecrated life or society of apostolic life requires, in addition to the consent of the competent major superior and council, the *nihil obstat* of the diocesan bishop when the market value of the property to be leased exceeds \$1,000,000 or the lease is to be for three years or longer.
5. The valid leasing of ecclesiastical goods by any public juridic person requires the consent of the Holy See when the market value of the goods exceeds \$5,000,000.

### **Guidance and Suggestions Concerning Canon 1297**

Key Concept – Canon 1297 applies when a diocese, a parish or any other qualifying entity within the territory of the diocese is the lessor, i.e. they lease their property to another entity. Accordingly, this decree does apply to situations when a diocese, parish or other qualifying entity enters into a lease transaction whereby they are the lease.

- I. Determination of which entities within the diocese that Canon 1297 applies to is important.
  - a. Parishes and other public juridic persons (norms 1, 2, 3 and 5).
  - b. Pontifical Institutes of Consecrated Life or Society of Apostolic Life (norm 4).
- II. Market value should be established by obtaining a qualified appraisal of the property to be leased.
  - a. Various commentaries addressing the implementation of Canon 1297 have suggested that market value can be obtained by:
    - i. Obtaining the tax value of the property adjusted if the tax value is based on a percentage of the actual market value, or
    - ii. The depreciated value of the property as given in the latest financial audit. The APC does not recommend these approaches. Consideration will need to be given for special situations, including:
      1. Leases may involve only a portion of a facility creating valuation difficulties.
      2. Leases may include both real and personal property (artworks, etc.) requiring additional appraisal experts.
- III. Suggested Guidance for Diocesan Finance Officers:

- a. Implementation of Canon 1297 should be done in close collaboration with Judicial Vicar or Canonist of the diocese.
- b. Create a list of those “qualifying entities” within the territory of the diocese. Utilizing the Official Catholic Directory listing or other sources, determine what entities are:
  - i. Parishes and other public juridic persons
  - ii. Pontifical Institutes of Consecrated Life
  - iii. Societies of Apostolic Life
- c. Update the particular norms/laws and/or guidance of the local diocese to address requirements of Canon 1297. While each diocese sets forth its own particular law in varying manners (e.g. policy and procedures manuals), such policies include the parishes and other juridic persons within the territory of each diocese.
- d. Consideration should be given to establishing materiality levels for Canon 1297 when obtaining fair value appraisals. For example, how many “expert opinions” are needed and what, if any, are the requirements for such “experts” (e.g. for transactions <\$100,000, between \$100,000 and \$5,000,000 and >\$5,000,000.
- e. In addition, each diocese must determine what constitutes a lease. For instance, it is doubtful that a parish making a facility available for wedding receptions or other Catholic group meetings falls under those norms. In these situations, a license agreement with proper insurance coverage is most appropriate.
- f. Prepare a diocesan notification letter to be sent to the administrator of those qualifying entities to notify them of the required norms of Canon 1297 and how these norms will be implemented as particular law of the diocese.

## Notes

- <sup>1</sup> All Canon Law quotes in this section are taken from the *Code of Canon Law* Latin-English Edition (Washington, D.C.: Canon Law Society of America, 1998).
- <sup>2</sup> R.T. Kennedy, “Book V: The Temporal Goods of the Church (cc. 1254-1310),” in John P. Beal, James A. Coriden and Thomas J. Green, eds., *New Commentary on the Code of Canon Law* (Mahwah, N.J.: Paulist Press, 2000), 1493-1494.
- <sup>3</sup> The USCCB has fulfilled this obligation through complementary legislation for the implementation of Canon 1277 of the Code of Canon Law for the dioceses of the United States, effective as of April 5, 2010. The complementary norm can be found on the USCCB website at <http://www.usccb.org/beliefs-and-teachings/what-we-believe/canon-law/complementary-norms/canon-1277-acts-of-extraordinary-administration-by-diocesan-bishop.cfm>

## **XIV. Cemeteries and Columbariums**

Many dioceses operate cemeteries and columbariums. These may be separate not-for-profit corporations, or they may be divisions operating within the central administrative offices. The accounting for these operations is the same regardless of the entity structure.

Generally accepted accounting principles for diocesan cemeteries are generally included in the Codification as it relates to various assets, liabilities, revenues and expenses. Accounting policies and disclosures in the following areas may be unique to cemeteries and columbariums:

- Provision of perpetual care and maintenance
  - i. Liability for future care costs
  - ii. Net asset classification
- Revenue recognition policies for deferred service contracts
- Rights of return
- Recognizing the costs of developed space as those spaces are sold
- Installment sales contracts

In addition, state and local laws and regulations do vary significantly and these variations can have a significant impact on the items discussed below. Dioceses should have discussions with their auditors and legal counsel.

### **Provision of Perpetual Care and Maintenance**

Typically, cemeteries and columbariums maintain the property and facilities associated with the operations of the cemetery or columbarium in perpetuity. The annual operating costs can be substantial and when projected into perpetuity, in most instances, can be material to not only the cemeteries but also to the diocese that oversees their operations.

From a canonical perspective there is no explicit obligation on the part of the operators of the cemeteries and columbariums to ensure perpetual maintenance. However, given the fact that cemeteries and columbariums are sacred grounds for the burial of the dead, they should be cared for with dignity, thus implying a moral obligation to maintain cemeteries. As a result, contractual terms vary greatly from one diocese to another but generally call for some commitment by the cemeteries to maintain properties as cemeteries. In addition, state and local laws vary. In some cases, state law may require that operating cemeteries and columbariums are required to deposit a portion of new sales proceeds into a state-run or state-supervised fund set up to provide for perpetual care. Other regulations require the establishment of segregated or set-aside net assets in separate bank accounts but maintained on the statement of financial position of the cemeteries and columbariums. Finally, some state statutes specifically exclude religious cemeteries and columbariums from these requirements all together. A brief legal description of maintenance funds can be found here:

<http://cemeteries.uslegal.com/cemetery-maintenance/maintenance-funds/>



The accounting treatment for the perpetual care and maintenance of cemeteries and columbariums is dependent on the applicability of a number of the above factors. A careful and detailed review of the contractual terms and the state and local laws in each jurisdiction should be undertaken with the assistance of the operator's attorneys and accountants in arriving at the appropriate accounting treatment. Most contracts would be governed by state law and the contractual terms should be reviewed periodically to ensure a continued appropriate understanding and accounting of the contractual terms. In some instances, a conclusion may be reached that supports the recording of an actuarially calculated liability projection to properly reflect a specific obligation to provide perpetual care and maintenance. In other instances, the review may lead to the conclusion that amounts set aside should be recorded as unrestricted assets held for limited use.

An essential step is determining whether the existing factors (contractual terms, state and local laws and regulations, published intent, etc.) support recording a liability. A conclusion that a liability exists would result in future maintenance costs (discounted at an appropriate discount rate) being recorded as sales occur.

Readers may want to review the discussion paper prepared in 2013 by the Accounting Practices Committee: *Grant Thornton's Whitepaper: Managing Cemetery Perpetual Care Obligations within Your Diocese* at:

[http://www.gallagherpost.com/gallagher\\_post/docs/Grant%20Thornton%20--%20Managing%20cemetery%20perpetual%20care%20obligations%20within%20your%20diocese%202013.pdf](http://www.gallagherpost.com/gallagher_post/docs/Grant%20Thornton%20--%20Managing%20cemetery%20perpetual%20care%20obligations%20within%20your%20diocese%202013.pdf)

## **Net Asset Classifications**

Under ASU Topic 958, the balance sheet financial presentation of net asset reporting will be streamlined and clarified. The existing three-category classification of net assets (i.e., unrestricted, temporarily restricted, and permanently restricted) will be replaced by combining temporarily restricted and permanently restricted into a single category called "net assets with donor restrictions." Differences in the nature of donor restrictions will be disclosed in the notes, with an emphasis on how and when the resources can be used. The guidance for classifying deficiencies in endowment funds ("underwater endowments") and on accounting for the lapsing of restrictions on gifts to acquire property, plant, and equipment have also been simplified and clarified.

The net assets of cemeteries and columbariums are typically classified in the financial statements as unrestricted, as the revenues generally originate from exchange transactions. As discussed above, some cemeteries and columbariums designate a portion of unrestricted net assets for permanent maintenance and future development. Some operate in accordance with state laws that require a set-aside of sales contracts for permanent maintenance funds and for future development funds. Such laws may require that the principal shall remain inviolate thus disclosing that fact would be made in the footnotes. The net assets that previously fell under the following categories:

- Unrestricted – operating (includes net assets invested in land, building and equipment)
- Unrestricted – designated for future development or for future maintenance
- Unrestricted – assets held for limited use

- Temporarily restricted – donor-imposed
- Permanently restricted – donor-imposed restrictions (such as trust funds) would be shown as net assets without donor-restriction or net assets with donor restrictions.

### **Net Assets Without Donor-Restriction**

Previously used terminology noted below would be classified as net assets without donor-restriction.

*Undesignated unrestricted net assets.* These represent general operations of the cemeteries.

*Unrestricted designated for future development or future maintenance.* Some cemeteries internally designate a portion of the unrestricted net assets for future development or future maintenance. These designations should be formally made by the appropriate governing persons or groups. These designated net assets are to be held by the cemeteries and are to be used solely for development and maintenance of cemetery grounds. Such designations may be re-designated by the cemeteries because they do not represent funds restricted by a donor. Other designations may be contractually stipulated.

*Unrestricted assets held for limited use.* States may have a requirement that a portion of the sales for lots, crypts, and niches be set aside for permanent maintenance funds. In some cases, the principal is to remain inviolate. If after review of state and local laws and the contractual terms the organization concludes that amounts set aside should be recorded as net assets, these should be recorded as unrestricted assets held for limited use.

### **Net Assets with Donor Restriction**

*Temporarily restricted.* In the event a contribution, independent of a burial contract, is made to the cemetery that is restricted by time or purpose, the unexpended portion is presented as temporarily restricted. Expenses may be incurred for purposes for which both unrestricted and temporarily restricted net assets are available. If such an expense is incurred, the temporarily restricted net assets are used first unless the expense is for a purpose that is directly attributable to another specific external source of revenue.

*Permanently restricted.* If a contribution is made to the cemetery which stipulates that the principal cannot be used and only the earnings thereon are to provide special care or adornments (i.e. flags, wreaths, etc.) or perpetual maintenance for all or any portion of the entire cemetery grounds, then these funds are permanently restricted. The earnings on the funds used to provide this required special care or adornments are treated as current revenue. Any unused earnings would be treated as temporarily restricted until the required special care or adornments are provided. Please refer to ASU 2016-14: *Presentation of Financial Statements of Not-for-Profit Entities*, which was issued on August 18, 2016. It is effective for annual financial statements issued for fiscal years beginning after December 15, 2017. This new standard eliminates the distinction of Temporarily and Permanently Restricted Assets and classifies assets as Without Donor Restriction and With Donor Restrictions. This new standard also requires additional disclosures including the amount, purpose and type of board designations. It also requires disclosure of the composition

(nature and amount) of donor restrictions at year-end, addressing how and when resources can be used. This new Standard will apply to fiscal year 2018-2019 for most dioceses.

### **Revenue Recognition for Deferred Service Contracts**

Typically, revenue is recognized upon the execution of a contract at the time a contract is signed. Some sales contracts provide for the option to prepay burial or other service fees. Such prepayments are reflected as deferred revenues and are recognized as revenue when the burial or other service is performed.

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers which will provide authoritative guidance to change the criteria for revenue recognition. The core principle of the new standard is that revenue should be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, several new revenue recognition disclosures will be required. This guidance is effective for reporting periods beginning after December 15, 2018.

### **Rights of Return**

Some cemeteries have sales contracts that provide for the right of return for a definite period. A provision for cancellation of those sales contracts written in prior years is recorded in the financial statements based upon historical expense.

### **Amortization of Developed Space**

Inventory of developed space should be recorded at historical cost. The cost of each space is based on an allocation of total expenses incurred in developing the burial space. The cost of the space is computed on a basis of the cost of each space sold and is recorded as cost of sales at the time of sale.

### **Installment Sales Contracts**

Some cemeteries allow customers to purchase contracts on the installment method. A provision for interest in accordance with Codification 835 needs to be considered if the interest rate is below market.

If preneed contracts are sold, there could be state requirements to segregate some or all of the funds collected in a trust. The accounting and reporting can be significant based on contractual and cancellation terms.

## **XV. Group Programs**

Most dioceses and their affiliated entities establish group programs to administer financial activities of common interest and need. These activities have also been referred to as “Service Funds.” The two most common examples are Benefit Plans and Property/Liability/Casualty

Insurance Plans that include all of the affiliated ministry entities of the diocese and their employees. These Programs are usually administered by or at the Central Administrative Offices of the Diocese.

The following are general matters that must be considered in administering the financial activities of the Programs:

1. Legal Structure of the Program – Programs operate within the legal structure of the diocese or through separate corporations, trusts or other legal entities established to manage the activities of the Programs.
2. The Governing Body of the Program – Separate governing bodies for these Programs may be established with varying degrees of accountability to the Ordinary, in accordance with Canon Law.
3. Federal, State and Local Regulation – Federal, State and Local laws and regulations applicable to these Programs must be considered. Legal Counsel should be consulted in these matters.

