

**DIOCESE OF WINONA-
ROCHESTER
(Debtor in Possession)**

**FINANCIAL STATEMENTS WITH
INDEPENDENT AUDITORS' REPORT**

JUNE 30, 2021

**DIOCESE OF WINONA-ROCHESTER
(Debtor in Possession)**

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INDEPENDENT AUDITORS' REPORT

To the Finance Council
Diocese of Winona-Rochester (Debtor in Possession)
Winona, Minnesota

We have audited the accompanying financial statements of the Diocese of Winona-Rochester (Debtor in Possession) (a nonprofit organization) (the "Diocese"), which comprise the statement of financial position as of June 30, 2021, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Diocese of Winona-Rochester (Debtor in Possession) as of June 30, 2021, and the changes in its net assets, and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Substantial Doubt About the Diocese's Ability as a Going Concern

As discussed in Note 1 to the financial statements, the Diocese of Winona-Rochester (Debtor in Possession) filed a petition for relief under Chapter 11 of the bankruptcy law. The accompanying financial statements have been prepared assuming that the Diocese will continue as a going concern. As discussed in Note 2 to the financial statements, the Diocese has been named as a defendant in several lawsuits that raise substantial doubt about its ability to continue as a going concern. Management's evaluation of the events and conditions and management's plans regarding those matters also are described in Note 2. Our opinion is not modified with respect to this matter.

Report on Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The Statement of Activities by Department on page 20 is presented for purpose of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The budget information included in the financial statements on pages 5 and 20, which are of a nonaccounting nature, have not been subjected to the auditing procedures applied in the audit of the financial statements, and, accordingly, we do not express an opinion or provide any assurance on it.

Hawkins Ash CPAs, LLP

La Crosse, Wisconsin
October 19, 2021

**DIOCESE OF WINONA-ROCHESTER
(Debtor in Possession)**

FINANCIAL STATEMENTS

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
 STATEMENT OF FINANCIAL POSITION
 JUNE 30, 2021

ASSETS

Cash and cash equivalents	\$ 17,066,097
Accounts receivable	300,091
Loan receivable	692,174
Prepaid expenses	269,117
Restricted cash and cash equivalents	280,075
Investments	5,298,011
Beneficial interest in trusts	488,561
Property and equipment, net	<u>999,106</u>
TOTAL ASSETS	<u>\$ 25,393,232</u>

LIABILITIES AND NET ASSETS

LIABILITIES NOT SUBJECT TO COMPROMISE

Accounts payable	
Vendors and others	\$ 670,440
Charitable organizations	114,867
Funds held for others	12,946
Accrued expenses	<u>18,585,066</u>
TOTAL LIABILITIES NOT SUBJECT TO COMPROMISE	19,383,319

LIABILITIES SUBJECT TO COMPROMISE

Accounts payable	
Vendors and others	<u>10,779</u>
TOTAL LIABILITIES	<u>19,394,098</u>

NET ASSETS

Without donor restrictions	1,781,222
With donor restrictions	<u>4,217,912</u>
TOTAL NET ASSETS	<u>5,999,134</u>

TOTAL LIABILITIES AND NET ASSETS	<u>\$ 25,393,232</u>
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The accompanying notes are an integral part of these statements.

DIOCESE OF WINONA-ROCHESTER
(Debtor in Possession)
STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2021

	WITHOUT DONOR RESTRICTIONS	WITH DONOR RESTRICTIONS	TOTAL	BUDGET
REVENUE, GAINS, AND OTHER SUPPORT				
Diocesan tax	\$ 1,733,745	\$ -	\$ 1,733,745	\$ 1,733,228
Contributions and bequests	623,893	22,314	646,207	342,001
Interest and dividends, net of fees	95,188	19,619	114,807	14,000
Net realized and unrealized gain on investments	783,387	493,661	1,277,048	324,000
Departmental, including CMA case statement disbursements of \$1,526,000	2,223,958	-	2,223,958	2,542,352
General diocesan, including CMA case statement disbursements of \$628,418	668,119	-	668,119	615,300
Self insurance	2,395,165	-	2,395,165	2,236,460
Other	10,583	-	10,583	600
Net assets released from restrictions	74,977	(74,977)	-	-
TOTAL REVENUE, GAINS, AND OTHER SUPPORT	8,609,015	460,617	9,069,632	7,807,941
EXPENSES				
Program	5,589,387	-	5,589,387	
Management and general	579,618	-	579,618	
Fundraising	211,942	-	211,942	
TOTAL EXPENSES	6,380,947	-	6,380,947	9,507,941
CHANGE IN NET ASSETS BEFORE REORGANIZATION ITEMS	2,228,068	460,617	2,688,685	
REORGANIZATION ITEMS				
Professional fees	1,797,591	-	1,797,591	
Settlement losses	18,125,000	-	18,125,000	
Miscellaneous	49,589	-	49,589	
TOTAL REORGANIZATION ITEMS	19,972,180	-	19,972,180	
CHANGE IN NET ASSETS	(17,744,112)	460,617	(17,283,495)	\$ (1,700,000)
NET ASSETS AT BEGINNING OF YEAR	19,525,334	3,757,295	23,282,629	
NET ASSETS AT END OF YEAR	\$ 1,781,222	\$ 4,217,912	\$ 5,999,134	

The accompanying notes are an integral part of these statements.

