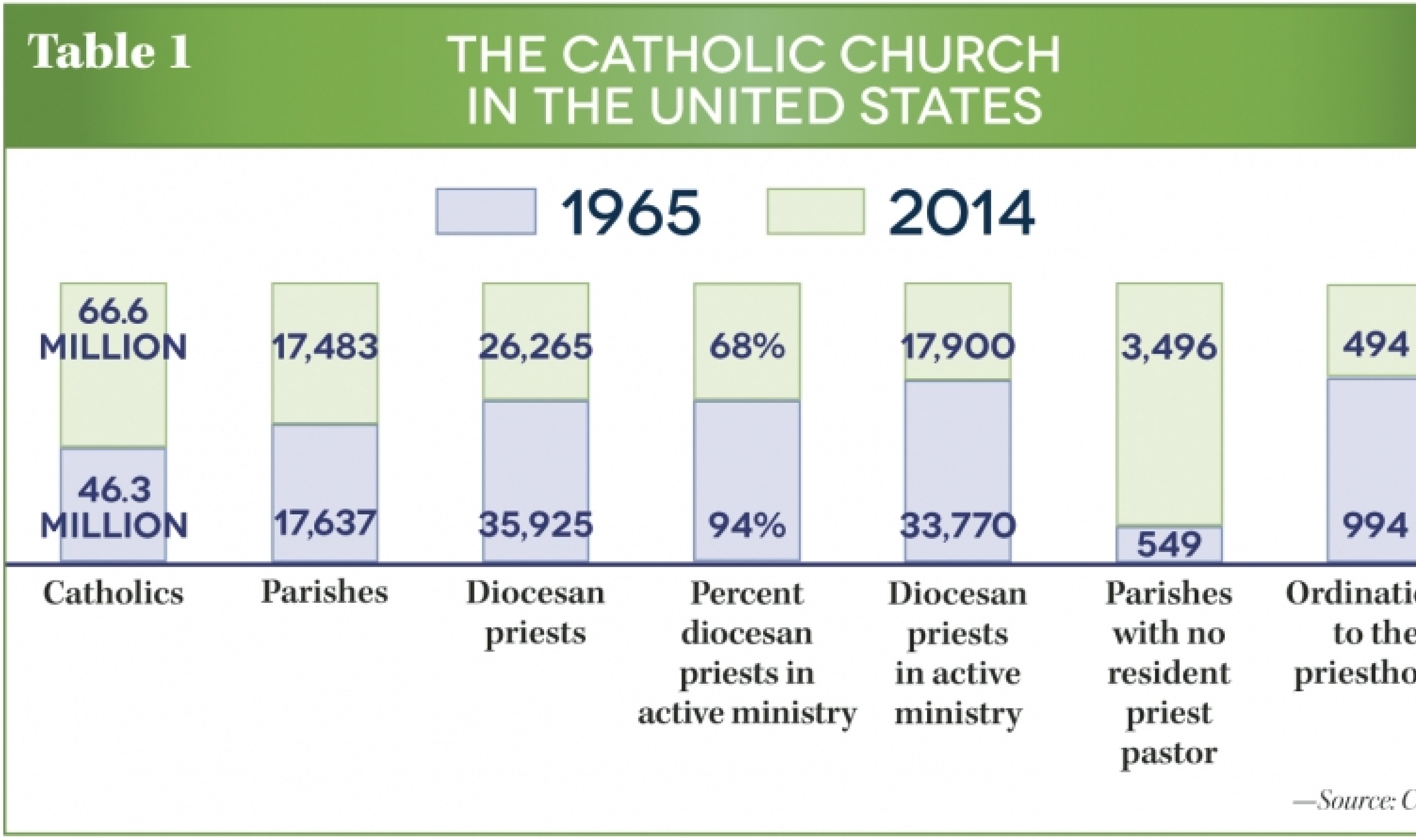
Feb 24, 2015

Survey finds serious flaws in diocesan financial management

by Jack Ruhl

Analysis

The Catholic priesthood is aging at an alarming rate, and thousands of U.S. diocesan priests are expected to retire within the next few years. With most diocesan priest pension plans significantly underfunded, questions over where the money comes from to support them may point to a major crisis in the making.