The following are major financial administration matters pertinent to these Programs:

1. These Programs should be accounted for as separate “funds” in accordance with not-for-profit accounting principles, distinct from the other operating activities of the diocese.
2. Generally Accepted Accounting Principles in the United States (GAAP) should be followed in accounting for and reporting on the activities of these Programs. Generally accepted industry accounting and reporting standards (i.e. Insurance industry) should also be considered and applied as needed.
3. The main sources of revenue to these Programs should be contributions and premiums paid by the participating entities. Similarly, the benefits, claims or other expenses of the Programs should be on behalf of, or for benefit of the same entities.
4. The financial activities of these Programs are reported as Unrestricted activities. In individual financial reports prepared in accordance with GAAP, the Net Assets of the Programs could be reported as Unrestricted. When these Programs’ accounts are included in Combined or Consolidated reports of a larger entity, the Net Assets of the Program should be reported as Unrestricted, Designated funds.
5. As with all designated funds, the Governing Body of the Program may change its Net Asset Designations from time-to-time based upon the financial needs and plans of the Program. With insurance funds, an example would be the need to carry sufficient reserves for self-insured claims (a liability).

6. ASU 2013-6 requires a recipient not-for-profit entity to recognize all services received from personnel of an affiliate that directly benefit the recipient not-for-profit entity. Those services should be measured at the cost recognized by the affiliate for the personnel providing those services. Under certain circumstances, these provisions may apply to Group Programs.

## **XVI. National Special Collections**

### **Canon Law**

Canon 1266 of the revised *Code of Canon Law* states:

In all churches and oratories which are, in fact, habitually open to the Christian faithful, including those which belong to religious institutes, the local ordinary can order the taking up of a special collection for specific parochial, diocesan, national, or universal projects; this collection must be diligently sent afterwards to the diocesan curia.<sup>1</sup>

The *New Commentary on the Code of Canon Law* explains this further:

The collection must be for a specific, not indeterminate, undertaking, but it need not be diocesan; it can be parochial (i.e. aid to a poor or struggling parish) or national or international. Nor does the undertaking or project which is the object of a mandated collection have to rise to the level of a need or necessity, as in the case of a tax (see Canon 1263), suggesting that the motivating causes for collections can be less urgent than those for taxes.

The final clause in Canon 1266 requires that the proceeds of a mandated collection be sent diligently (*sedulo*) to the diocesan curia. The import of the adverb is twofold: that the proceeds are sent without delay and in their entirety. All proceeds should be remitted within five (5) months of the collection date. Unless contributors have been so informed in advance, no part of the proceeds may be withheld at the parish or any other level; not to turn over the entirety of the collection immediately is to violate the intentions of the donors. In addition, as such withholding becomes known, it seriously compromises the perceived integrity of fundraising in the Church.<sup>2</sup>

### **Collections**

The United States Conference of Catholic Bishops administers nine (9) national collections. These collections are submitted using USCCB transmittal forms:

- Church in Latin America
- Aid to the Church in Central and Eastern Europe
- Catholic Relief Services (formerly the American Bishops' Overseas Appeal)
- Catholic Home Missions Appeal
- Catholic Communication Campaign (50% retained in local diocese)
- Peter's Pence
- Catholic Campaign for Human Development (25% retained in local diocese)
- Retirement Fund for Religious
- Church in Africa

Other collections that do not use USCCB transmittal forms include the following:

- Black and Indian Missions
- CRS Rice Bowl
- The Catholic University of America
- Good Friday Collection for the Holy Land
- Peter’s Pence (Charities of the Holy Father)
- World Mission Sunday
- Archdiocese for the Military (every three years)

## Accounting Treatment

Special collections are free-will offerings of the faithful with no mandatory quota placed on a parish or a diocese. To do so would transform a collection into a tax (Canon 1263). A tax would be revenue and accounted for accordingly. Paragraph 3, Canon 1267 states, “Offerings given by the faithful for a certain purpose can be applied only for that same purpose.”

Accounting for special collections is primarily set forth in the FASB’s Accounting Standards Codification Topic #958 – Not for Profit Entities and, its related sub-topic 605 – Revenue Recognition.

Special collection proceeds that are not retained by a diocese should be accounted for as an agency transaction (liability) by the diocese, unless the diocese has been granted the power by the donors to determine the beneficiaries (“variance power”). To the extent a diocese has variance power, that portion should be accounted for as temporarily restricted revenue and temporarily restricted net assets until the funds are remitted to the beneficiaries chosen by the diocese.

Where donors have been so informed, portions of certain collections are permitted to be retained by a diocese and used by the diocese. Those funds are classified as a temporarily restricted revenue and net asset until they are used for the same intent as a portion transmitted nationally or internationally. The donor provided the offering for a particular purpose; therefore, there is a donor restriction on the retained portion, causing the revenue to be temporarily restricted.

The USCCB has issued specific guidelines, *One Church, One Mission: Guidelines for Administering USCCB National Collections in Dioceses.*

For further information, please refer to the following websites:

- *One Church, One Mission: Guidelines for Administering USCCB National Collections in Dioceses:* <http://www.usccb.org/about/national-collections/collection-administration/upload/one-church-one-mission-guidelines-national-collections.pdf>
- National Collection Schedule: <http://www.usccb.org/about/national-collections/upload/2019-2020-Collections-Schedule.pdf>
- National Collection Dates: [http://www.usccb.org/about/national-collections/collection-administration/upload/2018\\_2019\\_2020\\_collxndates.pdf](http://www.usccb.org/about/national-collections/collection-administration/upload/2018_2019_2020_collxndates.pdf)
- National Collections Transmittal Forms and Electronic Remittance: <http://www.usccb.org/about/national-collections/collection-administration/index.cfm>

## Notes

- <sup>1</sup> *Code of Canon Law: Latin-English Edition, New English Translation* (Washington, D.C.: Canon Law Society of America, 1999).
- <sup>2</sup> R.T. Kennedy, “Book V: The Temporal Goods of the Church (cc. 1254-1310),” in John P. Beal, James A. Coriden, and Thomas J. Green, eds., *New Commentary on the Code of Canon Law* (Mahwah, N.J.: Paulist Press, 2000), 1468-1469.



## **XVII. Federal Funding**

### **General**

The past several decades have seen huge increases in federal awards to state and local governments and non-profit organizations. Many of these federal awards are of a social service nature and have been granted to church-related organizations interested in meeting the needs of the underprivileged in this country (e.g. foster care grants to Catholic Charities). As the amounts awarded to governmental units and non-profit organizations have increased, so have the attempts to ensure that such funds are spent as intended and that such funds are not subject to fraud, waste, and abuse. Additionally, the terms of federal awards are becoming more restrictive with regard to the religious character that may be involved with the use of those funds. Care should be taken to safeguard the free exercise of our Catholic faith. Failure to spend funds in accordance with grant terms can result in disallowed costs or permanent loss of funding.

In December 2013, the Office of Management and Budget (OMB) issued the Uniform Guidance, which establishes uniform cost principles and audit requirements for federal awards to nonfederal entities and administrative requirements for all federal grants and cooperative agreements. Once the administrative requirements and cost principles of the Uniform Guidance are effective for all federal awards to nonfederal entities, the previous OMB guidance and requirements related to administrative requirements and cost principles will be superseded.

The Uniform Guidance states that nonfederal entities that expend \$750,000 or more of federal awards in a fiscal year must have a single or program-specific audit.

In accordance with the *AICPA Government Auditing Standards and Single Audits – Audit Guide*, “the Single Audit should cover the entire operations of the auditee, or at the option of the auditee, the audit may include a series of audits that cover departments, agencies and other organizational units that expended or otherwise administered federal awards during the fiscal year, provided that each audit encompasses the financial statements and schedule of expenditures of federal awards for each such department, agency and organizational unit which must be considered to be a nonfederal entity. The financial statements and schedule of expenditures of federal awards must be for the same audit period.”

In defining the entity to be audited, the *AICPA Government Auditing Standards and Single Audits – Audit Guide* states, “One of the initial tasks during the planning process of a single audit is determining whether management has properly defined the entity to be audited. The Uniform Guidance states that the audit must cover the entire operations of the auditee, or, at the option of the auditee, such audit must include a series of audits that cover an auditee’s departments, agencies, and other organizational units that expended or otherwise administered federal awards during the audit period. If an auditee elects this option, each audit must encompass the financial statements and the schedule of expenditures of federal awards for each such department, agency, or other organizational unit, which must be considered a nonfederal entity. The financial statements and schedule of expenditures of federal awards must be for the same audit period. In these circumstances, the nonfederal entity-wide financial statements may also include the departments,

agencies, or other organizational units that have separate audits and prepare separate financial statements.

Recipients of federal funds subject to Uniform Guidance include non-profit organizations such as colleges and universities, museums, libraries, and health and welfare agencies. These entities operate in an environment that often has two specific attributes:

1. These organizations often carry out the programs legislated by Congress. To do that, they receive federal grants and contracts that include certain terms and conditions that must be met. Administrative rules and cost principles, as well as specific statutory requirements, dictate the responsibilities imposed by the receipt of federal funds. A considerable amount of federal government guidance on audits of these organizations deals with the receipt and expenditure of such awards.
2. These organizations generally have tax-exempt status under applicable provisions of the Internal Revenue Code. As a condition of receiving tax-exempt status, many of these non-profit organizations agree to limit or handle in accordance with federal regulations certain activities (e.g. lobbying, operating a business that is not related to the exempt purpose, etc.).

### **Responsibilities of the Receiving Organization**

By accepting donations from individuals or organizations that have attached restrictions to the donation, an organization incurs a legal and moral obligation to adhere to the restrictions imposed by the donor. The clear alternative is not to accept the donations. Federal awards are no different in this respect. The receipt of federal funds in any form as explained below implicitly acknowledges acceptance of grant-imposed responsibilities. Ignoring or inadequately adhering to these requirements may cause the federal agency to refuse further funding or even require the return of the federal funds granted.

It should be noted that non-profit organizations may receive federal funds directly (i.e. from the federal government) or indirectly (i.e. the funds may be passed through from state or local governments or other non-profit organizations). Even if the funds are received indirectly, the organization is still subject to Uniform Guidance requirements.

### **Data Collection Form**

The Uniform Guidance states that the auditee must submit a data collection form (Form SF-SAC) that states whether the audit was completed in accordance with the Uniform Guidance and provides information about the auditee, its federal programs, and the results of the audit. The data collection form must include information available from the audit that is necessary for federal agencies to use the audit to ensure integrity for federal programs. This form is not an element of the reporting package; instead, the required information on the form represents a summary of the information contained in the reporting package.

The auditee completes the data collection form online (through the FAC website at <https://harvester.census.gov/facweb/>) and electronically certifies it (via an online signature) upon submission. The auditee certification statement must be signed by a senior level representative of

the auditee (for instance, state controller, director of finance, chief executive officer, or chief financial officer) and indicate, at a minimum, that (1) the auditee complied with applicable requirements; (2) the data were prepared in accordance with the requirements (and the instructions accompanying the form); (3) the reporting package does not include protected PII; (4) all information is included and it is accurate and complete.

### **Defining Federal Awards**

Federal awards include not only cash but also other types of assistance. There are fifteen types of assistance, of which eight are the most prevalent:

- Formula grants
- Project grants
- Direct payments for specified use
- Direct payments with unrestricted use
- Direct loans
- Guaranteed or insured loans
- Insurance
- Sale, exchange, or donation of property and goods

### **Compliance with Laws and Regulations**

An exhaustive analysis of the requirements imposed on an organization receiving federal funds is beyond the scope of this section. What follows is general background information on the kinds of requirements to which an organization may subject itself, as well as some direction for how to determine conclusively what the organization must do to meet those requirements. These compliance requirements subject to audit testing are found in the *OMB Compliance Supplement*.

- a. ***Activities allowed or unallowed.*** Requires that the types of goods or services purchased with federal awards be specified as allowable under program requirements.
- b. ***Allowable costs/cost principles.*** Prescribe direct and indirect costs allowable as costs of federally funded programs (these are further described in various OMB circulars; generally, the one impacting not for profits is OMB Circular A-122).
- c. ***Cash management.*** Requires recipients to have procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury and disbursement by the recipient.
- d. ***Reserved.***
- e. ***Eligibility.*** Specifies the criteria for determining the individuals, groups of individuals, or sub-recipients that can participate in the program and the amounts for which they qualify.

- f. ***Equipment and real property management.*** Requires organizations to maintain an equipment and property management system for its federal award programs and related activities in accordance with certain federal standards.
- g. ***Matching, level of effort, earmarking.*** Requires that an organization receiving federal awards contribute its own resources to programs funded in some specified ratio to resources provided by the funding source.
- h. ***Period of performance.*** Requires – where a funding period is specified – that a recipient charge to the grant only allowable costs resulting from obligations incurred during the funding period and any pre-award costs or carryover balances authorized by the federal awarding agency and the applicable cost circular.
- i. ***Procurement and suspension and debarment.*** Requires the following:
  1. That recipients establish procedures for the procurement of supplies and other expendable property, equipment, real property, and other services with federal funds to ensure that such materials and services are obtained in an effective manner and in compliance with the provisions of applicable federal statutes and executive orders.
  2. That contracts not be made to parties that are suspended or debarred or whose principals are suspended or debarred.
- j. ***Program income.*** Requires that gross income received which is directly generated by the federally-funded project during the grant period be retained by the recipient and used in accordance with federal awarding agency regulations or the terms and conditions of the award.
- k. ***Reserved.***
- l. ***Reporting.*** Requires that specific reports be filed and stipulates additional requirements that apply to those reports.
- m. ***Sub-recipient monitoring.*** Requires federal award recipients (pass-through entities) to have adequate monitoring and follow-up that covers entities to which they have in turn awarded federal funds.
- n. ***Special tests and provisions.*** Includes other provisions for which federal agencies have determined that noncompliance could have a direct and material effect on the program.