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
STATEMENT OF FUNCTIONAL EXPENSES
 YEAR ENDED JUNE 30, 2021

	<u>PROGRAM</u>	<u>MANAGEMENT AND GENERAL</u>	<u>FUNDRAISING</u>	<u>TOTAL</u>
Labor and benefits	\$ 1,999,443	\$ 484,124	\$ 31	\$ 2,483,598
Professional expenses	318,691	23,397	143,338	485,426
Office expenses	111,615	49,143	1,558	162,316
Program material expenses	25,071	658	66,969	92,698
Local travel expenses	39,771	603	-	40,374
Professional conference expenses	4,178	826	-	5,004
Diocesan meeting expenses	300,313	166	-	300,479
Insurance premiums	1,559,722	-	-	1,559,722
Care of Priests	2,786	-	-	2,786
Liturgical expenses	74,030	-	-	74,030
Membership assessments	159,390	-	-	159,390
Mission support	311,913	-	-	311,913
Seminarian education	501,261	-	-	501,261
Depreciation	48,670	18,099	-	66,769
Miscellaneous	132,533	2,602	46	135,181
TOTAL EXPENSES BEFORE REORGANIZATION ITEMS	<u>5,589,387</u>	<u>579,618</u>	<u>211,942</u>	<u>6,380,947</u>
Professional expenses	-	1,797,591	-	1,797,591
Settlement losses	-	18,125,000	-	18,125,000
Miscellaneous	-	49,589	-	49,589
TOTAL REORGANIZATION ITEMS	<u>-</u>	<u>19,972,180</u>	<u>-</u>	<u>19,972,180</u>
TOTAL EXPENSES AFTER REORGANIZATION ITEMS	<u>\$ 5,589,387</u>	<u>\$ 20,551,798</u>	<u>\$ 211,942</u>	<u>\$ 26,353,127</u>

The accompanying notes are an integral part of these statements.

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
STATEMENT OF CASH FLOWS
 YEAR ENDED JUNE 30, 2021

CASH FLOWS FROM OPERATING ACTIVITIES	
Change in net assets	\$ (17,283,495)
Adjustments to reconcile change in net assets to net cash provided by operating activities	
Depreciation	66,769
Net realized and unrealized (gain) on investments	(1,277,048)
Allowance for doubtful accounts	(9,962)
Changes in assets and liabilities	
(Increase) decrease in assets	
Accounts receivable	(4,265)
Prepaid expenses	34,630
Increase in liabilities	
Accounts payable	491,002
Charitable organizations (collections and transmittals)	87,759
Funds held for others	4,224
Accrued expenses	18,253,052
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>362,666</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchases of property and equipment	(23,756)
Purchases of investments	(1,500,310)
Proceeds from sale of investments	3,747,431
Payments on loan receivables	94,958
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>2,318,323</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	2,680,989
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>14,665,183</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 17,346,172</u>
<u>RECONCILIATION OF CASH AND CASH EQUIVALENTS AND RESTRICTED CASH AND AND CASH EQUIVALENTS PER STATEMENT OF CASH FLOWS TO THE STATEMENT OF FINANCIAL POSITION</u>	
Cash and cash equivalents	\$ 17,066,097
Restricted cash and cash equivalents	<u>280,075</u>
TOTAL CASH AND CASH EQUIVALENTS SHOWN IN THE STATEMENT OF CASH FLOWS	<u>\$ 17,346,172</u>
<u>SUPPLEMENTAL CASH FLOWS DISCLOSURE</u>	
Cash paid for reorganization items	<u>\$ 1,353,752</u>

The accompanying notes are an integral part of these statements.

DIOCESE OF WINONA-ROCHESTER
(Debtor in Possession)
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2021

NOTE 1 - Petition for Relief Under Chapter 11

On November 30, 2018, the Diocese of Winona-Rochester (the "Diocese") (the Debtor in Possession) filed a petition for relief under Chapter 11 of the United States bankruptcy laws in the United States Bankruptcy Court for the District of Minnesota. Under Chapter 11, certain claims against the Debtor in existence before the filing of the petitions for relief under the federal bankruptcy laws are stayed while the Debtor continues business operations as Debtor in Possession. These claims are reflected in the June 30, 2021 statement of financial position as liabilities subject to compromise. Additional claims (liabilities subject to compromise) may arise after the filing date resulting from rejection of executory contracts, including leases, and from the determination by the court (or agreed to by parties in interest) of allowed claims for contingencies and other disputed amounts.