Fewer than 26,265 diocesan priests remain in the U.S. today and of them, only 68 percent -- about 17,900 -- are still in active ministry (Table 1). Only about one-third as many new priests are being ordained each year to make up for the ones who are retiring, dying or leaving active ministry. Dioceses now have one retired priest for every two active priests, and half of all priests in active ministry are over the age of 60.

Half of all priests currently in active ministry also expect to retire by 2019, and most of them expect to receive the pension payments they've been promised. Church leaders have known for decades about the looming priest shortage and its implications for sustaining Catholic parishes as eucharistic communities. Another, more hidden crisis lurks in diocesan pension reserves that are underfunded, many of them seriously.

Thousands of priests retiring in the next few years could discover that the pension and post-retirement money they expect from their dioceses is not available. I reviewed the results of the USI Consulting Group's 2012 Diocesan Retirement Survey of priests and lay employees, focusing on priests. USI Consulting Group, founded in 1981 and headquartered in Glastonbury, Conn., provides retirement and employee benefit plan services throughout the United States.

The survey was sent to 194 archdioceses and dioceses. Responses were received from 97 dioceses, a 50 percent response rate, in 42 states as well as Canada, the Bahamas and Guam. The survey asked about defined benefit and defined contribution plans, but did not ask about post-retirement benefits (e.g., medical, dental, continuing education, and life insurance benefits).

Employers sponsoring a defined benefit pension agree to provide vested participants with a set amount of income for the duration of retirement. A defined benefit pension plan describes the benefits priests will receive when they retire. The benefits are a function of their years of service and age at retirement. Employers sponsoring a defined contribution plan state that they will provide a certain amount each pay period, and employees manage their own retirement funds. Plans such as 401(k) are defined contribution plans. Employers sponsoring defined benefit plans take on much more risk than those who sponsor a defined contribution plan.

Table 2

TYPES OF RETIREMENT PLANS OFFERED TO DIOCESAN PRIESTS

Defined Benefit (qualified)	58.4%
Defined Benefit (non-qualified)	29.2%
Defined contribution — 401(k)	7.9%
Defined contribution — 403(b) (with diocesan contribution)	15.7%
Defined contribution — 403(b) (without diocesan contribution)	27%
Other	6.7%

Source: USI Consulting Group 2012 Diocesan Retirement S

As shown in Table 2, 87.6 percent (58.4 percent plus 29.2) of priests are offered a defined benefit pension plan.

At first, the high percentage (87.6 percent) of priests covered by defined benefit plans seems reassuring. However, an important next question is the level of plan funding. The USI Consulting Group's survey also asked for the plan's funded ratio from the most recent valuation. The funding ratio is calculated like this: If pension obligations are $100 million, and the assets available to meet those obligations are $55 million, the plan would be 55 percent funded. Funded ratios apply only to defined benefit plans.

There is reason to be concerned if the pension plan is severely underfunded, because the employer may not be able to meet the financial obligation as employees retire. In the secular world, employees in defined benefit plans enjoy some protection under the Employee Retirement Income Security Act (ERISA) of 1974 and the Pension Protection Act of 2006. ERISA established a federal agency, the Pension Benefit Guaranty Corporation, which had the power to place liens on corporate assets for unfunded pension liabilities. The agency could also administer terminated pension plans. That is, if the secular employer went bankrupt, the agency would step in and pay a fraction of the pension due the employee.

In the secular world, the Department of Labor requires certain disclosures about pensions that are not required in the sacred world. If a plan is more than 80 percent funded, it is categorized as being in the green zone. If a plan is 65-80 percent funded, it is categorized as being in the yellow zone, or in endangered status. Yellow zone plans must adopt a funding improvement plan.