Not all of the compliance requirements necessarily apply to a given program. To determine which requirements do apply, the grant agreement, United States Statutes, the United States Code of Federal Regulations (CFR), the Uniform Guidance Compliance Supplement and the Catalog of Federal Domestic Assistance are sources that may be consulted.

The first place to look for these requirements is the grant document itself. Because all of these requirements are imposed by contract (as opposed to being a matter of law), all should be incorporated into the grant or contract either directly or by reference – so read the document first. Also, many grants or contracts, although quite brief, will refer to standard attachments that are incorporated by reference into every grant issued by a given agency.

OMB has issued a number of circulars that may be incorporated completely or partially by reference in grants or contracts. Circulars from the OMB can be found at <https://www.whitehouse.gov/omb/offices/offm>. Some of the more important circulars are as follows:

- A-110 – *Uniform Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Nonprofit Institutions*
- A-21 – *Cost Principles for Educational Institutions*
- A-122 – *Cost Principles for Nonprofit Organizations*

The first circular, A-110, includes many of the administrative requirements pertaining to federally funded programs. The last two – A-21 and A-122 – establish the principles to be used in determining the costs of grants and contracts, including the basic principles of allowable and unallowable costs and the mechanics involved in establishing indirect cost rates.

Federal sponsors want to ensure that the limited financial assistance is spent appropriately by non-profit organizations. Over the past few years, the federal government has continued to change promulgated cost principles to stop perceived abuses by recipients of federal funds. In many instances, these changes have simply reduced the recipients' ability to recover the cost of the program or research. While in the past the government was committed to full cost recovery by recipients of federal funds, the introduction of limitations on the amount of costs recovered has forced more organizations to increase their internal contributions to the programs.

### **Related Regulatory and Professional Literature**

Many of the publications referred to in this chapter are available on the internet.

## **XVIII. Foundations and Endowments**

Most dioceses have fundraising and investment functions. These may be legally separate not-for-profit corporations (“foundations”) or may be divisions operating within the Central Administrative Offices (CAO). The receipts of restricted gifts, including endowments, require specific accounting treatment.

### **Foundations**

Please refer to FASB Codification Subtopic 958-20, Financially Interrelated Entities. In many cases a foundation may require consolidation, as discussed in Subtopic 958-810 of the Codification.

Classification of a beneficiary’s interest in the net assets of a financially interrelated fundraising foundation in the beneficiary’s financial statements also is discussed in the AICPA’s Technical Practice Aids Section 6140.13 to 6140.18.

### **Endowments**

Financial reporting standards for the presentation and classification of net assets, including unrestricted and restricted endowment funds, generally are included in FASB Codification Sections 958-210-45 and 958-205-45. For a more thorough discussion of accounting for investment, please refer to Chapter XII Investments. Also, Chapter 4 of the AICPA Audit & Accounting Guide for Not-for-Profit Entities has an in-depth discussion of accounting for investments.

The model Uniform Prudent Management of Institutional Funds Act (UPMIFA) was approved by the Uniform Law Commission in July 2006 to modernize the Uniform Management of Institutional Funds Act of 1972 (UMIFA) for governing the investment and management of donor-restricted endowment funds by not-for-profit organizations. State legislatures may enact UPMIFA as written or a modified version of it, and they may issue supplementary guidance that affects the accounting for endowment funds. Classification of Donor Restricted Endowment Funds Subject to UPMIFA is discussed in Paragraphs 958-205-45-28 through 32 of the Codification. Classification of Donor Restricted Endowment Funds Subject to Trust Law or to UPMIFA is discussed in Paragraphs 958-205-45-33 through 958-205-45-35 of the Codification.

Information on the Uniform Prudent Management of Institutional Funds Act of 2006 is available at:

<http://www.uniformlaws.org/LegislativeFactSheet.aspx?title=Prudent%20Management%20of%20Institutional%20Funds%20Act>

[http://www.uniformlaws.org/shared/docs/prudent%20mgt%20of%20institutional%20funds/upmifa\\_final\\_06.pdf](http://www.uniformlaws.org/shared/docs/prudent%20mgt%20of%20institutional%20funds/upmifa_final_06.pdf)

## **Spending Rate Policies**

Many dioceses manage their investments on a total return basis. Under the total return concept, the dioceses focus on the overall return of their investments, including both investment income and net appreciation. A diocese may adopt a specific spending-rate formula to calculate how much of that return will be used for current operations. A typical spending policy could be a percentage rate applied to the average three-year or twelve-quarter endowment balance. Some states that have enacted UPMIFA may have adopted a safe harbor spending rate, so it is important to comply with the state law where the diocese is located. In making a determination to appropriate or accumulate endowment funds, UPMIFA requires the institution to act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, and shall consider, if relevant, the following factors: (1) the duration and preservation of the endowment fund; (2) the purposes of the institution and the endowment fund; (3) general economic conditions; (4) the possible effect of inflation or deflation; (5) the expected total return from income and the appreciation of investments; (6) other resources of the institution; and (7) the investment policy of the institution.

## **Donor Advised Funds**

For Donor Advised Funds, please refer to Chapter XX Income Tax for a discussion of this topic.

## **Net Asset Classifications**

Section 958-210-45 of the FASB Codification provides guidance for the classification of net assets. The amounts for each of the three classes of net assets (permanently restricted, temporarily restricted, and unrestricted) are based on the existence or absence of donor-imposed restrictions. For fiscal years beginning after December 15, 2017, only two classes of net assets are reported: with donor restrictions and without donor restrictions. Chapter 11 of the AICPA Audit and Accounting Guide for Not-for-Profit entities also provides guidance for net asset classifications.

## **XIX. Fundraising Appeals: Canonical Norms, Accounting Guidance and Gift Acceptance**

Canon 1262 – *“The faithful are to give support to the Church by responding to appeals and according to the norms established by the Episcopal Conference.”*

In accord with the prescripts of Canon 1262 and effective as of August 15, 2007, the following norms (verbatim) were decreed by the USCCB to govern fundraising appeals to the faithful for Church support.

### **I. Norms**

#### Motivation

1. Fundraising appeals are to be truthful and forthright, theologically sound, and should strive to motivate the faithful to a greater love of God and neighbor.
2. Fundraising efforts are to be for defined needs.
3. The relationship of trust between donor and fundraiser requires that:
  - a. Funds collected are used for their intended purposes;
  - b. Funds collected are not absorbed by excessive fundraising costs.
4. Donors are to be informed regarding the use of donated funds and assured that any restrictions on the use of the funds by the donor will be honored.

#### Competent Ecclesiastical Authority

5. Institutes of consecrated life and societies of apostolic life require approval of the respective competent major superiors and the diocesan bishop to solicit funds; diocesan entities require approval of the diocesan bishop to solicit funds; other Catholic entities and organizations require the approval of the diocesan bishop to solicit funds.
6. Approval for fundraising by the competent authority is to be given in writing with reference to the purpose for which the funds are being raised, the time-frame, and the methods to be used in raising them.
7. Oversight of fundraising programs is to be maintained by competent authority through periodic review and, where necessary, appropriate sanction.
8. Competent major superiors of institutes of consecrated life and societies of apostolic life are to submit to the diocesan bishop of the place where the fundraising originates periodic reports on the fundraising programs and the apostolic activities they support.



### Accountability

9. Fundraisers are to provide regular reports to competent authority on the extent to which promises expressed or implied in the solicitation of funds have been fulfilled.
10. Fundraising reports are to be prepared in scope and design to meet the particular concerns of those to whom the reports are due:
  - a. The governing body and membership of the fundraising organization;
  - b. The competent authorities who approved and monitor the fundraising effort;
  - c. The donors to the organization;
  - d. The beneficiaries of the funds raised.
11. Annual fundraising reports are to provide both financial information and a review of the apostolic work for which the funds were raised. They are to set forth, at the least, the amount of money collected, the cost of conducting the fundraising effort, and the amount and use of the funds disbursed.

### Procedures

12. Funds beyond operating expenses are not to be accumulated or invested by a fundraising office but are to be turned over to the appropriate office for allocation and investment.
13. Special care is to be taken to see that ethical business relationships are maintained by the fundraiser with suppliers of goods and services.
14. Contracts between a religious fundraiser and commercial suppliers and consultants are to ensure that control over materials, designs, money and general operations remain in the hands of the religious fundraiser.
15. Agreements are not to be made which directly or indirectly base payment either to the commercial firm or to the religious fundraiser on a percentage basis.

### Oversight

16. Competent authority is to ensure that fundraising organizations:
  - a. Make available fundraising reports to benefactors on a regular basis or upon reasonable request;
  - b. Provide their governing bodies with an annual financial statement prepared in accordance with generally accepted accounting principles and, where size warrants, by a certified public accountant.
17. In response to formal complaints, competent authority is to promptly investigate charges, remedy abuses and, when necessary, terminate the fundraising program.

[End of Norms]

## II. Guidance and Suggestions Concerning Canon 1262

- It is important to determine which entities (“Qualifying Entities”) within a diocese are subject to Canon 1262 (norm 5).
  - Diocesan entities – juridic persons (parishes and seminaries) and other entities
  - Public juridic persons and their apostolates
  - Institutes of Consecrated Life (religious orders of men or women and their related religious institute schools and retreat centers)
  - Societies of Apostolic Life
  - Other Catholic entities (e.g. Catholic Schools, Opus Dei Apostolates, Religious Institute Schools, Catholic Cemeteries and Mortuaries, Retreat Centers and Catholic Foundations)
- Ongoing oversight of fundraising programs (norms 7 and 8) is required. The norms require *periodic* reports but do not define the meaning of “periodic.” This is left to the agreement between the qualifying entities and the diocesan bishop. In making the periodic report on the programs, care must be taken to honor a donor’s request for confidentiality.
- Implementation of Canon 1262 should be done in close collaboration with a Judicial Vicar or Canonist of the diocese.
- Create a list of Qualifying Entities within the territory of the diocese.
  - Utilizing the Official Catholic Directory listing or other official sources, determine what entities within the territory of the diocese are Public Juridic Persons and their apostolates.
  - Research should include a review of the underlying canonical decrees for these entities within a diocese.
- Update the particular norms/laws and/or guidance of the local diocese to address requirements of Canon 1262. Each diocese should set forth its own particular law in varying manners (e.g. policy and procedures manuals), which should include the parishes and other public juridic persons within the territory of each diocese.

The general principles of Canon 1262 do not reference materiality. Consideration should be given to establishing applicability or materiality thresholds for Canon 1262 within the diocese. For example, it is doubtful that to “solicit funds” includes events such as parish school raffles, auctions, candy sales, and festivals whereas it certainly includes the solicitation of pledges payable over an extended period of time in order to finance significant expenditures representing acts of extraordinary administration.

- Prepare a diocesan notification letter to be sent to the administrator of those qualifying entities to notify them of the required norms of Canon 1262 and how these norms will be implemented as particular law within the diocese.
- Prepare a template for a letter to be used by those qualifying entities when requesting approval of the diocesan bishop to solicit funds which outlines the information specified in Canon 1262.
- Consider a two-step process for fundraising campaigns in order to obtain the bishop's written approval:
  - Phase I – Preliminary Approval. This should be completed during the early stages of planning for the fundraising campaign prior to commencement of a feasibility study or retention of a campaign consultant. Essentially, this initial request is to seek confirmation with the bishop that the fundraising concept makes sense prior to incurring substantial time, effort and dollars.
  - Phase II – Formal Approval. After feasibility and other planning work has been completed, including the approvals of the applicable entity's Board, finance council and/or administrator have been received, a formal written request should be made to the bishop requesting written approval. Such request should include the goals, methods and purpose of the fundraising campaign as explicitly as possible.
- The publication of annual fundraising reports should be made available to all donors and beneficiaries of raised funds.
- Periodic fundraising reports should be supplied to the governing body (finance council, board of directors, board of trustees, etc.) concerning the status of the fundraising.
- Annually, the qualifying entity conducting a fundraising campaign should provide to the office of the diocesan bishop information updating the status of the campaign, the cost/benefits, problems/complaints, etc.
- The due process procedures of the particular diocese should be used to resolve disputes or conflicts arising between donors and organizations, in accord with the norms for due process.

### **III. Accounting for Fundraising Activities (Updated for FASB ASU 2016-14)**

Unconditional promises to give should be recorded as pledges receivable and contribution revenue in accordance with the requirements of FASB ASC Topic #958, Sub-topic #605, Not for Profit Revenue Recognition. Contribution revenue is to be recorded as either restricted support or unrestricted support. Contributions are recorded as restricted support when donor's explicit stipulations or circumstances surrounding the receipt of the contribution makes clear the donor's implicit restriction on its use. Receipts of unconditional promises to give with payments due in future periods are to be recorded as restricted support unless explicit donor stipulations or circumstances surrounding the receipt of a promise make clear that the donor intended it to be used

to support activities of the current period. Absent a purpose or time restriction contribution revenue should be recorded as unrestricted support.