NOTE 2 - Going Concern

The Diocese is a Defendant in a number of asserted claims alleging personal injury damages arising out of alleged sexual misconduct by former employees of the Diocese. The Plaintiffs are seeking compensatory remuneration from the Diocese in connection with these asserted claims. On October 14, 2021, the U.S. Bankruptcy Court ordered approval of the Diocese's Plan of Reorganization (the "Plan"). The Plan requires that the Diocese fund a settlement Trust that will not exceed \$22,056,000, less certain bankruptcy expenses already paid, and yet to be paid, by the Diocese. Estimated losses in connection with these asserted claims have been accrued in accordance with the Contingencies Topic of the FASB Accounting Standards Codification ("ASC 450"). Under ASC 450, estimated losses shall be accrued by a charge to income when it is probable that a liability has been incurred and the amount can be reasonably estimated. Changes in accounting estimates are recorded in the year of the change. As of June 30, 2021, the Organization has accrued losses to fund the settlement trust of \$18,125,000.

49 personal injury tort claims remain unsettled. These tort claims will be litigated in State District Court, in the event that the tort claimant chooses to pursue litigation and forgo settlement from the Trust established by the Plan. The Diocese liability regarding these tort claims is non-recourse in nature and limited only to insurance coverage, including, but not limited to, primary coverage, excess indemnity coverage, and umbrella policies. Management has contacted the insurance companies to determine what claims are covered by insurance. A declaratory judgment action (Dec Action) has been initiated in the Federal District Court. The Dec Action seeks to clarify the coverage applicable to the tort claimants and indemnification of Diocesan liability. The Diocese continues to meet with counsel for the Plaintiffs and coverage counsel for the insurance companies to seek resolution of the unliquidated tort claim liability.

Due to the circumstances described above, there is substantial doubt about the Diocese's ability to continue as a going concern. Management continues to look to reduce expenses, yet maintain essential ministries and operations of the Diocese of Winona-Rochester (Debtor in Possession). The ability to continue as a going concern is dependent upon unsettled personal injury tort claims, and the Diocese ability to raise funds and liquidate assets.

DIOCESE OF WINONA-ROCHESTER
(Debtor in Possession)
NOTES TO THE FINANCIAL STATEMENTS - Continued
JUNE 30, 2021

NOTE 3 - Nature of Organization and Significant Accounting Policies

Nature of Organization - The Diocese is a religious corporation formed under the laws of the State of Minnesota. The purpose of the Diocese is to promote the spiritual, educational and other interests of the Catholic Church within the Diocese and to manage the temporal affairs of the Roman Catholic Church in fulfilling that mission. The Diocese through administrative offices serves other Diocesan entities within the territorial limits of the Diocese of Winona-Rochester (Debtor in Possession). The territorial limits are comprised of the following counties in the State of Minnesota: Winona, Wabasha, Olmsted, Dodge, Steele, Waseca, Blue Earth, Watonwan, Cottonwood, Murray, Pipestone, Rock, Nobles, Jackson, Faribault, Martin, Freeborn, Mower, Fillmore and Houston. The Diocese is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code.

Basis of Accounting -The financial statements of the Diocese have been prepared on the accrual basis of accounting and accordingly reflect all significant receivables, payables, and other liabilities. The accompanying financial statements include the administrative offices of the Diocese of Winona-Rochester (Debtor in Possession) as shown in the supplementary information to the financial statements conducted at the Diocesan Pastoral Center. Other Diocesan entities within its territorial limits are separately incorporated and are not included in the financial statements. All interdepartmental transactions have been eliminated.

Basis of Presentation - The accompanying financial statements are prepared in accordance with the accounting principles generally accepted in the United States of America (U.S. GAAP) as codified by the Financial Accounting Standards Board.

The Diocese is required to report information regarding its net assets and its activities based on the existence or absence of donor or grantor imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

- *Net Assets Without Donor Restrictions* - Net assets available for use in general operations and not subject to donor restrictions. The governing board has designated, from net assets without donor restrictions, net assets for an operating reserve, scholarship funds, capital improvement funds, and certain retirement funds.
- *Net Assets With Donor Restrictions* - Net assets subject to donor imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both.

Cash and Cash Equivalents - The Diocese's cash and cash equivalents consists of cash on deposit with banks and a money market account. For purposes of the statements of cash flows, the Diocese considers all unrestricted, highly liquid investments with an initial maturity of three months or less to be cash equivalents.

Restricted Cash - Certain donor-restricted assets that meet the definition of cash and cash equivalents that have donor-imposed restrictions limiting their use to long-term purposes are classified as restricted cash, as well as worker's compensation deposits, in the statement of financial position.

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
 NOTES TO THE FINANCIAL STATEMENTS - Continued
 JUNE 30, 2021

NOTE 3 - Nature of Organization and Significant Accounting Policies - Continued

Accounts Receivable - Receivables are stated at the amount management expects to collect from outstanding balances. Management provides for uncollectible amounts through a provision for bad debt expense and an adjustment to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge of the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements. Allowance for doubtful accounts at June 30, 2021 was \$-0-. Bad debt recovery for the year ended June 30, 2021 was \$9,962.