Advertisement

Defined benefit plans that are less than 65 percent funded are categorized as being in the red zone, or in critical status. Red zone plans must adopt a rehabilitation plan and must notify all those enrolled in the pension plan. The Department of Labor provides a listing of all red or yellow plans for for-profit firms on its website. The department provides no such disclosure for religious organizations.

Neither the Department of Labor, nor ERISA, nor the Pension Protection Act offers any pension protection to priests. Dioceses are not required to disclose any pension funding information to enrollees, and the Pension Benefit Guaranty Corporation will not step in to supply benefits if dioceses do not or cannot. Therefore, I was especially interested in reviewing the funding status of priests' defined benefit pensions. The USI Consulting Group survey provided this information in the aggregate for all survey respondents.

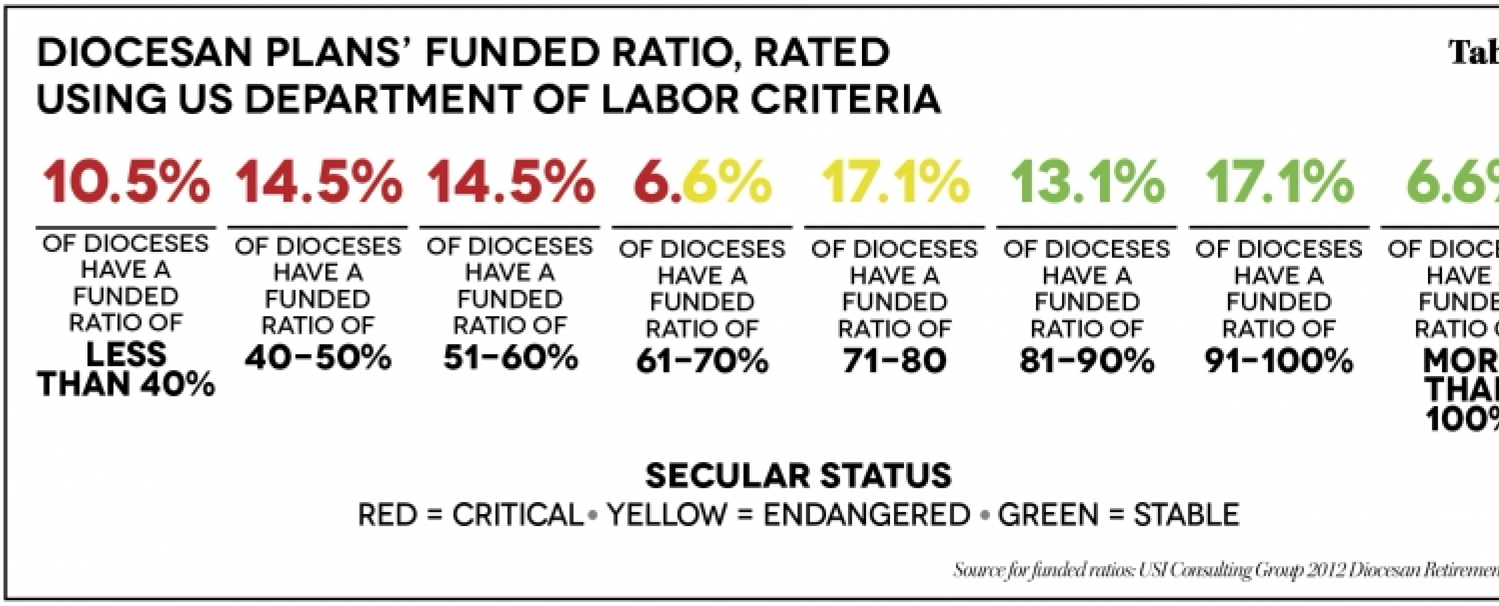


Table 3 shows that 36.8 percent of diocesan defined contribution plans were in the green zone, while 63.2 percent are in yellow (endangered) or red (critical) zones. If these plans were subject to the Department of Labor requirements, most of them would have to adopt either a funding improvement plan or rehabilitation plan.