Many dioceses conduct appeals (also sometimes referred to as campaigns) to raise funds for specific programs, obligations or other special needs of the diocese and/or its parishes and schools. The purpose of the appeal as represented in the appeal literature or other communications and the existence or lack of other specific donor-imposed restrictions should determine the accounting and reporting for the funds donated as either Without Donor Restrictions or With Donor Restrictions.

Additionally, generally accepted accounting principles stipulate that contributions are to be measured at fair value upon recognition. Fair value for unconditional promises to give is measured at net realizable value for pledges due within one year and at net present value for pledges to be collected in future years. The discounts on those amounts are to be computed using risk-adjusted interest rates applicable to the periods in which the promises are received. Decreases in the value of restricted pledges receivable after initial recognition are to be recognized as losses on uncollectible contributions, or bad debt expense if related to unrestricted pledges. Recoveries of previously recognized decreases in the value of restricted pledges receivable (up to the amount of decreases previously recognized) are to be recognized as a reduction of losses on uncollectible contributions or as reduction of bad debt expense, if related to unrestricted pledges. If the reporting entity is raising funds explicitly for another entity, those funds should be reported as an “agency transaction” in accordance with ASC 958-20, Not-for-Profit Entities, Financially Interrelated Entities and ASC 958-605-30, Not-for-Profit Entities, Revenue Recognition, Initial Measurement.

Generally accepted accounting principles require that fundraising expenses be reported separately within the functional expense allocation reporting in the financial statements. Fundraising expenses may consist of direct and indirect expenses requiring allocation. SOP 98-2, *Accounting for Costs of Activities of Not-for-Profit Organizations* and ASC 958-720-25-4, Not-for-Profit Entities, Other Expenses, Fundraising Expense Recognition, contains guidance for acceptable cost allocation methodologies. A description of the methods used to allocate costs among program and support functions must also be disclosed in the financial statements.

#### **IV. Gift Acceptance Guidelines**

Consistent with the precepts of Canon 1262 and other relevant Canons, it is important for a diocese to carefully consider the need to establish guidelines for the acceptance and proper handling of gifts to the Church. The primary purpose of such procedures is to preserve the donor’s charitable intentions and specifically the precepts of Canon 1267 §3, “offerings given by the faithful for a specified purpose may only be used for that purpose.” While each diocese would establish such guidelines through its own particular law, consideration should be given to incorporating the following general principles for all types of gifts:

1. Preparation of written acknowledgments and appropriate tax correspondence that fully comply with IRS regulations (see Chapter XX). Such procedures should specifically address non-monetary gifts, such as stock, vehicles, real estate, etc.

2. Procedures to value gifts in accordance with generally accepted accounting principles. Such procedures should specifically address non-monetary gifts, such as stock, vehicles, real estate, etc.
3. Procedures to review restrictions imposed by donors so as to fully understand the ramifications of accepting said restrictions. If a gift is deemed unacceptable because of the restrictions the donor has placed on its use, the donor should be informed immediately and provided with the opportunity to remove and/or modify the identified restriction(s) or revoke the gift. Typically, only the Ordinary can refuse such gifts unless the diocese's particular law delegates such responsibility (Canon 1267 §2).
4. Procedures to evaluate the suitability of the gift. A gift may need to be refused or returned when the gift:
  - Is inappropriate or not conducive to the best interest of the mission or ministry of the diocese or parish.
  - Is known or suspected to be from an illegal or questionable source.
  - Would obligate the parish or the diocese to undertake responsibilities, financial or otherwise which are not prudent to undertake relative to the gift amount and conditions.
  - Creates excessive administrative, recording, tracking or reporting procedures for the diocese or parish.
  - Creates a conflict of interest or could damage the reputation of the diocese or parish.
  - Contains a perpetual condition (that is, no matter how enticing the gift may be, those requiring conditions for greater than 20+ years, might often be refused, as such conditions could become very onerous). Should a condition be attached to a gift that is more specific than the basic mission of the entity and is of an extended duration, the gift should not be accepted unless it provides a mechanism for the bishop to change the purpose.

Procedures to review legal obligations associated with gifts of real estate, planned gifts and bequests and/or other types of gifts. It is important to understand that such gifts can result in complicated transactions that must be evaluated carefully to ensure that the diocese and/or parish are not accepting potential or real liability upon acceptance (such as environmental liabilities associated with real estate).

## **XX. Income Tax**

*Please note that IRS regulations are being constantly updated and that this section is meant only as a general guide to issues. You should verify the current accuracy of any section before placing a final reliance on it.*

### **USCCB Group Tax Exemption Ruling**

Annually since 1946, the Internal Revenue Service (IRS) has issued to the United States Conference of Catholic Bishops, a group tax exemption ruling with respect to the Catholic organizations listed in *The Official Catholic Directory* (OCD) for a particular year (“Group Ruling”). The Group Ruling establishes (1) that organizations included in the OCD are exempt from federal income tax under section 501(c)(3) of the Code and from federal unemployment tax; and (2) that contributions to such organizations are deductible for federal income, gift, and estate tax purposes. An entire group ruling application (Form 0928A), and any applicable schedule, must be completed prior to a diocese sending a Form 0928-1 for approval. All of the forms and instructions can be found at: <http://www.usccb.org/about/general-counsel/tax-and-group-ruling.cfm>. At that website there is also a full explanation of what the Group Ruling provides as well as application forms for including newly formed organizations in the Group Ruling and OCD. Inclusion in the Group Ruling has no effect on an organization’s liability for any federal excise taxes, nor does it automatically establish an organization’s exemption from state or local income, sales, or property taxes.

### **Accounting Treatment**

The accounting treatment for income taxes is specified in Accounting Standards Codification Topic 740 – Income Taxes.

Generally Accepted Accounting Principles require that entities disclose the effect of uncertainties in tax positions. This is a two-step process where first a determination is made whether or not benefit should be recognized. Second, if the recognition threshold is met, determine the amount of benefit. While this may not affect most dioceses, they will need to document for their files that they have examined their tax positions, including non-profit status and whether they need to file forms 990, 990-N or 990-T. Because there are complex issues involved it will be helpful to involve outside experts including auditors in this examination.

*The following is intended to provide general information about income tax issues (other than accounting treatment) to dioceses in the United States.*

### **Deductibility/Substantiation of Contributions**

One of the primary benefits of section 501(c)(3) exemption is deductibility of contributions for federal income (§170), estate (§2055), and gift (§2522) tax purposes. Cash contributions by individuals to organizations listed in the OCD generally are deductible up to 50% of the donor’s adjusted gross income (“AGI”) [IRC §170(b)(1)(A)], with a five-year carryover for any excess [IRC §170(d)(1)]. After December 31, 2017 and before January 1, 2026, cash contributions may

qualify for a 60% of AGI limit [IRC Sec. 170(b)(1)(G)]. Non-cash contributions can have different limitations. Corporate gifts are deductible up to 10% of taxable income [IRC §170(b)(2)], with a five-year carryover [IRC §170(d)(2)].

In order to be deductible, a payment must first qualify as a *gift*, which is defined as a voluntary transfer of money or property without receipt of or expectation of a commensurate return benefit. Thus, for example, the payment of tuition, whether made directly to a school or to a church operating the school, is not deductible. In addition, payments made in various fundraising contexts may or may not be deductible, depending on whether goods or services are received in return. For example, payment for a purchase at a charity auction will be deductible only to the extent the payment exceeds the stated fair market value (FMV) of goods or services received in return. Payments for charity raffle tickets are not deductible, since the amount paid is not a gift, but rather payment for the chance to win whatever prize is being offered.

In response to abuses with respect to charitable contributions, in 1993 Congress enacted enhanced substantiation rules applicable to contributions of \$250 or more. Section 170(f)(8) provides that no contribution of \$250 or more will be deductible unless the donor obtains, prior to filing his or her tax return, written acknowledgment from the donee charity verifying the amount of the contribution and whether any goods or services were received in return. If so, such goods or services must be identified and must be valued by the donee charity. If the benefits received consist solely of intangible religious benefits, a statement to that effect must be included. Although the burden of requesting appropriate acknowledgment is placed on the donor and not imposed on the donee charity, charities that knowingly provide false written substantiation statements may be subject to penalties for aiding and abetting an understatement of tax liability under section 6701.

Beginning in 2007 donors must retain written documentation for **all** monetary donations in the form of a cancelled check, bank record or receipt from the donee organization showing the name of the donee organization, the date of the contribution and the amount of the contribution. This will make it important that donors use checks or contribution envelopes. This requirement is in addition to the section 170(f)(8) substantiation requirements noted above.

Certain payments are considered quid pro quo contributions – namely, they are made partly as a gift and partly in consideration for goods or services furnished to the donor. An exception is provided for payments made to an exclusively religious organization in return for which the donor receives solely intangible religious benefits. Under section 6115, charitable organizations must inform donors in writing that quid pro quo contributions in excess of \$75 are deductible only to the extent that they exceed the value of any goods or services provided by the charitable organization in return, and the organizations must provide a good-faith estimate of the value of such goods or services. This disclosure must be made either at the time of solicitation or upon receipt of the quid pro quo contribution. Penalties are imposed on any charity that fails to make appropriate disclosure under section 6115 at \$10 per contribution, capped at \$5,000 per particular fundraising event or mailing. Typical quid pro quo contribution situations include charity golf tournaments, auctions, dinner dances, and so forth, where part of the payment constitutes a contribution. In such situations, the disclosure statement may be placed in solicitation materials, in event programs or brochures, or on the face of event tickets – i.e. in any reasonable manner likely to come to the attention of the donor.

Additional substantiation requirements are imposed with respect to certain contributions. Most non-cash contributions require that the donor receive a receipt from the charitable organization showing the name of the charitable organization, the date and location of the contribution and a reasonable description of the item(s) donated. Items dropped off at collection boxes and valued at less than \$250 do not require a receipt however the items donated must be in “good condition,” with no guidance provided on what constitutes “good condition.” Contributors of non-cash gifts valued at \$500 or more must complete Form 8283 and attach it to Form 1040. Contributors of non-cash gifts valued at \$5,000 or more (other than gifts of publicly traded securities) must:

- Obtain a qualified appraisal and submit an appraisal summary with the Form 8283 attached to Form 1040, and
- Have the donee charity complete and return to the donor the “Donee Acknowledgment Section” (in doing so, the donee charity is not vouching for the appraised value)

The donee charity is required to report to the IRS on Form 8282 if such contributions are subsequently sold or otherwise disposed of within three years of receipt.

The IRS has issued special rules for the claiming of deductions for donated vehicles. In general, the deduction will be limited to the actual sales price the charity receives for the vehicle. Donors may claim a deduction for the fair market value under the following circumstances:

- The charity makes a significant intervening use of the vehicle, such as using it to deliver meals on wheels.
- The charity makes a material improvement to the vehicle, i.e. major repairs that significantly increase its value and not mere painting or cleaning.
- The charity donates or sells the vehicle to a needy individual at a significantly below-market price, if the transfer furthers the charitable purpose of helping a poor person in need of a means of transportation.

Sales of donated vehicles are reported to the IRS and to donors on form 1098-C. Copy A must be filed with the IRS. Copies B and C must be furnished to the donor (for donor’s records and for attachment to his or her tax return) not later than 30 days after the date of sale if box 4a is checked, or 30 days after the date of the contribution if box 5a or 5b is checked. Form 1098-C is available on the IRS website at [www.irs.gov](http://www.irs.gov) under Forms and Publications.

Finally, diocesan entities often benefit from contributed services. A parishioner may volunteer to clean the church every week, or a carpenter may replace the windows and only charge for materials. These acts of charity are welcomed, and often the volunteer asks for a tax receipt for the contributed services. While it is permissible to write a letter thanking the volunteer for donating his or her time, it is not permissible to give the volunteer a tax receipt or include the value of services on the volunteer’s annual contribution statement. The value of contributed services is not deductible. The donor may deduct his or her unreimbursed out of pocket expenditures.

## **Lobbying Activities**



Section 501(c)(3) organizations may not engage in more than insubstantial lobbying activities. Lobbying includes contacting, or urging the public to contact, members of a legislative body for the purposes of proposing, supporting, or opposing legislation or advocating adoption or rejection of legislation [Treas. Reg. §1.5019(c)(3)-1(c)(3)(ii)]. Legislation includes any action by Congress, by a state or local legislative body, or by the public in a referendum, initiative, constitutional amendment, or similar procedure [Treas. Reg. §1.501(c)(3)-1(c)(3)(ii)]. No distinction is made between “good” and “bad” legislative activity (see Rev. Rul. 67-293, 1967-2 C.B. 185).

The IRS has never defined “insubstantial” in this context or identified a percentage safe harbor for legislative activities. Court cases suggest a 5 to 15% range, but the IRS comfort zone is at the lower end. See *Murray Seasongood v. Commissioner* (227F.2d 907 (6<sup>th</sup> Cir. 1955)), which rules that less than 5% time and effort is not substantial; and *Haswell v. U.S.* (500F.2d 1133 (Ct. Cl. 1974), cert. denied, 419 U.S. 1107 (1975)), which rules that 16 to 17% of a budget was substantial. A more specific elective lobbying standard was enacted in 1976 as section 501(h) of the Code. Churches, conventions of churches, and integrated auxiliaries at their own request were made ineligible [IRC §§501(h)(5) and 4911(f)(2)].