Loans Receivable - During 2015, the Diocese purchased a loan portfolio from the Diocese of Winona-Rochester Deposit and Loan Fund. All loans have been repaid with the exception of the one loan to a Diocesan parish. The loan is stated at the amount of unpaid principal. The loan is collateralized by the assets of the parish. Interest on the loan is recognized over the term of the loan and is calculated using the simple interest method on principal amounts outstanding. The interest rate, which is subject to change by approval of the Finance Council, was 3.40 percent as of June 30, 2021. The balance as of June 30, 2021, was \$692,174.

Investments - Investments are reported at cost, if purchased, or at fair value, if donated. Thereafter, investments are reported at their fair values in the statement of financial position.

The aggregate of (a) the unrealized appreciation (depreciation) in the fair value of investments during the year (b) the realized gains (losses) on sales of investments during the year (c) dividend income (d) interest income, and (e) investment fees are reflected in investment return on the statement of activities.

Purchases and sales of securities are recorded on a trade-date basis. Gains and losses on sales of securities are based on average cost and are recorded in the statement of activities in the period in which the securities are sold. Dividends are recorded on the ex-dividend date.

Donated Assets - Donated marketable securities and other noncash donations are recorded as contributions at their estimated fair values at the date of donation.

Property and Equipment - Land, buildings, vehicles, and equipment are recorded at purchased cost or fair value at the date of gift if donated. The Diocese has recorded depreciation on the buildings, furnishing, automobiles, and equipment using the straight-line method over the estimated useful lives of 3 to 40 years.

<u>Asset</u>	<u>Life</u>
Furniture, fixtures, and equipment	3 - 10 years
Vehicles	5 - 7 years
Land improvements	10 - 20 years
Buildings	40 years

Valuation of Long-lived Assets - U.S. GAAP requires that long-lived assets and certain identifiable intangible assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Management reviews all material assets annually for possible impairment. If such assets are considered to be impaired, the impairment recognized is measured as the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. No assets are considered to be impaired at June 30, 2021.

DIOCESE OF WINONA-ROCHESTER
(Debtor in Possession)
NOTES TO THE FINANCIAL STATEMENTS - Continued
JUNE 30, 2021

NOTE 3 - Nature of Organization and Significant Accounting Policies - Continued

Funds Held For Others - Funds held for others represent cash collected on behalf of other Catholic organizations and programs by the Diocese which have not yet been disbursed.

Self-Insurance - The Diocese, both for itself and as the agent for parishes and other Catholic entities operating within the territorial limits of the Diocese (the "Members"), participates in a liability, property, casualty and worker's compensation self-insurance program. The Members pay an annual premium based on various criteria to cover their portion of the cost of this program. The Diocese contracts with Catholic Mutual as an insurance broker to purchase self-insurance coverage on behalf of itself and the other Members and to act as risk manager. The Diocese administers the insurance program by collecting the premiums from the Members and arranging for the payment of claims as they are incurred. The Diocese is self-insured for \$100,000 per claim with an annual aggregate exposure of \$400,000 for the year ended June 30, 2021.

Diocesan Tax - Each parish within the Diocese is assessed a tax. The tax is based on a percentage of parish support in prior years. Revenue is recorded in the period the tax is assessed.

Catholic Ministries Appeal (CMA) - Annually, the Catholic Foundation of Southeastern Minnesota conducts the Catholic Ministries Appeal on behalf of the Diocese of Winona-Rochester (Debtor in Possession) to support specific ministries and programs of the Diocese and other Catholic organizations. The Foundation distributes these funds to the Diocese to be allocated to these individual ministries according to the campaign case statement. These contributions are reflected in Departmental revenue and General diocesan revenue in the statement of activities. Catholic Ministries Appeal distributions to the Diocese totaled \$2,154,418 for the year ended June 30, 2021.

Contributed Services - Services of the clergy and religious orders have been recognized only to the extent of actual compensation paid. No computation is made for the difference between the compensation paid to these employees and the comparable compensation which would be paid to lay personnel.

Revenue Recognition: The Diocese records the following exchange transaction revenue in its statements of activities and changes in net assets:

Program Fees: The Diocese offers various programs, workshops and seminars for which program fees are charged. The performance obligation is the delivery of the program. Program fees are billed at the time of registration and recognized as earned. The unearned portion is included as deferred revenue.

Contribution Recognition - Contributions are recognized when received or unconditionally pledged. Contributions received are recorded as net assets without donor restrictions or net assets with donor restrictions depending on the existence and/or nature of any donor restrictions.

Contributions restricted by donors are reported as increases in net assets without donor restrictions if the restrictions expire in the reporting period in which the revenue is recognized. All other donor-restricted contributions are reported as increases in net assets with donor restrictions, depending on the nature of the restrictions.

Functional Allocation of Expenses - The costs of providing various programs and other activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the program services and supporting activities benefited. Those expenses include occupancy and depreciation, which are allocated on a square footage basis, as well as salaries and wages, benefits, payroll taxes, professional services and certain office expenses, which are allocated based on estimates of time and usage.