While the survey information was interesting, I wanted to know the health of specific diocesan priests' retirement plans in the U.S. In the secular world, the best way to determine the financial health of such a plan is to check the financial statements of the employing organization.

Catholic dioceses, however, are under no obligation to release any financial information whatsoever, in the form of audited financial statements or IRS-mandated disclosures. While other nonprofits must file Form 990 (Return of Organization Exempt From Income Tax) with the Internal Revenue Service, or IRS Form 5500 (Annual Return/Report of Employee Benefit Plan), the church is under no such obligation. Any diocesan financial disclosures are purely voluntary.

Still, I searched for the financial disclosures of the 178 Latin-rite dioceses that belong to the U.S. Conference of Catholic Bishops. To find out the status of the priests' pension funds, a search was done of the websites of the dioceses for any sort of financial disclosure for fiscal year 2013. Of the 178 dioceses, only 102 have financial information available. The other 76 release no financial information, as far as I could determine.

The quality of financial disclosures varies dramatically. Some dioceses post a full set of audited financial statements on their websites. Others post unaudited "stewardship reports," "annual reports" or "financial reports" on their websites or publish them in the diocesan newspaper. These are useless for determining diocesan financial health, let alone the pension plan's health. The laity think that they are obtaining useful information by reading them, when in fact they are obtaining nothing.

A stewardship report, annual report or unaudited financial report is nothing more than an unsupported assertion by the diocese. In the secular world, an audited financial statement provides support for management's assertions with numbers and explanations. A stewardship report, annual report or unaudited financial report may be incomplete, and thus useless.

A report is incomplete if it lacks a statement of financial position that quantifies diocesan assets (like cash and buildings) and liabilities (like amounts owed to clergy abuse survivors). It is also incomplete if it lacks a statement of cash flows, which shows if the diocese has sold assets or borrowed or loaned money. Finally, it is incomplete if it lacks disclosure notes, which state exactly what is being accounted for -- for example, just the chancery -- and what is not being accounted for -- for example, the priests' pension fund, parishes, cemeteries and lots more. The New York archdiocese's Financial Services Report is a good example of an unsupported and incomplete set of assertions.

Of the 102 dioceses providing some level of financial information, only 61 have pension information that they make publicly available. According to the Official Catholic Directory for 2014, there are 11,093 diocesan priests domiciled in these 61 dioceses. Given that the Center for Applied Research in the Apostolate (CARA) says there are 25,634 priests in the U.S. Latin-rite dioceses, the information I gathered relates to about 43 percent of the total U.S. diocesan priests.

Almost without exception, U.S. dioceses end their fiscal year on June 30 and they are typically a year in arrears in reporting financial results, meaning that by August 2014 they were just releasing financial statements for the fiscal year ended June 30, 2013. When the diocesan website had no financial disclosures, I sent an email to the chief financial officer of the diocese, asking him or her to email me the fiscal year 2013 financials. Most of my emails received no reply.

Accountants take an entity perspective with regard to financial reporting. This means that financial statements prepared in accordance with generally accepted accounting principles must state in the disclosure notes what is being accounted for and what is excluded. The majority of dioceses define the accounting entity very narrowly. This allows for the omission of a great deal of information.

Typically, the diocesan entity was defined as only the chancery, central ministries or central administrative offices. The disclosure notes to the financial statements usually state that parishes, schools, cemeteries (there are 1,900 Catholic cemeteries in the United States), old-age homes, and sometimes pension funds were excluded. This is the case for the dioceses of Cheyenne, Wyo., and Detroit, for example. Dioceses are allowed to exclude these other entities by asserting that they do not have "direct operational control" over them.