### **Political Activities**

A section 501(c)(3) organization may not engage in any political campaign activity. Unlike the lobbying limitation, this is an absolute prohibition. The statute states that 501(c)(3) organizations may not “participate in or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.” The prohibition applies only to candidates for elective public office. The IRS has indicated that it will be paying special attention to so called “issue advocacy” materials distributed by churches, focusing on both the content and the manner of distribution. They have also indicated that they will scrutinize links provided on website to determine if there is inappropriate advocacy of candidates.

Although very little additional interpretation is provided in the regulations, the penalties for violating the prohibition are severe. In addition to loss of tax-exempt status and deductibility of contributions, two-tiered excise taxes may be imposed on the exempt organization (10% and 100%) and on the organization manager (2-1/2% and 50%) for political expenditures (IRC §4955). In flagrant cases, the IRS may seek an injunction against further political expenditures (IRC §7409[a]) and immediate determination and assessment of income and excise taxes (IRC §6852). For more information, check the OGC website, [www.usccb.org/ogc](http://www.usccb.org/ogc).

### **Donor Advised Funds**

Section 1231 of the Pension Protection Act of 2006 (the “Act”) added new Code section 4966, which includes for the first time a definition of the term “donor advised fund:” a fund or account that (1) is separately identified by reference to contributions of a donor(s); (2) is owned and controlled by a sponsoring organization; and (3) with respect to which a donor (or his appointee

or designee) has, or reasonably expects to have, advisory privileges with respect to the distribution or investment of amounts held in the fund/account by reason of the donor's status as donor. All three criteria must be satisfied in order for a fund or account to be classified as a donor advised fund.

The following funds or accounts are *not* classified as donor advised funds: (1) a fund or account that makes distributions only to a single identified organization or governmental entity; or (2) a fund or account with respect to which the advisor (including donor, appointee and designee) advises as to the recipients of grants for travel, study or similar purpose if (i) the advisory privileges are performed exclusively as a member of a committee appointed by the sponsoring organization, (ii) no combination of advisors (or related parties) directly or indirectly control the committee, and (iii) all grants are awarded on an objective and nondiscriminatory basis under procedures that are approved in advance by the sponsoring organization's board of directors and are designed to meet the requirements of §4945(g)(1), (2) and (3).

A "sponsoring organization" is defined as any organization that is described in section 170(c) (other than a government entity and without regard to the requirement to be created or organized in the U.S.), is not a private foundation, and maintains one or more donor advised funds.

The most likely candidates for holding donor advised funds are "foundations" or endowment funds of dioceses, parishes, schools, hospitals and other diocesan organizations. If a diocesan organization maintains donor advised funds, however, it may need to make changes in terms of operations, including relationships with donors/advisors, fund distributions, investments, reporting, and donor acknowledgments.

In late 2017, the IRS issued Notice 2017-73 that provided guidance and requested comments on several issues related to donor-advised funds. The Notice indicates the Service's intent to issue regulations providing that (1) certain distributions from a DAF that pay for the purchase of tickets enabling a donor, donor advisor, or related person to attend a charity-sponsored event result in a more than incidental benefit to such person, and (2) certain distributions from a DAF that the recipient charity treats as fulfilling a pledge made by a donor, donor advisor, or related person, do not result in a more than incidental benefit if certain requirements are met.

### **Excess Benefit Transactions – Intermediate Sanctions**

In 1996, Congress enacted section 4958 of the Internal Revenue Code, the so-called "intermediate sanctions" provisions, which were designed to provide the IRS with a sanction other than revocation of exemption for non-fair market value transactions with insiders, defined in section 4958 as "excess benefit" transactions. Section 4958 applies to transactions occurring on or after September 14, 1995 (with the exception of transactions pursuant to certain binding written contracts in effect before that date). In 1998, proposed regulations were issued to provide interpretive guidance under section 4958. Public hearings were held in March 1999. In January 2001, the IRS issued temporary regulations; and in January 2002, the IRS issued final regulations. Some of the major provisions of the final regulations are summarized below.

#### ***Applicable Tax-Exempt Organizations***

Section 4958 applies to any organization that, without regard to any excess benefit, would be described in section 501(c)(3) or (c)(4) and exempt from tax under section 501(a) (EO, or “exempt organization”), at any time during a five-year period ending on the date of the excess benefit transaction (“lookback period”). An organization is described in section 501(c)(3) for purposes of section 4958 only if it provides notice under section 508 (filing form 1023), unless it is otherwise described in section 501(c)(3) and is specifically excluded from application of section 508. Accordingly, churches, their integrated auxiliaries, and conventions and associations of churches – which are statutorily excepted from section 508 are nonetheless subject to section 4958.

### **Excise Taxes Imposed**

Section 4958 imposes excise taxes on any excess benefit resulting from an excess benefit transaction between the EO and a disqualified person (DP). Significantly, these taxes are not imposed on the organization. Rather, the DP is liable for a 25% first-tier tax, and for a 200% second-tier tax, if the excess benefit transaction is not corrected within the correction period. In addition, a tax equal to 10% of the excess benefit (up to a maximum tax of \$20,000) is imposed on an organization manager (OM) who knowingly participates in an excess benefit transaction, unless participation was not willful and was due to reasonable cause. An OM will not be liable for tax if he or she opposed the transaction. If more than one person is liable for tax under section 4958, all such persons are jointly and severally liable.

### ***“Disqualified Person” Defined***

Section 4958 defines a “disqualified person” as any person who was in a position to exercise substantial influence over the affairs of the organization at any time during a five-year lookback period ending with the date of the transaction. The term also encompasses certain members of the DP’s family and certain 35%-controlled entities.

*Persons Having Substantial Influence.* The final regulations state that individuals holding any of the following powers, responsibilities, or interests are in a position to exercise substantial influence over the affairs of an EO: (1) voting members of the governing body; (2) individuals who, regardless of title, have ultimate responsibility for implementing the decisions of the governing body or for supervising the management, administration, or operation of an EO (persons serving as president, chief executive officer, or chief operating officer have such responsibility unless they demonstrate otherwise); and (3) individuals who, regardless of title, have ultimate responsibility for managing the finances of an EO (persons serving as treasurer or chief financial officer have such responsibility unless they demonstrate otherwise).

*Persons Deemed Not to Have Substantial Influence.* The final regulations state that the following are deemed not to have substantial influence over the affairs of an EO: (1) organizations exempt under section 501(c)(3); (2) certain section 501(c)(4) organizations; and (3) employees receiving direct or indirect economic benefits of less than the “highly compensated employee” amount in section 414(q)(1)(B)(i) (\$120,000 for 2018), who are not otherwise classified as DPs by virtue of position, family relationship, or substantial contribution. In all other cases, whether an individual is a DP depends on all relevant facts and circumstances. The final regulations clarify that an organization can be a DP.

### ***“Organization Manager” Defined***

An “organization manager” is defined as any officer, director, or trustee of an EO, or any individual having similar powers with respect to the EO, regardless of title. An officer includes an individual who (1) is so designated in organizational documents, or (2) “regularly exercises general authority to make administrative or policy decisions on behalf of the organization.” The final regulations provide that independent contractors, acting solely in their capacity as attorneys, accountants, or investment managers/advisors, are not officers. In addition, individuals who are not officers, directors or trustees, but who serve on a committee of an EO’s governing body that is attempting to invoke the rebuttable presumption of reasonableness (discussed below) based on the committee’s actions, are considered OMs for purposes of section 4958.

### ***“Excess Benefit Transaction” Defined***

The final regulations define an “excess benefit” as the amount by which the value of the economic benefit provided by an EO directly or indirectly to or for the use of any DP exceeds the value of the consideration (including the performance of services) received by the EO for providing such benefit. With certain exceptions explained below, all consideration and benefits exchanged between a DP and an EO (including any controlled entities) must be taken into account in order to determine whether an excess benefit transaction has occurred. The final regulations provide that, in determining the reasonableness of compensation that is paid (or vests, etc.) in one year, services performed in prior years may be taken into account.

*Rebuttable Presumption of Reasonableness.* Consistent with the legislative history of section 4958, the final regulations establish a rebuttable presumption whereby compensation paid by an EO to a DP, or the transfer of property or other benefit between the EO and a DP, will be presumed to be at FMV, provided three conditions are satisfied: (1) the compensation or terms of transfer are approved in advance by the organization’s governing body (or a committee of the governing body) composed entirely of individuals who do not have a conflict of interest with respect to the arrangement or transaction; (2) the governing body or committee obtained and relied upon appropriate data as to comparability prior to making its determination; and (3) the governing body or committee adequately and concurrently documented the basis for its determination. The IRS may rebut the presumption only if it develops sufficient contrary evidence to rebut the probative value of the comparability data relied upon by the governing body or committee.

*Certain Economic Benefits Disregarded.* All fringe benefits that are excluded from income under section 132 (except certain liability insurance premiums, payments, or reimbursements) are disregarded for purposes of section 4958. The final regulations also disregard expense reimbursements paid under an accountable reimbursement plan that meets the requirements of section 1.62-1(c). Thus, as is the case with section 132(d) on working condition fringe benefits, the existing standards under section 162 and 274 will apply to determine whether employee expense reimbursements are disregarded or should be treated as part of a DP’s compensation for purposes of determining reasonableness under section 4958.

*Written Contemporaneous Substantiation.* An EO must provide written substantiation that is contemporaneous with the transfer of benefits at issue in order to provide clear and convincing evidence of its intent to treat benefits provided to a DP as compensation for services. To satisfy this requirement, either (1) the EO must report the economic benefit as compensation on an original or amended federal tax return with respect to the payment, e.g. Form W-2 or 1099, filed prior to commencement of an IRS examination; or (2) the DP must report the benefit on his or her original or amended federal tax return, e.g. Form 1040, also filed prior to commencement of an IRS examination.

If a benefit is not reported on a return filed with the IRS, other written contemporaneous evidence, e.g. employment contract, may be used to demonstrate that the appropriate decision-making body or an authorized officer approved a transfer as compensation for services in accord with established procedures. The final regulations clarify that the term “established procedures” refers to the EO’s usual practice for approving compensation and does not require that an EO have a formal written procedure for approving compensation.

*Correction.* An excess benefit transaction is corrected by undoing the excess benefit to the extent possible and by taking any additional measures necessary to place the EO in a financial position not worse than that in which it would be if the DP were dealing under the highest fiduciary standards. The correction amount equals the sum of the excess benefit and the interest thereon. Generally, a DP corrects an excess benefit by making a payment in cash or cash equivalents (not a promissory note) to the EO equal to the correction amount. However, with the agreement of the EO, the DP may make correction by returning specific property previously transferred in the excess benefit transaction. The DP will be treated as making a payment equal to the lesser of the following: either the property’s FMV determined on the date the property is returned or the FMV determined on the date the excess benefit transaction occurred. If such payment is not equal to the correction amount, the DP must make additional cash payment to the EO in the amount of the difference. If the DP makes payment of less than the full correction amount, the 200% tax is imposed only on the unpaid portion.

The final regulations clarify the rules governing correction when an EO no longer exists or is no longer tax-exempt by requiring that another section 501(c)(3) organization receiving the correction amount be a publicly supported charity that has been in existence as such for a continuous period of at least sixty calendar months ending on the correction date. This time-in-existence requirement is designed to prevent a DP from creating a new EO to receive the correction amount. The final regulations also require that the organization receiving the correction amount not allow the DP to make or recommend any grants or distributions by the organization. Finally, the DP may not also be a DP with respect to the organization receiving the correction amount.

### ***Special Rule for Churches***

The final regulations provide that the church audit procedures under section 7611 of the Internal Revenue Code will be used in initiating and conducting any IRS inquiry or examination into whether an excess benefit transaction has occurred between a church and a DP. The reasonable belief required to initiate a church tax inquiry will be satisfied if there is a reasonable belief that taxes under section 4958 are due from a DP with respect to a transaction involving a church.

### ***Embezzlement***

Any economic benefit received by a DP (who by definition has substantial influence) from the assets of an EO is considered to be provided by the EO, even if the transfer of the benefit was not authorized under the regular procedures of the organization. The practical result of this rule is that funds embezzled by a DP generally constitute excess benefit transactions. The final regulations clarify that in no event will an economic benefit that a DP obtains by theft or fraud be treated as consideration for the performance of services.

### ***Substantive Exemption Requirements Still Apply***

The final regulations verify that section 4958 does not affect the substantive requirements for exemption under sections 501(c)(3) or (4), including the requirements that the EO be organized and operated exclusively for exempt purposes and that no part of the net earnings inure to the benefit of any private shareholder or individual. Thus, regardless of whether a transaction is subject to excise taxes under section 4958, existing exemption principles and rules apply (e.g. a transaction that is not subject to section 4958 because of the initial contract exception may still jeopardize the EO's exempt status). The preamble to the temporary regulations indicated that the IRS would exercise its administrative direction provided in the legislative history and would publish guidance concerning factors it will consider with respect to revocation of exemption in excess benefit transaction situations. Until such time, the IRS will consider all facts and circumstances in the administration of section 4958 (see Final Regulations on Excise Taxes on Excess Benefit Transactions, 67 Fed. Reg. 3076 [January 23, 2002]).