DIocese OF WINONA-ROCHESTER
(Debtor in Possession)
NOTES TO THE FINANCIAL STATEMENTS - Continued
JUNE 30, 2021

NOTE 3 - Nature of Organization and Significant Accounting Policies - Continued

Use of Estimates - Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenue and expenses. Actual results could differ from those estimates.

Tax Status - The Diocese is exempt from Federal income tax under Section 501(c)(3) of the Internal Revenue Code (IRC). However, income from certain activities not directly related to the Diocese's tax-exempt purpose is subject to taxation as unrelated business income.

Accounting for Uncertainty in Income Taxes - U.S. GAAP requires management to evaluate tax positions taken by the Diocese and recognize a tax liability (or asset) if the Diocese has taken an uncertain position that more likely than not would not be sustained upon examination by a taxing authority. Management has analyzed the tax positions taken by the Diocese, and has concluded that as of June 30, 2021, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements. The Diocese is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. The Diocese will recognize future accrued interest and penalties related to unrecognized tax benefits in income tax expense if incurred.

Subsequent Events - The Diocese evaluated subsequent events through October 19, 2021, the date which the financial statements were available to be issued.

NOTE 4 - Concentration of Cash and Credit Risk

The Diocese may have deposits with a financial institution at times during the year that exceed the Federal Deposit Insurance Corporation (FDIC) insurance threshold of \$250,000. The Diocese's deposits at June 30, 2021 did exceed the FDIC insurance threshold; however, the Diocese has sufficient collateral or other security to support deposits subject to this credit risk.

NOTE 5 - Liquidity and Availability

As stated in Note 1, the Diocese is currently in Chapter 11 bankruptcy proceedings and therefore, all expenditures of the Diocese are subject to review by the court.

Liquidity Management

The Diocese manages its liquidity and reserves following three guiding principles: operating within a prudent range of financial soundness and stability, maintaining adequate liquid assets to fund near-term operating needs, and maintaining sufficient reserves to provide reasonable assurance that long-term obligations will be discharged. The Diocese has a liquidity policy to maintain current financial assets less current liabilities at a minimum of 30 days operating expenses. In addition, the Diocese has a policy to target a year-end balance of reserves of net assets without donor restrictions and, undesignated net assets to meet 15 to 30 days of expected expenditures. To achieve these targets, the Diocese forecasts its future cash flows, monitors its liquidity quarterly, and monitors its reserves annually. During the year ended June 30, 2021, the level of liquidity and reserves was managed within the policy requirements.

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
 NOTES TO THE FINANCIAL STATEMENTS - Continued
 JUNE 30, 2021

NOTE 6 - Investments and Endowment Funds

The following is a summary of investment at June 30, 2021:

	<u>COST</u>	GROSS UNREALIZED <u>GAINS</u>	GROSS UNREALIZED <u>LOSSES</u>	<u>FAIR VALUE</u>
Common/collective trust funds	\$ 3,759,349	\$ 1,366,749	\$ -	\$ 5,126,098
Private equity investments	<u>419,775</u>	<u>10,011</u>	<u>(257,873)</u>	<u>171,913</u>
TOTAL INVESTMENTS AND ENDOWMENT FUNDS	<u>\$ 4,179,124</u>	<u>\$ 1,376,760</u>	<u>\$ (257,873)</u>	<u>\$ 5,298,011</u>

The following schedule summarizes investment returns as of June 30, 2021:

Unrealized losses	\$ (306,234)
Realized gains	1,583,282
Investment income, less fees	<u>52,877</u>
TOTAL INVESTMENT RETURN	1,329,925
Interest income, net of bank fees	<u>61,930</u>
TOTAL	<u>\$ 1,391,855</u>

NOTE 7 - Beneficial Interests in Charitable Remainder Trusts

The Diocese has been named a beneficiary of a split-interest agreement. Upon the death of the beneficiaries, the Diocese will receive 5 percent of the remainder of the trusts fair market value. The balance in the beneficial interest in the Charitable Remainder Trusts as of June 30, 2021 is \$28,460.

The Diocese has been named a beneficiary of a split-interest agreement in land. The Diocese owns the property subject to a life estate. Upon the death of the beneficiary, the Diocese will receive their portion of the remainder of the trust's fair market value. The balance of this remainder interest as of June 30, 2021 is \$460,101.

NOTE 8 - Property and Equipment

Property and equipment include all properties which are owned by the Diocese. A summary of property and equipment as of June 30, 2021, is as follows:

Land	\$ 596,970
Buildings and furnishings	1,515,079
Automobiles and equipment	<u>510,409</u>
	2,622,458
Less: Accumulated depreciation	<u>(1,623,352)</u>
NET PROPERTY AND EQUIPMENT	<u>\$ 999,106</u>

Values assigned to certain property, other than property acquired after 1979 which has been recorded at cost, were obtained from insurance appraisals performed during 1979. The amounts above represent 1979 depreciated replacement cost, plus subsequent additions less retirements at cost. This method is not in conformity with accounting principles generally accepted in the United States of America. The difference in the amount measured by depreciated replacement cost and methods required by generally accepted accounting principles as of June 30, 2021 is not material. Depreciation expense was \$66,769 for the year ending June 30, 2021.