The 102 dioceses that provided financial information are shown in this spreadsheet. (If a diocese is not included on the chart, I could not obtain the information.) The spreadsheet shows the known benefit obligation and the pension funding ratio. The pension funding zone then reflects the pension funding ratio.

The spreadsheet next provides what is known about post-retirement benefits: the post-retirement obligation, the funding ratio, and the funding zone.

Note that the total unfunded pension liability is $820,848,371. The unfunded post-retirement obligation is $509,030,297. The total unfunded obligations exceed $1.3 billion.

Of the 61 dioceses releasing pension information, 33 were less than 65 percent funded (in the red zone or critical), 12 were 65-80 percent funded (yellow zone or endangered), and 16 were in the green zone. The percentages are given in Table 4.

Table 4

PENSION FUNDING INFORMATION FROM 61 DIOCESES

54% OF THE DIOCESES ARE FUNDED **LESS THAN 65%**

20% OF THE DIOCESES ARE FUNDED **65–80%**

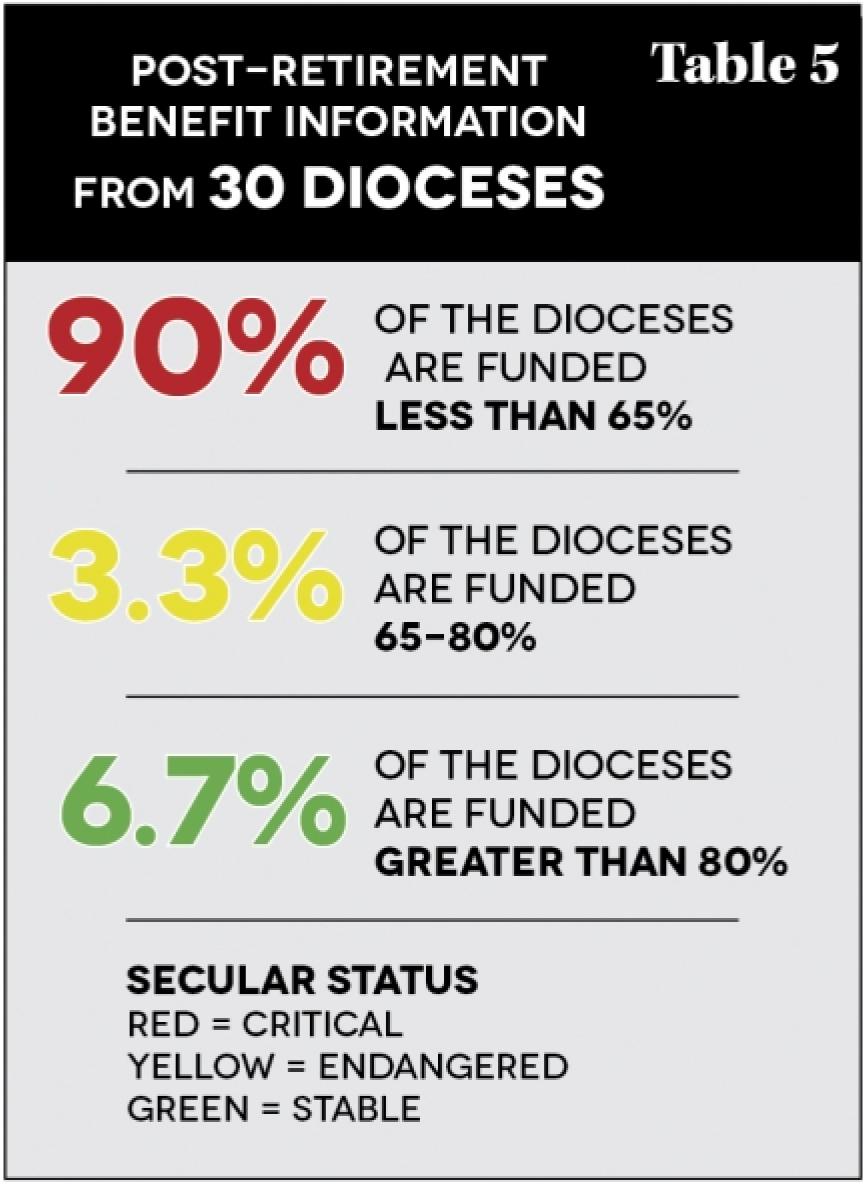
26% OF THE DIOCESES ARE FUNDED **GREATER THAN 80%**