### ***Automatic Excess Benefits***

An economic benefit may not be treated as consideration for the performance of services (and therefore looked at together with other reasonable compensation for services) unless the church has clearly indicated its intent to treat the benefit as compensation when the benefit is paid. In determining intent, the relevant factors include whether (1) the appropriate decision-making body has approved the transaction as compensation in accordance with its procedures or (2) the church has provided written substantiation (such as inclusion of the benefit as taxable wages on Form W-2 or other IRS return or form) that is contemporaneous with the transfer of the economic benefit at issue. Failure to provide this documentation would cause the provision of such benefit to be outside the realm of reasonable compensation for services and thereby considered a transfer of assets/benefit without a return benefit to the church. Such automatic excess benefits are subject to the penalties outlined above and include perquisites such as companion travel, personal services, housing and similar benefits not otherwise excluded from taxable wages under the Code or as a properly substantiated and qualified expense reimbursement.

### **Filing Requirements for Form 990**

All organizations included in the Official Catholic Directory (OCD) must file Form 990, Return of an Organization Exempt from Income Tax, unless they are eligible for a mandatory or discretionary exemption to this filing requirement. There is no automatic exemption from the

Form 990 filing requirement simply because an organization is included in the Group Ruling or listed in the OCD. Organizations required to file Form 990 must do so by the 15<sup>th</sup> day of the fifth month after the close of their fiscal year. Among the organizations not required to file Form 990 under section 6033 of the Code are: (i) churches and interchurch organizations of local units of a church; (ii) integrated auxiliaries (including a men's or women's organization, a youth group, a religious school, and a mission society), and conventions or associations of churches; (iii) the exclusively religious activities of religious orders; (iv) schools below college level affiliated with a church or religious order; (v) organizations with gross receipts normally not in excess of \$50,000 (but see below for requirements to file Form 990-EZ or 990-N); and (vi) certain church-affiliated organizations that finance, fund or manage church assets, or maintain church retirement insurance programs, and organizations controlled by religious orders that finance, fund or manage assets used for exclusively religious purposes. Diocesan entities not covered by the above exemptions are required to file Form 990, Form 990-EZ if gross receipts are less than \$200,000 and total assets are less than \$500,000, or 990-N if annual revenues are less than \$50,000.

*Special Rules for Section 509(a)(3) Supporting Organizations.* The Pension Protection Act of 2006 eliminated discretionary exceptions to the Form 990 filing requirement as applied to section 509(a)(3) supporting organizations. The discretionary exceptions likely to be affected by this provision are exceptions (v) and (vi) above. This means that if an organization exempt under the Group Ruling is classified as a section 509(a)(3) supporting organization, it may no longer rely on exceptions (v) or (vi) above as the basis for not filing Form 990. However, a section 509(a)(3) supporting organization that qualifies as an integrated auxiliary of a church under section 6033 may continue to rely on that exception as a basis for not filing Form 990. Because it is a statutory exception, the integrated auxiliary of the church exception was not affected by the Pension Protection Act. Beginning in calendar year 2014, an organization classified as a section 509(a)(3) supporting organization that is required to file Form 990 or 990-EZ, will now be required to demonstrate in detail on Schedule A how it meets the supporting organization classification.

*Form 990-N Filing Requirements.* Under the Pension Protection Act of 2006, an organization exempt under the Group Ruling that claims exception (v) above (gross receipts normally not in excess of \$50,000) as its sole basis for not filing Form 990 must file annual electronic Form 990N ("e-postcard") as required by IRS, setting forth the following information: (1) the legal name of the organization; (2) any name under which the organization operates or does business; (3) the Organization's mailing address and Internet website address; (4) the organizations EIN; (5) the name and address of a principal officer; (6) evidence of the organization's continued qualification for exemption from the Form 990 filing requirement; and (7) notification of termination, if applicable. Form 990-N must be submitted electronically through the IRS website on or before the 15<sup>th</sup> day of the fifth calendar month following the close of the fiscal year for which it is filed.

*Public Disclosure and Inspection.* Any organization that is required to file either Form 990, Form 990-EZ, or Form 990-N must upon request make a copy of the form and its schedules and attachments (other than Form 990 contributor lists) available for public inspection during regular business hours at the organization's principal office and at any regional or district offices having three or more employees. Form 990, Form 990-EZ, or Form 990-N for a particular year must be made available for a three-year period beginning with the due date of the return. In addition, any organization that files Form 990, Form 990-EZ, or Form 990-N must comply with written or in-

person requests for copies of the form. The organization may impose no fees other than a reasonable fee to cover copying and mailing costs. If requested, copies of the forms for the past three years must be provided. In-person requests must be satisfied on the same day. Written requests must be satisfied within 30 days.

*Public Disclosure of Form 990-T.* Under the Pension Protection Act of 2006, Form 990-T, Exempt Organization Unrelated Business Income Tax Return, is subject to the same public inspection and copying rules that apply to Forms 990, 990-EZ, and 990-N, except that only attachments to the form that relate to the imposition of tax must be disclosed.

*Revocation for Failure to File.* Under the Pension Protection Act of 2006, the tax-exempt status of an organization, including an organization exempt under the Group Ruling, that is required to file either Form 990, Form 990-EZ, or Form 990-N but that fails to do so for three consecutive years will be considered revoked. Reapplication to IRS (not through the Group Ruling process) will be required in order to reinstate exemption.

Because the requirements for filing Forms 990, 990-EZ, 990-N and 990-T are complicated and the questions with regard to financial governance need to be answered in a uniform manner, it is suggested that all 990 forms be reviewed centrally at the diocesan level prior to being filed.

### **Filing Requirements for Form 5578**

Rev. Proc. 75-50, 1975-2 C.B. 587, sets forth notice, publication, and record keeping requirements regarding racially nondiscriminatory policies that must be complied with by private schools, including church-related schools, as a condition of establishing and maintaining exempt status under section 501(c)(3) of the Code. Under Rev. Proc. 75-50, private schools are required to file an annual certification of racial nondiscrimination with the IRS. For private schools not required to file Form 990, the annual certification must be filed on Form 5578, Annual Certification of Racial Nondiscrimination for a Private School Exempt from Federal Income Tax. Form 5578 must be filed by the fifteenth day of the fifth month following the close of the fiscal year. Form 5578 may be filed individually by school or by the diocese on behalf of all its diocesan schools.

### **Filing Requirements for Foreign Investments**

All organizations that have investments in offshore funds are also subject to various informational filings, with failure to file penalties of \$10,000 per form or greater. The forms required depend on the type of investment and the percentage of ownership of such investment, but include Forms 926, 8865, 8621 and 5471. The investments can be directly held through a domestic limited partnership or held by a U.S. investment advisor on your behalf. The requirement to file is triggered by transferring cash of \$100,000 or any amount of non-cash asset in a rolling 12-month period or a change in, or actual ownership of, 10% or more of the investment vehicle or similar thresholds. Organizations holding foreign financial accounts with a value that exceeds \$10,000 at any time during the year must also file a Report of Foreign Bank and Financial Accounts.

### **Unrelated Business Income Tax (UBIT)**



Although organizations included in the Group Ruling are exempt from federal income tax, they are subject to tax on the income from any unrelated trade or business in which they regularly engage. Unrelated business income is governed by sections 511-514 of the Internal Revenue Code. UBIT is imposed at the normal corporate rates. A Form 990-T must be filed if an organization has gross income from unrelated trade or business of \$1,000 or more, regardless of whether tax is due or whether the organization is required to file Form 990. The Form 990-T must be filed no later than the fifteenth day of the fifth month after the close of the organization's tax year [IRC §6072(e)]. If taxes are owed, organizations are expected to file quarterly estimated income tax returns.

An "unrelated trade or business" is as follows: (1) a trade or business as defined under section 162 of the Code (generally, any activity carried on for the production of income from the sale of goods or the performance of services); (2) one that is regularly carried on; and (3) one that is not substantially related to an organization's exempt purposes. The IRS applies a "fragmentation rule" to classify different aspects of what might otherwise appear to be a unitary business endeavor as being either related or unrelated. For example, the sale of advertising in an otherwise exempt educational periodical is considered a trade or business, which will generally be unrelated to its exempt purposes. This provision will apply to most diocesan newspapers that accept paid advertising.

To be considered "regularly carried on," a trade or business must exhibit "frequency and continuity" and be carried on in a manner similar to its commercial counterpart [Treas. Reg. §1.513-1(c)(1)]. In order to qualify as "related," IRS requires a substantial causal relationship between the activity and an organization's exempt purposes [Treas. Reg. §1.513-1(d)(2)]. The fact that an organization uses funds derived from its unrelated business activity in order to further its exempt programs does not convert an unrelated activity into a related one. Further, even if an activity relates to exempt purposes, it may be carried on to an extent greater than necessary to achieve those purposes. In such situations, income derived from excess activity will be subject to unrelated business income tax.

There are a number of exceptions to the UBIT rules, including the following:

***Volunteer Exception.*** This exception applies when substantially all of the work in a particular activity is performed by volunteers [IRC §513(a)(1)]. The IRS's standard for "substantially all" is 85%. This exception typically applies to activities like church raffle, bingo games, and other fundraisers, although many such activities could also avoid being characterized as subject to UBIT because they are not regularly carried on.

***Convenience Exception.*** This exception applies to any trade or business carried on primarily for the convenience of its members, students, patients, officers, or employees [IRC §513(a)(2)]. Classic examples of this exception include the hospital pharmacy sales made to patients, the sale of books by a university bookstore to students, sales in hospital gift shops, and laundry and vending operations provided for student use.

***Donated Merchandise and Low-Cost Item Exceptions.*** The donated merchandise exception applies to the sale of merchandise that has been received as a contribution or gift [IRC §513(a)(3)]. This exception applies to thrift stores operated by churches and other charitable organizations. The Code also contains an exception for the distribution of low-cost items incident to charitable solicitations. If a church mails unrequested, low-cost items as part of a fundraising effort, the church is not liable for UBIT on the income received [IRC §513(h)(1)(A)]. The dollar amount is indexed for inflation and changes each year.

***Mailing List Exception.*** Section 513(h)(1)(B) of the Code provides that income from the rental or exchange of mailing lists between or among section 501(c)(3) organizations is not subject to UBIT. The IRS has taken the position that rentals or exchanges with non-501(c)(3) organizations is subject to UBIT. However, after a string of litigation losses, the IRS will agree that properly structured licensing agreements for the use of mailing lists can generate non-taxable royalty income (see below).

***Bingo and Gambling Activities Exception.*** An important UBIT exception for many churches and related entities is the bingo exception, which applies to bingo games where participants place wagers, winners are determined, and prizes are distributed in the presence of all persons placing wagers in the game [IRC §513(f)]. The bingo exception does *not* apply to scratch-off bingo cards, bingo machines or to other forms of “walk-away” games. In addition, there are various IRS reporting and withholding requirements related to awards from these activities. See IRS publication 3079, “Tax Exempt Organizations and Gaming.”

***Miscellaneous Exceptions.*** There are also UBIT exceptions for qualified convention and trade show activities conducted by section 501(c)(3), (c)(4), (c)(5), and (c)(6) organizations, and for certain services, including data processing, food services, and laboratory services provided at cost to hospitals with one hundred or fewer beds [IRC §§513(d), (e)].

In addition to the above exceptions to the definition of unrelated trade or business, the Code provides certain modifications to the computation of UBI, primarily for passive income sources. Thus, although unrelated, income from certain sources will be excluded from the computation of unrelated business income. The major modification categories under §512(b) include dividends, interest, annuities, rents, and royalties.

***Royalties.*** A “royalty” is a payment for the use of a valuable intangible property right, e.g. use of an exempt organization’s name and logo. Payments for services provided by the organization are not considered royalties [Rev. Rul. 81-178, 1981 C.B. 135]. Royalties are not included in the computation of unrelated business income [IRC §512(b)(2)]. The scope of the royalty exception has been unclear for the past several years, particularly in the context of affinity credit card and similar arrangements. However, after a string of litigation losses, the IRS determined in late 1999 to stop litigating affinity card and mailing list rental cases except where the factual record clearly established that the exempt organization was providing more than incidental services in exchange for payments received. Thus, income from an exempt organization’s licensing of the use of its name, logo, mailing lists or other valuable intangible property rights will generally be treated as

nontaxable royalty income, provided that no more than incidental services – i.e. those inherent in and necessary to the nature of the arrangement – are provided in return.

***Rents from Real Property.*** Rents from real property are not subject to UBIT under section 512(b)(3) of the Code. Rents from personal property rented with real property may also be exempt provided that the rent attributable to personal property is no more than 10% of the total. If 10 to 50% of the rent is attributable to the rental of personal property, then a pro rata share of the rental income will be subject to UBIT. However, if more than 50% of the rent is attributable to personal property, then the modification is lost and the entire rental amount will be taxed.

Further, an exempt organization may not provide services in connection with the rental of real property, with the exception of services customary in connection with the rental of space: such as light, heat, trash collection, and cleaning of common areas. This issue of services often arises in the context of retreat houses and parking lots. For example, if an exempt organization rents its parking lot to a third party, which is responsible for all aspects of its operation, the income is considered the rental of real property not subject to UBIT. If, on the other hand, a church rents certain spaces in its parking lot during the week for use by nearby business people, these rents will generally be subject to UBIT. They do not qualify for the rental of real property exception because the church remains responsible for lot maintenance, snow removal, signs, barriers, security, line painting, etc. [see, e.g. PLR 9301024 (October 15, 1992)]. In the retreat house situation, frequently church organizations rent excess capacity in their facilities for business retreats, wedding receptions, and the like. Because a full range of services is typically provided in such situations, including maid service, food service, etc., it is not considered the rental of real property, but rather is more analogous to hotel operations.