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
 NOTES TO THE FINANCIAL STATEMENTS - Continued
 JUNE 30, 2021

NOTE 9 - Fair Value Measurements

The Diocese has determined the fair value of certain assets and liabilities in accordance with the provision of U.S. GAAP, which provides a framework for measuring fair value under generally accepted accounting principles.

U.S. GAAP defines fair value as the exchange price that would be received for an asset in the principal or most advantageous market for the asset in an orderly transaction between market participants on the measurement date. U.S. GAAP requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs. U.S. GAAP also establishes a fair value hierarchy, which prioritizes the valuation inputs into three broad levels.

Level 1 inputs consist of quoted prices in active markets for identical assets that the reporting organization has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the related asset. Level 3 inputs are unobservable inputs related to the asset.

The asset's fair value measurement within the fair value hierarchy is based on the lowest of any input that is significant to the fair value measurement. The following is a description of the valuation methodologies used for assets measured at fair value:

Common/Collective Trust Funds: Valued at net asset value (NAV) of shares held by the Diocese at year end.

Private Equity Investments: Valued at the estimated fair value of the underlying assets and consist of the Diocese's investments in the Catholic Umbrella Pool and the National Catholic Risk Retention Group which are restricted. The Diocese must provide 180 day notice before they can be liquidated.

Beneficial Interest in Trusts: Valued at the estimated fair value of the underlying trust assets.

The methods described above may produce a fair value calculation that may be indicative of net realizable value or reflective of future fair values. Furthermore, while the Diocese believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table sets forth by level, within the fair value hierarchy, the Diocese's assets at fair value on a recurring basis as of June 30, 2021.

	JUNE 30, 2021	QUOTED PRICES IN ACTIVE MARKETS FOR IDENTICAL ASSETS (LEVEL 1)	SIGNIFICANT OTHER OBSERVABLE INPUTS (LEVEL 2)	SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)
Investment in marketable securities				
Common/collective trust funds	\$ 5,126,098	\$ -	\$ 5,126,098	\$ -
Private equity investments	171,913	-	-	171,913
Beneficial interest in trusts	488,561	-	-	488,561
TOTAL	\$ 5,786,572	\$ -	\$ 5,126,098	\$ 660,474

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
 NOTES TO THE FINANCIAL STATEMENTS - Continued
 JUNE 30, 2021

NOTE 9 - Fair Value Measurements - Continued

The following is a reconciliation of activity for assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3 inputs):

Private Equity Investments

Fair value at beginning of year	\$ 160,921
Market value gains and adjustments	10,992
FAIR VALUE AT END OF YEAR	<u>\$ 171,913</u>

Beneficial Interest in Trusts

Fair value at beginning of year	\$ 488,561
Increase (decrease) in fair value of trusts	-
FAIR VALUE AT END OF YEAR	<u>\$ 488,561</u>

NOTE 10 - Net Assets

Included in net assets without donor restrictions are amounts designated by the board for the following purposes at June 30, 2021:

Capital improvements	\$ 409,500
Quasi endowment - Scholarship funds	187,428
Retirement funds	70,000
Operating reserve	125,000
Student loan and scholarship funds	173,400
TOTAL DESIGNATED NET ASSETS	<u>\$ 965,328</u>

The Diocese's Board of Directors has created an operating reserve which sets aside cash for operating expenses to be drawn upon in the event of financial distress or an immediate liquidity need.

Net assets with donor restrictions are restricted for the following purposes or periods at June 30, 2021:

Subject to expenditure for specified purpose:

Schulze Foundation	\$ 73,500
Handicapped Children Fund	9,774
Works of Justice Fund	41,172
Rice Bowl Poverty Program	31,796
Hullerman Fund	91,566
Priests' Retirement Fund	38,728
Education of Seminarians	254,250
Continuing education of priests	128,234
Training of lay leaders/ministers	68,928
Catholic Education	25,264
	<u>763,212</u>

Subject to the passage of time:

Poire land interest	460,101
Beneficial interest in gift annuity	28,460
	<u>488,561</u>

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
 NOTES TO THE FINANCIAL STATEMENTS - Continued
 JUNE 30, 2021

NOTE 10 - Net Assets - Continued

Endowments	
Amount required to be held in perpetuity	
Seminarian education	\$ 1,610,676
McHugo fund (income to help the poor and needy)	233,501
	<u>1,844,177</u>
Earnings subject to appropriation and expenditure for specified purpose	
Seminarian education	955,677
McHugo endowment income fund	166,285
	<u>1,121,962</u>
TOTAL ENDOWMENTS	<u>2,966,139</u>
TOTAL NET ASSETS WITH DONOR RESTRICTIONS	<u>\$ 4,217,912</u>

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purpose or by occurrence of the passage of time or other events specified by the donors as follows for the year ended June 30, 2021:

Satisfaction of purpose restrictions:	
Works of Justice	\$ 14,000
Rice Bowl Poverty Program	20,000
Education of seminarians	20,540
Catholic education	20,437
TOTAL RESTRICTIONS RELEASED	<u>\$ 74,977</u>

NOTE 11 - Endowments

The Diocese's endowment fund consists of both donor-restricted endowment funds and funds designated by the Board of Directors to function as endowments. As required by U.S. GAAP, net assets associated with endowment funds are classified and reported based on the existence of or absence of donor-imposed restrictions.