SECULAR STATUS
RED = CRITICAL
YELLOW = ENDANGERED
GREEN = STABLE

With regard to post-retirement information (e.g., medical, dental, continuing education, and life insurance benefits), only 30 dioceses provided financial information. This may be because they did not provide post-retirement benefits or they chose not to disclose these benefits. We applied the Department of Labor classification scheme to these 30 dioceses. Of this total, 27 are less than 65 percent funded (in the red zone or critical), one is 65-80 percent funded (yellow zone or endangered), and two are in the green zone. Twenty-four of the 27 dioceses have zero funding of post-retirement benefits (Table 5).

Looking at just 61 of 191 dioceses, we found more than $800 million in defined pension benefit underfunding. As mentioned above, $800 million in underfunding relates to about 43 percent of the total number of U.S. Catholic priests. I extrapolated this underfunding by dividing $800 million by 43 percent, to estimate the total amount of pension underfunding in the U.S. to be about $1.9 billion.

I applied the same approach to estimate the total post-retirement underfunding in the U.S., dividing $268 million by 43 percent to get about $623 million. I estimate the total pension and post-retirement underfunding for U.S. priests to exceed $2.5 billion.



The problem of pension and post-retirement underfunding is not insurmountable, but major change is needed. To paraphrase Cardinal George Pell, prefect of the Vatican's Secretariat for the Economy, there is no "return to the bad old days."

First, as the great U.S. Supreme Court Justice Louis Brandeis said, "Sunlight is said to be the best of disinfectants; electric light the most efficient policeman." In this case, the sunlight will illuminate the financial state of each diocese (including priests' pension and retirement benefits) in a timely manner. Presenting financial results one year in arrears is unacceptable. Each diocese should post a full set of audited financial statements on its website within 60 days of the close of the fiscal year.

Second, priests and laity must assume the roles of financial watchdogs over diocesan resources. In the secular world, shareholders scrutinize audited financial statements to assess the stewardship of corporate leaders. Diocesan leaders should be held to this same standard. For generations, the laity have provide material resources, while the priests provided pastoral care. Both groups apparently trusted that the financial house was in good order and retiring priests would be well cared for.

Third, the audited financials must accurately depict the entire diocesan accounting entity. This may include the chancery, parishes, schools, seminaries, cemeteries, old-age homes, and priests' pensions. Auditors must adopt appropriate professional skepticism when diocesan leaders dig their heels in, arguing that the reporting entity is just the chancery. Suggesting that the accounting entity is just the chancery results in incomplete financial reports.

Fourth, beginning immediately, all dioceses with a pension and/or post-retirement funding shortfall should engage the services of a qualified professional to assist them in developing a plan to fully fund all shortfalls within a reasonable period, preferably the next five years. This must be a priority of diocesan leadership, and the hierarchy must own up to the fact that they may not have been good stewards of retirement resources.

The hierarchy must admit that changes are needed in financial management. At the same time, priests and laity must demand more financial transparency and accountability. Pell, referring to anticipated changes in the Vatican bank said, "There need to be changes in the economic area -- not just with the so-called Vatican bank -- but more generally there is work there to be done [and] a need to ensure that things are being properly done."

Let's hope the American hierarchy gets the message.

[Jack Ruhl is a professor of accountancy at Western Michigan University in Kalamazoo, Mich.]

Links
[1] https://www.ncronline.org/join-conversation