***Sales or Exchanges.*** Under Section 512(b)(5), all gains or losses from the sale, exchange, or other disposition of property is excluded from the computation of UBIT, with the exception of stock in trade or other property that would be classified as inventory, and property held primarily for sale to customers in the ordinary course of business.

There are two major exceptions to the exclusions from UBIT under section 512(b) outlined above that render income taxable despite the section 512(b) modifications:

1. ***Debt-Financed Income.*** Under the provisions of section 514 of the Code, income that would otherwise be excluded from taxation under section 512(b)(1), (2), (3), and (5) (i.e. dividends, interest, royalties, rents and certain gains and losses from the sale of property) may nonetheless be subject to UBIT if it is subject to acquisition indebtedness – i.e. was acquired or improved with borrowed funds. Unrelated debt-financed income from such property is taxable in proportion to its acquisition indebtedness.
2. Certain exceptions to the debt-financed income rules are relevant to church property. First, where substantially all (at least 85%) of the property's use is substantially related (aside from the need for funds) to the organization's exempt purposes, it is not treated as debt-financed property [IRC §514(b)(1)(A)]. Second, where property is owned by one exempt organization and is used by certain related organizations, it is not treated as debt-financed

property to the extent that the property is used by either organization in furtherance of its exempt purposes [IRC §514(b)(2)].

3. Third, under the “neighborhood land rule” exception, if an organization acquires real property and intends to convert it to use for exempt purposes within ten years, the property will not be treated as debt-financed property if it is in the neighborhood of other property used by the organization for exempt purposes and if the intent to use the property for exempt purposes within ten years is not abandoned [IRC §514(b)(3)(A)]. Note, however, that section 514(b)(3)(C)(i) vitiates the neighborhood land rule exception with respect to any structure on the land, when it is acquired, that is not required to be removed or demolished as part of the conversion. Special consideration is given to churches and conventions or associations of churches. Among other things, a fifteen-year period applies instead of the regular ten-year period, and the requirement that the acquired land be in the neighborhood of other property used for exempt purposes is eliminated [IRC §514(b)(3)(E)].

- a. *Controlled Subsidiary Exception.* Section 512(b)(13), which was significantly revised in 1997, provides that specific payments such as rent, royalty, annuity, and interest income, which is generally excluded from unrelated business taxable income, are not so excluded if it is received from a controlled subsidiary of a tax-exempt organization. Under section 512(b)(13) prior to 1997, a controlled subsidiary was defined as 80% controlled by the tax-exempt parent organization. The control test did not incorporate any indirect ownership rules, so that rents, royalties, annuities, and interest from second-tier subsidiaries generally did not constitute unrelated business taxable income to the tax-exempt parent organization. In an attempt to thwart tax-exempt organizations’ attempts to elude UBIT on amounts received from subsidiary organizations, Congress lowered the threshold for “control” from 80% to the current 50%. With respect to stock subsidiaries, “control” means ownership by vote or value of more than 50% of the stock. For partnerships or other entities, “control” means ownership of more than 50% of the profits, capital, or beneficial interests. In addition, the constructive ownership rules of section 318 of the Code were made applicable to section 512(b)(13). As a result, a tax-exempt parent organization will be considered to control a subsidiary in which it holds, directly or indirectly, more than 50% of the voting power or value. Any rent, royalty, annuity, or interest received by an exempt organization from its controlled entity will be unrelated business taxable income to the extent that the payment reduces the net unrelated income or increases the net unrelated loss of the controlled entity.

- b. There are currently two exceptions that would allow a tax-exempt organization to receive specified payments from controlled subsidiaries free from UBIT. The first exception is if the controlled subsidiary carries out an activity that would further the exempt purpose of the tax-exempt parent organization, then the specified payments would not be subject to UBIT by the tax-exempt parent. The second exception comes from the Pension Protection Act of 2006 which allowed for qualifying specified payments that meet the section 482 arm’s length transfer

standards to be excluded from UBIT treatment. A qualifying specified payment is any specified payment made under a contract that was in force as of August 16, 2006, or a contract that is a renewal under substantially similar terms as those entered into under a prior contract in force as of August 17, 2006. Any amount in excess of an arm's length amount would be subject to UBIT. The second exception is currently subject to extension each calendar year by Congress. The exception has currently been extended to January 1, 2015. With the uncertainty of the extension, it is suggested that a tax advisor be consulted to verify if it is still applicable.

### ***Corporate Sponsorship Regulations***

The Taxpayer Relief Act of 1997 amended the Internal Revenue Code to add section 513(i), which provides that the receipt of qualified sponsorship payments by an exempt organization subject to tax imposed under section 511 of the Code does not constitute receipt of income from an unrelated trade or business. Section 513(i) applies to payments solicited or received after December 31, 1997. In March 2000, the IRS issued proposed regulations interpreting section 513(i). The IRS has issued final regulations under section 513(i), which are effective as of April 25, 2002, and are applicable for payments solicited or received after December 31, 1997.

### ***Applicability***

The final qualified sponsorship payment regulations apply to the following: single events conducted by an exempt organization (e.g., a bowl game, TV show, or walkathon); a series of events (e.g. an athletic tournament or concert series); or an activity conducted over a period of time (e.g. an art exhibit). It is irrelevant whether the sponsored event is substantially related to the exempt organization's tax-exempt purpose. The qualified sponsorship provisions do not apply to payments made in connection with exempt organization trade shows [governed by section 1.513-3 of the regulations] or to income derived from the sale of advertising or acknowledgements in exempt organization periodicals [governed by section 1.512(a)-1(f)]. A "periodical" is defined as "regularly scheduled and printed material published by or on behalf of the exempt organization that is not related to and primarily distributed in connection with a specific event conducted by the exempt organization." The final regulations clarify that printed material includes material that is published electronically.

### ***Qualified Sponsorship Payments***

The final regulations define a "qualified sponsorship payment" as a payment made by any person engaged in a trade or business for which there is no expectation or arrangement that the payer (or persons designated by the payer) will receive any substantial return benefit from the exempt organization. "Payment" means the payment of money, transfer of property, or performance of services.

### ***Substantial Return Benefit***

Substantial return benefit is defined as any benefit *other than* (1) a use or acknowledgement or (2) certain disregarded benefits. With respect to the latter, the final regulations delete the \$79 cap (the 2002 inflation-adjusted figure) found in the proposed regulations, so that benefits may be disregarded if the aggregate fair market value of all benefits provided to the payer (or persons designated by the payer) is not more than 2% of the payment. If the aggregate fair market value of the benefits exceeds 2%, then (except to the extent that the benefit constitutes an acknowledgment) the entire fair market value of such benefits, not merely the excess amount, is a substantial return benefit. Benefits to the payer (or persons designated by the payer) may include the following: advertising, exclusive provider arrangements; goods, facilities, services, or other privileges; and exclusive or non-exclusive rights to use an intangible asset (trademark, patent, logo, etc.) of the exempt organization.

### ***Use or Acknowledgement***

For purposes of section 513(i), a substantial return benefit does not include the use or acknowledgment of the name, logo, or product line of the payer's trade or business. Use or acknowledgment does not include advertising but may include the following: exclusive sponsorship arrangements; logos and slogans that do not contain qualitative or comparative descriptions of the payer's products, services, facilities, or company; a list of the payer's locations, telephone numbers, or Internet address; a value-neutral description, including displays or visual depictions, of the payer's product line or services; and the payer's brand or trade names and product or service listings. Logos or slogans that are an established part of the payer's identity are not considered to contain qualitative or comparative descriptions.

### ***Advertising***

For purposes of section 513(i), "advertising" means any message or other programming material that is broadcast or otherwise transmitted, published, displayed, or distributed, and that promotes or markets any trade, business, service, facility, or product. Advertising includes messages containing the following: qualitative or comparative language; price information or other indications of savings or value; an endorsement; or an inducement to purchase, sell, or use any company, service, facility or product. Mere display or distribution – whether for free or for a charge – of a payer's product to the general public at the sponsored activity is not considered an inducement to purchase, sell, or use the product. A single message with both advertising content and an acknowledgment is advertising. These provisions do not apply to activities a payer undertakes on its own (e.g. the purchase of broadcast time from a television station during commercial breaks in a sponsored program).

### ***Exclusivity Arrangements***

The final regulations adopt the distinction between an "exclusive sponsor" and an "exclusive provider" that was delineated in the proposed regulations. An arrangement that acknowledges a company as the exclusive sponsor (or the exclusive sponsor representing a particular business or industry) of an exempt organization activity does not, by itself, constitute a substantial return benefit. However, if the arrangement is an exclusive provider arrangement that limits the sale,

distribution, availability, or use of competing products in connection with the sponsored activity, the payer has received a substantial return benefit.

### ***Allocation of Payments***

The final regulations adopt a reasonable allocation rule. If an arrangement provides that a payer will receive substantial return benefit, only the portion, if any, of the payment that exceeds the FMV of the return benefit is a qualified sponsorship payment. The burden of establishing valuation is on the exempt organization. The final regulations clarify that the fair market value of the substantial return benefit generally is to be determined when the benefit is provided. However, if the parties enter into a binding, written sponsorship contract, the fair market value of any substantial return benefit provided pursuant to that contract is to be determined on the date the parties enter into the sponsorship contract (except in the case of material changes).

### ***Contingent Payments***

The amount of a qualified sponsorship payment may not be contingent, by contract or otherwise, on attendance at the exempt organization's event, on broadcast ratings, or on other indications of public exposure that would be typical of advertising. A qualified sponsorship payment may, however, be contingent on the sponsored activity's actually taking place.

***Public Support Determinations.*** Qualified corporate sponsorship payments in the form of money or property (but not services) will be considered as contributions for purposes of the public support tests of sections 170(b)(1)(A)(vi) and 509(a)(2) of the Code. However, this "contribution" classification with respect to the exempt organization does not determine whether the corporate sponsorship payment is deductible by the payer under section 162 as a business expense or under section 170 as a charitable contribution.

***Written Agreements.*** The final regulations maintain that neither the existence nor the detail of a written sponsorship agreement, by itself, disqualifies payment from classification as a qualified sponsorship payment.

***Sponsor Hyperlinks.*** For purposes of section 513(i), the final regulations address the issue of whether a hyperlink constitutes an acknowledgment or advertising in two new examples. In Example 11, a symphony orchestra maintains a website with information about its performance schedule. A music shop makes a payment to fund a concert series. The symphony posts a list of sponsors on its websites, including the music shop's name and Internet address, which appears as a hyperlink from the symphony's website to the music shop's website. The symphony's website does not promote or advertise the music shop. The entire payment by the music shop is a qualified sponsorship payment. The posting of its Internet address as a hyperlink does not constitute advertising.

In Example 12, a health-based charity sponsors a year-long program to educate the public about a particular medical condition. A drug company that produces a drug used in treating the condition provides funding for the program to help the charity produce educational materials and post information on its website, which contains a hyperlink to the drug company's website. The drug

company's website contains an endorsement by the charity of its drug, which was reviewed and approved in advance by the charity. The endorsement is advertising, the fair market value of which exceeds 2% of the total payment from the drug company to the charity. Thus, only the portion of the payment, if any, in excess of the fair market value of the advertising can be classified as a qualified sponsorship payment.

The preamble to the final regulations cautions that these two examples deal with hyperlinks in the section 513(i) context only and should not be relied upon with respect to the treatment of hyperlinks for purposes of other sections of the Code.

***Safe Harbor Application.*** The final regulations reiterate that the UBIT treatment of any payment or portion thereof that does meet the requirements for the qualified sponsorship payment safe harbor will be determined by application of the ordinary UBIT rules under sections 512, 513, and 514.

See Final Regulations on Taxation of Tax-Exempt Organizations' Income from Corporate Sponsorship, 67 Fed. Reg. 20433 (April 25, 2002).

### **2017 Tax Reform Changes**

On December 22, 2017, Congress enacted the bill commonly known as the Tax Cuts and Jobs Act of 2017. This act contained several provisions impacting the taxation of unrelated business income.

- **Tax rate:** For tax-exempt organizations structured as corporations, UBTI was previously taxed at the graduated corporate income tax rates ranging from 15% to 39%. Effective for tax years beginning after December 31, 2017, the corporate tax rate has changed to a flat 21%. For tax years including December 31, 2017, the two rate structures will be applied on a blended basis based on the number of days before and after December 31, 2017.
- **Activity basketing:** Under previous law, tax-exempt organizations with more than one UBI activity could net the income and losses from multiple activities to arrive at one net income or net loss figure. Effective for tax years beginning after December 31, 2017, each unrelated trade or business must be treated as a separate activity so that income and losses from each activity will stand on their own. This has been referred to as "basketing" or "siloing." In addition, in Notice 2018-67, the IRS provided preliminary guidance as to methodologies to appropriately determine an organization's activities. The notice provides that while any reasonable method may be used to make this determination, the NAICS classification system is one suggested method of defining separate activities. The Notice also provides a de minimis test, control test, and transitional rule that apply to certain investments in pass-through entities.
- **Qualified transportation fringe:** For amounts paid or incurred after December 31, 2017, the amount of certain fringe benefits provided by a tax-exempt employer to its employees is treated as an addition to UBTI. These amounts include qualified transportation fringes such as transit passes and bus passes, as well as qualified parking provided to employees. This provision is intended to mirror the impact to for-profit



employers, who are no longer to claim deductions for such fringe benefits. As of October 2018, the IRS has not provided guidance to determine with certainty how this new provision should be interpreted. The greatest uncertainty revolves around the potential taxation of parking provided to employees; until additional guidance is provided, organizations should consult with their tax advisors to discuss the potential impact to them.