Interpretation of the Law - The Finance Council of the Diocese has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Diocese classifies as net assets with restrictions (a) the original value of gifts donated to the endowment, (b) the original value of subsequent gifts to the endowment, and (c) accumulations to the endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. Donor-restricted amounts not retained in perpetuity are subject to appropriation for expenditure by the Diocese in a manner consistent with the standard of prudence prescribed by UPMIFA.

The Diocese considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purpose of the Diocese and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the Diocese
7. The investment policies of the Diocese

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
 NOTES TO THE FINANCIAL STATEMENTS - Continued
 JUNE 30, 2021

NOTE 11 - Endowments - Continued

Investing and Spending Policy - The Diocese has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the principal and purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Diocese must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds. Under this policy, as approved by the Finance Council, the endowment assets are invested in a manner to preserve capital, provide growth in principal combined with a sufficient return on investment that will generate continued income, and invest in such a manner to satisfy anticipated liquidity requirements. The Diocese expects its endowment funds, over time, to provide an average rate of return of approximately 5 percent annually. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate-of-return objectives, the Diocese relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Diocese targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

The Diocese distributes grant funds based on the total investment earnings earned for each endowment. Accordingly, over the long term, the Diocese expects the current spending policy to allow their endowments to grow. This is consistent with the Diocese's objective to maintain the principal and purchasing power of the endowment assets held in perpetuity or for a specified term, as well as to provide additional real growth through new gifts and investment return.

Endowment Net Asset Composition by Type of Fund as of June 30, 2021:

	<u>Without Donor Restriction</u>	<u>With Donor Restriction</u>	<u>Total</u>
Board-designated endowment funds	\$ 187,428	\$ -	\$ 187,428
Donor-restricted endowment funds:			
Original donor-restricted gift and amounts required to be maintained in perpetuity by donors	-	1,844,177	1,844,177
Accumulated investment gains	-	1,121,962	1,121,962
TOTAL	<u>\$ 187,428</u>	<u>\$ 2,966,139</u>	<u>\$ 3,153,567</u>

Funds with Deficiencies - From time to time, the fair value of assets associated with donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Diocese to retain as a fund of perpetual duration (underwater endowments). In accordance with U.S. GAAP, deficiencies of this nature are reported in net assets with donor restrictions. The deficiencies may result from unfavorable market fluctuations that have occurred. The Diocese did not have any such deficiency as of June 30, 2021.

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
 NOTES TO THE FINANCIAL STATEMENTS - Continued
 JUNE 30, 2021

NOTE 11 - Endowments - Continued

Changes in Endowment Net Assets for the Year Ended June 30, 2021:

	<u>Without Donor Restriction</u>	<u>With Donor Restriction</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 2,660,244	\$ 2,473,396	\$ 5,133,640
Investment return, net	-	513,283	513,283
Appropriation of endowment assets pursuant to spending-rate policy	<u>(2,472,816)</u>	<u>(20,540)</u>	<u>(2,493,356)</u>
Endowment net assets, end of year	<u>\$ 187,428</u>	<u>\$ 2,966,139</u>	<u>\$ 3,153,567</u>

**NOTE 12 - Pension Plan for Priests Within the Diocese of Winona-Rochester
(Debtor in Possession)**

The Diocese participates in a multiple employer defined benefit pension plan (the "Plan") for all priests ordained or incardinated into the Diocese who are employed by Participating Employers. The Plan is funded through assessments to the Participating Employers and contributions from donors. A participant who retires at the normal age of 68 shall receive, currently, a monthly pension benefit for life of \$2,050. The Plan also provides Medicare supplemental health and dental coverage for fully-retired priests for life. Plan assets consist primarily of investments in common/collective trust funds.

The Plan is voluntary on the part of the Participating Employers, and the continuance of the Plan and the payment of contributions hereunder are not to be regarded as a contractual obligation of the Participating Employers. The Participating Employers do not guarantee any of the benefits provided by the Plan. The Plan provides that the Participating Employers reserve the right to reduce or suspend, in whole or in part, at any time, the contributions specified in the Plan.

The Participating Employers use June 30 to determine the annual contributions to the Plan for accrued pension expense. As this is a multiple employer plan, valuation information is not available by employer.

The Plan is not required to comply with ERISA, as it is a church plan. Employer contributions to the Plan for 2021 were \$19,688.