- Net operating losses: Previous law provided that any net losses generated by UBI activities were able to be carried back to two previous tax years and carried forward 20 years. The new law provides that while pre-2018 net operating losses may continue to be carried forward and applied to the net income from any UBI activity, post 2017 losses (1) may only be used to offset income from the activity generating the loss, and (2) will only be allowed to offset 80% of the income from that activity. These post-2017 losses do not expire but carry forward indefinitely.

### **Other Tax Reform Changes**

In addition to the UBI changes, the TCJA added two excise taxes for tax-exempt organizations.

- Excess compensation: Effective for tax years beginning on or after January 1, 2018, IRC Section 4960 imposes a 21% excise tax on certain tax-exempt organizations when compensation paid to “covered employees” either exceeds \$1,000,000 or meets the requirements on an excess parachute payment. Covered employees are the top five highest-compensated employees in an organization. Once employees are designated as covered employees, they retain this status for all future years. Certain medical professionals are excluded from covered employee status.
- Private educational institutions: Certain private colleges and universities will be subject to a 1.4% excise tax on their net investment income for tax years beginning after December 31, 2017. Based on the definitions in IRC Section 4968, this tax will only apply to a small number of private institutions with large endowments. See also IRS Notice 2018-55 for interim guidance containing a transition rule on the calculation of recognized gains for purposes of this tax.

In addition, the TCJA suspended the deduction for moving expenses for taxable years beginning after December 31, 2017, and before January 1, 2026. This has the effect of making any employer payment or reimbursement of employee moving expenses treated as taxable compensation, since the expenses would not be deductible if borne directly by the employee.

### **Caveat**

The general information provided herein is not a substitute for specific legal advice. You should contact your diocesan tax/legal counsel for advice concerning the application of the tax law to particular fact situations.

## **XXI. School Tuition vs. Donation**

Payments made to a parish by parents of children enrolled in a Catholic school may qualify as deductible contributions if they are gifts, i.e. if they are voluntary transfers of funds made with no expectation of obtaining commensurate benefit. Specifically, enrollment in the school must in no manner be contingent on making the payment; the payment must not be made pursuant to a plan, whether express or implied, to convert nondeductible tuition into charitable contributions; and the receipt of the benefit, schooling or reduced tuition payments, must not otherwise be dependent upon such payment.

Rev. Rul. 83-104, 1983-2 C.B. 46, cites the following factors as creating a presumption that a payment is NOT a charitable contribution:

1. The existence of a contract, express or implied, whereby a taxpayer (i.e. parents, etc.) agrees to make a contribution and which ensures school admission for the taxpayer's child;
2. A plan allowing taxpayers either to pay tuition or make contributions in exchange for schooling;
3. The earmarking\* of contributions for the direct benefit of a particular individual; or
4. The otherwise unexplained denial of admission/readmission of children of taxpayers who are financially able but who do not contribute.

Additional adverse factors include:

5. The absence of a significant tuition charge;
6. Substantial or unusual (different from that applied to non-parents) pressure applied to parents of children attending school;
7. Contribution appeals made as part of the admissions or enrollment process;
8. The absence of significant school revenue sources other than parent contributions; and
9. Other factors suggesting a contribution policy created as a means of avoiding characterization of payments as tuition.

Situation 6 of Rev. Rul. 83-104 sanctions differential tuition for parishioners and non-parishioners in certain limited circumstances, as follows. This is a case in which there is no tuition to the parish school for parishioners, but non-parishioners are charged tuition. The parish receives contributions from all its members. These contributions are available to support all parish activities, a substantial portion of which are unrelated to the school. The parish has full control over the use of the contributions it receives. Most parish members do not have children in the school. The methods of soliciting contributions from parishioners with children in the school are the same as the methods of soliciting members without children in the school. In this situation, IRS concluded that the contributions made by parishioners with children in the school are ordinarily deductible, unless there is a showing that contributions by parishioners with children in the school are significantly larger than those of other parishioners. The IRS has indicated in other rulings that it will compare parental giving levels to non-parental giving levels in evaluating deductibility of payments. The test is whether the parish has full control of the donated funds, and discretion as to their use, to ensure that they will be used to carry out the parish's functions and purposes.

Any attempt to link school enrollment or tuition reductions/benefits to parish contributions or level of parish contributions jeopardizes the deductibility of contributions by parishioners who benefit from such practices. Various labels given to parish contributions, e.g. sacrificial giving, tithing, negotiated tuition, stewardship, minimum giving, etc., are not determinative of deductibility. Further, parishes cannot qualify under Situation 6 by defining parish membership or otherwise qualifying for reduced or no tuition, according to level of contribution. All such practices undercut parish claims that parish contributions are gifts, the *sine qua non* of charitable deductibility.

Schools should adopt a policy for determining eligibility for financial aid and tuition reductions. Factors which may be considered in determining eligibility for tuition reductions/benefits include:

- Being registered in the parish, and attending Mass regularly
- Participating in parish life with time and talent

It is important for the parish to clearly communicate the determinative factors to parents of children attending Catholic schools.

Finally, to keep offertory contributions from families with children attending Catholic schools from being misinterpreted as tuition, the parish should not treat these families differently than other parish families. Tracking what school families give compared to non-school families or soliciting time and talent information only from school families are examples of some of the actions that could lead to a determination that payments from these families are tuition and not charitable contributions.

Generally, contributions earmarked by a donor for a particular individual are treated as gifts to the designated individual and are not deductible. However, a deduction will be allowed if it is established that the gift is intended by the donor for the use of the charitable organization. The test is whether the organization has full control of the donated funds, and discretion as to their use, to ensure that they will be used to carry out the charitable organization's functions and purposes. See Revenue Ruling 62-113, 1962-1 C.B. 10.

**Note:**

Tripp v. Commissioner, 337 F.2d 432 (7<sup>th</sup> Cir. 1964), the court held that payments made to an educational institution and earmarked for the educational expenses of a particular individual were not deductible because they were neither made to the college for use as it saw fit nor made for the benefit of an indefinite number of persons, as, for example, a scholarship fund.

## **Appendix A – Financial Statements and Notes – Samples**

The following Accounting Standards Codification subtopics establish standards for general purpose external financial statements provided by a not-for-profit entity:

- a. ASC 958-205: Presentation of Financial Statements

- b. ASC 958-219: Balance Sheet
- c. ASC 958-225: Income Statement
- d. ASC 958-230: Statement of Cash Flows

Even though ASC Topic 958 specifies certain requirements, including the classification of net assets based upon the existence or absence of donor-imposed restrictions, it does allow the organization a certain degree of flexibility in their presentation of financial information.

In that context, the following links are provided to actual financial statements issued by various dioceses based upon various factors including, size of the diocesan population, geographic location, and function of diocesan entity. The links to financial statements included herein address the myriad of functions that various diocesan administrations oversee and administer, such as, Catholic Charities, a deposit and loan corporation, cemeteries, foundations, and other related organizations. The appendix is designed to be used as a guide to various financial statement presentation and disclosure options for similar entities within dioceses.

#### **LARGE DIOCESES:**

*Archdiocese of Chicago*

[https://www.archchicago.org/news\\_releases/annual\\_report.shtm](https://www.archchicago.org/news_releases/annual_report.shtm)

*Diocese of Orange*

[https://www.rcbo.org/wp-content/uploads/RCBO\\_Financial\\_Audit\\_FY14\\_Final.pdf](https://www.rcbo.org/wp-content/uploads/RCBO_Financial_Audit_FY14_Final.pdf)

#### **MEDIUM DIOCESES:**

*Diocese of Davenport*

<https://www.davenportdiocese.org/finance-human-resources>

*Archdiocese of Kansas City (Kansas)*

<https://www.archkck.org/finance>

#### **SMALL DIOCESES:**

*Diocese of Boise*

<https://www.catholicidaho.org/finance>

*Diocese of Salt Lake City*

<https://www.dioslc.org/ministries/finance-office>

## **Appendix B – Resources**

**American Institute of Certified Public Accountants (AICPA)** – Promulgates auditing standards for CPAs in the United States and is also a source of additional guidance on application of

accounting standards. Includes the Accounting Standards Executive Committee (AcSEC). Website: <http://www.aicpa.org>. Address: 1211 Avenue of the Americas, New York, NY 10036.

**Association of Certified Fraud Examiners** – Offers resources to help organizations implement fraud protection environment and measures to reduce risk of fraud. Website: <http://www.acfe.com>.

**Canon Law Society of America (CLSA)** – A professional association whose members are dedicated to the promotion of the study and application of canon law in the Roman Catholic Church. Website: <http://www.clsa.org/>. Address: 415 Michigan Ave., NE, Suite 101, Washington, DC 20017.

**Conference for Catholic Facility Management (CCFM)** – Provides a forum and a network for persons having responsibility for diocesan or religious-owned buildings and/or properties. Website: <http://www.ccfm.net>. Address: 20 Archbishop May Dr., St. Louis, MO, 63119.

**Church Law & Tax Report** – A review of legal and tax developments affecting ministers and churches. Published bimonthly by Christianity Today. Website: <http://www.churchlawandtax.com/>. Address: 465 Gundersen Drive, Carol Stream, IL 60188.

**Diocesan Fiscal Management Conference (DFMC)** – Provides fiscal and administrative expertise and professional services to the local and national Church. Website: <http://www.dfmconf.org>. Address: 4727 East Bell Road, Suite 45-358, Phoenix, AZ 85032.

**Diocesan Information Systems Conference (DISC)** – Maintains an up-to-date listing of financial and other software used by member dioceses throughout the United States. Website: <http://www.discinfo.org>.

**Ethics and Compliance Initiative** – Provides expertise and services to strengthen ethical leadership. Website: <http://www.ethics.org>.

**Financial Accounting Standards Board (FASB)** – Promulgates accounting standards for nonprofit and commercial entities in the United States. Source for Statements of Financial Accounting Standards (SFAS). Website: <http://www.fasb.org>. Address: 401 Merritt 7, P.O. Box 5116, Norwalk, CT 06856-5116.

**Foundations and Donors Interested in Catholic Activities (FADICA)** – An association of independent foundations with interests in projects under Catholic sponsorship. Website: <http://www.fadica.org/main/>. Address: 4201 Connecticut Avenue NW, Suite 505, Washington, DC 20008.

**Institute of Management Accountants** – Predominately for “for-profit” organizations, but, their financial management resources still recommended for use in most dioceses. Website: <http://www.imanet.org>.

**Internal Revenue Service (IRS)** – Offers Publication 517, *Social Security and Other Information for Members of the Clergy and Religious Workers*, and Publication 1828 *Tax Guide for Churches and Religious Organizations* as well as other publications. Website: <http://www.irs.gov>.

**Information Systems Audit and Control Association** – Offers resources to aid in automated systems environment, structure and controls. Website: <http://www.isaca.org>.

**National Association of Church Personnel Administrators (NACPA)** – Offers resources for use in church personnel management. Website: <http://www.nacpa.org>. Address: 2050 Ballenger Ave., Suite 200, Alexandria, VA 22314.

**Resource Center for Religious Institutes (RCRI)** – Created to serve the needs of Catholic Communities of religious men and women. Navigates complexities related to taxes and tax exemption, corporate structure, internal organization set-up, finance, administration and canon law. Website: <http://www.trcri.org>. Address: 8824 Cameron St., Silver Spring, MD 20910.

**Shepherds Advisor** -- Offers *Income Taxes for Priests Only* by Scott A. Hoselton, CPA, CDFM. Website: <http://shepherdsadvisor.org>. Address: 5600 Bishops Blvd S, Fargo, ND 58104.

**Society for Human Resource Management** – Offers resources for use in personnel management. Website: <http://www.shrm.org>.

**Thomson Reuters (f/k/a PPC)** – Offers a variety of publications, including *Guide to Preparing Nonprofit Financial Statements*, *990 Deskbook*, and *Audits of Nonprofit Organizations*. Website: <https://tax.thomsonreuters.com/products/brands/checkpoint/ppc/>

**United States Conference of Catholic Bishops (USCCB)** – Offers this manual and *Diocesan Internal Controls: A Framework* (available from USCCB Publishing), as well as a variety of resources from the Office of General Counsel. Website: <http://www.usccb.org>. Address: 3211 Fourth Street NE, Washington, DC 20017-1194. Phone: USCCB Publishing, 800-235-8722; OGC or other offices, 202-541-3000.

**United States Office of Management and Budget (OMB)** – Issues rules for entities receiving federal assistance and for audits of those entities. Website: <http://www.whitehouse.gov/omb/>. Address: 725 17<sup>th</sup> Street NW, Washington, DC 20503.