NOTE 13 - Lay Retirement Plan

The Diocese contributes 3 percent of the employee's base compensation plus up to an additional 3 percent as an employer match for those employees who are at least 21 years of age, and who work more than 20 hours per week. Participation is effective at date of hire for eligible employees. As of June 30, 2021, the Diocese contributed \$88,572 to this plan.

DIOCESE OF WINONA-ROCHESTER
(Debtor in Possession)
NOTES TO THE FINANCIAL STATEMENTS - Continued
JUNE 30, 2021

NOTE 14 - Service Agreements

The Diocese has service agreements with Catholic Foundation of Southern Minnesota, Pension Plan for Priests of the Diocese of Winona, and Immaculate Heart of Mary Seminary, Inc. whereby, the various entities reimburse the Diocese for accounting services and use of buildings owned by the Diocese. Revenue received from these agreements as of June 30, 2021, is as follows:

Pension Plan for Priests of the Diocese of Winona	\$ 26,522
Immaculate Heart of Mary Seminary, Inc.	28,401
Catholic Foundation of Southern Minnesota	<u>51,714</u>
	<u>\$ 106,637</u>

The Diocese also contracts with Catholic Foundation of Southern Minnesota to conduct their annual Catholic Ministries Appeal. Expenses paid for these services as of June 30, 2021, were \$211,896.

NOTE 15 - Risk and Uncertainties

Investments - The Diocese's investments are exposed to various risks, such as interest rate, and market and credit risks. Due to the level of risk associated with certain investments and the level of uncertainty related to changes in the values of investments, it is reasonably possible that changes in risks in the near term could materially affect the amounts reported in the statements of financial position and the statements of activities.

COVID-19 Pandemic - During 2020 and 2021, the world-wide Coronavirus Pandemic impacted national and global economies. The Diocese is closely monitoring its operations, liquidity, and capital resources and is actively working to minimize the current and future impact of this unprecedented situation. As of the date of issuance of these financial statements, the current and future full impact to the Diocese is not known.

**DIOCESE OF WINONA-ROCHESTER
(Debtor in Possession)**

SUPPLEMENTARY INFORMATION

DIOCESE OF WINONA-ROCHESTER
 (Debtor in Possession)
 STATEMENT OF ACTIVITIES BY DEPARTMENT
 YEAR ENDED JUNE 30, 2021

	<u>REVENUE</u>	<u>EXPENSES</u>	<u>CHANGE IN NET ASSETS</u>	<u>BUDGET</u>
Bishop	\$ 226,460	\$ 179,955	\$ 46,505	\$ -
Bishop Emeritus	61,152	53,092	8,060	-
Vicar General	67,177	73,656	(6,479)	-
Chancellor	30,961	16,414	14,547	-
Vicar Judicial (Tribunal)	247,483	179,321	68,162	-
General Diocese	3,870,139	1,937,791	1,932,348	46,000
Chapter 11 Reorganization	-	19,972,180	(19,972,180)	(1,825,000)
Human Resources	196,480	176,402	20,078	-
Safe Environment	105,035	105,039	(4)	-
Mission Advancement Stewardship/Development	-	31	(31)	-
Mission Advancement - Annual Appeal	229,500	211,896	17,604	-
Finance	467,631	461,921	5,710	-
Parish Financial Services	99,828	73,193	26,635	-
Contracted Services	81,350	74,444	6,906	-
Planning	12,635	6,121	6,514	-
Moderator of Curia	27,667	20,130	7,537	-
Support Services	154,951	122,168	32,783	-
Cemeteries	38,439	40,066	(1,627)	-
Courier	57,628	35,468	22,160	-
Communications	304,040	250,723	53,317	-
Care of Priests	209,882	160,713	49,169	-
Priestly Life - Clergy Education	87,800	86,007	1,793	-
Seminarian/Theological Education	519,895	519,898	(3)	-
Vocations	41,930	74,216	(32,286)	-
Catholic Education/Formation - Schools	317,902	298,426	19,476	-
Media Center	1,836	1,254	582	-
Mankato Newman Center	153,945	153,945	-	-
Winona Newman Center	108,820	113,301	(4,481)	-
Catholic Education/Formation - Faith Formation	71,647	54,033	17,614	-
Apostolate - Ministry Formation	299,324	276,833	22,491	-
Apostolate - Permanent Diaconate	51,724	38,376	13,348	-
Divine Worship	55,774	40,218	15,556	-
Life	80,398	69,617	10,781	-
Youth and Young Adults	184,083	163,623	20,460	-
Apostolate - Hispanic Ministry	17,190	13,734	3,456	-
Apostolate - Hispanic Chaplaincy	53,107	55,190	(2,083)	-
TOTAL DEPARTMENTAL	<u>8,533,813</u>	<u>26,109,395</u>	<u>(17,575,582)</u>	<u>(1,779,000)</u>
Other Restricted Funds	535,819	243,732	292,087	79,000
TOTAL DIOCESAN	<u>\$ 9,069,632</u>	<u>\$ 26,353,127</u>	<u>\$(17,283,495)</u>	<u>\$ (1,700,000)</u>

* Includes interdepartmental transfers