

WATER STREET MINISTRIES
CONSOLIDATED FINANCIAL STATEMENTS
SIX-MONTH PERIOD ENDED JUNE 30, 2011

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Independent Auditor's Report

To the Board of Directors
Water Street Ministries
Lancaster, Pennsylvania

We have audited the accompanying consolidated statement of financial position of Water Street Ministries and affiliate (nonprofit organizations) as of June 30, 2011, and the related consolidated statements of activities, functional expenses, and cash flows for the six-month period then ended. These financial statements are the responsibility of Water Street's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Water Street Ministries and affiliate as of June 30, 2011, and the changes in their net assets and their cash flows for the six-month period then ended, in conformity with accounting principles generally accepted in the United States of America.

Hatter, Harris and Beittel, LLP
HATTER, HARRIS AND BEITTEL, LLP

September 29, 2011

WATER STREET MINISTRIES
CONSOLIDATED STATEMENT OF FINANCIAL POSITION

JUNE 30, 2011

ASSETS

Current assets:

Cash and cash equivalents	\$ 545,622
Investment income receivable	6,849
Accounts receivable	33,477
Deposits	28,358
Prepaid expenses	147,341
Bequests income receivable	719,946
Inventory (Note 2)	<u>410,013</u>
Total current assets	1,891,606
Investments, long-term (Note 3)	5,553,914
Property and equipment, net (Note 4)	8,792,652
Other real estate - temporarily restricted	200,000
Beneficial interest in split-interest agreements (Note 5)	599,372
Beneficial interest in assets held by others in perpetual trust (Note 6)	<u>4,371,296</u>
Total assets	\$ <u><u>21,408,840</u></u>

The accompanying notes are an integral part of these financial statements.

LIABILITIES AND NET ASSETS

Current liabilities:

Current portion of obligations under capital lease	\$ 3,198
Accounts payable - trade	129,959
Accrued payroll and employee benefits	117,966
Other current liabilities	38,715
Deferred revenue	<u>133,078</u>

Total current liabilities 422,916

Obligations under capital lease, net of current portion	15,434
Annuity obligations (Note 7)	<u>157,292</u>

Total liabilities 595,642

Net assets:

Unrestricted:

Designated by board (Note 9)	3,315,870
Allocated to property and equipment	8,792,652
Undesignated	<u>2,913,304</u>

Total unrestricted 15,021,826

Temporarily restricted (Note 10)	841,355
Permanently restricted (Note 11)	<u>4,950,017</u>

Total net assets 20,813,198

Total liabilities and net assets \$ 21,408,840

WATER STREET MINISTRIES
CONSOLIDATED STATEMENT OF ACTIVITIES
SIX-MONTH PERIOD ENDED JUNE 30, 2011

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenues, gains, and other support:				
Contributions	\$ 1,791,929	\$ 54,384	\$	\$ 1,846,313
Contributions - non-cash	1,167,306			1,167,306
Investment income, net of investment fees	34,079			34,079
Income from beneficial interest in assets held by others in perpetual trust	86,900			86,900
Program fees	164,049			164,049
Other income	129,341			129,341
Net assets released from restrictions	<u>30,463</u>	<u>(30,463)</u>		<u>-</u>
Total revenues, gains, and other support	3,404,067	23,921	-	3,427,988
Expenses:				
Program services -				
Water Street Ministries	2,767,797			2,767,797
Water Street Health Services	679,151			679,151
Management and general	411,418			411,418
Fundraising and development	<u>493,737</u>			<u>493,737</u>
Total expenses	<u>4,352,103</u>	<u>-</u>	<u>-</u>	<u>4,352,103</u>
Income (loss) from activities	(948,036)	23,921	-	(924,115)
Other changes:				
Adjustment to beneficial interest in assets held by others in perpetual trust			68,119	68,119
Adjustment to beneficial interest in split-interest agreements		24,081		24,081
Adjustment to annuity obligations	(10,765)			(10,765)
Gain (loss) on disposal of capital assets	1,132			1,132
Net realized and unrealized gain (loss) of investments	<u>172,864</u>	<u>4,155</u>	<u>17,256</u>	<u>194,275</u>
Total other changes	<u>163,231</u>	<u>28,236</u>	<u>85,375</u>	<u>276,842</u>
Change in net assets	(784,805)	52,157	85,375	(647,273)
Net assets at beginning of period	<u>15,806,631</u>	<u>789,198</u>	<u>4,864,642</u>	<u>21,460,471</u>
Net assets at end of period	<u>15,021,826</u>	<u>841,355</u>	<u>4,950,017</u>	<u>20,813,198</u>

The accompanying notes are an integral part of these financial statements.

WATER STREET MINISTRIES

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

SIX-MONTH PERIOD ENDED JUNE 30, 2011

	<u>PROGRAM SERVICES</u>		<u>SUPPORTING SERVICES</u>		<u>Total</u>
	<u>WSM</u> <u>Program</u> <u>Services</u>	<u>Water Street</u> <u>Health</u> <u>Services</u>	<u>Management</u> <u>and General</u>	<u>Fundraising</u> <u>and</u> <u>Development</u>	
Salaries and wages	\$ 864,833	\$ 115,432	\$ 214,736	\$ 169,898	\$ 384,634
Donated services	16,003	139,819	-	-	-
Employee health and retirement benefits	195,436	8,114	41,619	32,441	74,060
Payroll taxes and unemployment claims	69,038	9,142	18,349	11,408	29,757
Gifts and grants to clients	102,323	-	-	-	-
Donated clothing and furniture	117,775	-	-	-	-
Donated food and supplies	660,380	-	-	-	-
Donated medical supplies, fees and other	-	329,731	-	-	-
Food and supplies purchased	65,227	8,653	8,103	563	8,666
Electric	69,364	3,080	2,633	1,373	4,006
Security	4,617	113	66	66	132
Building repairs and maintenance	20,910	1,440	7,347	-	7,347
Heating and cooking fuel	63,527	1,772	7,904	813	8,717
Vehicle and equipment repairs and small equipment	35,060	1,199	6,644	5,836	12,480
Vehicle fuel	37,458	-	1,712	-	1,712
Promotional expenses	28,300	809	2,574	237,196	239,770
Insurance	71,386	6,647	10,101	3,223	13,324
Trash removal	10,791	137	540	68	608
Water and sewer	12,432	1,114	1,209	213	1,422
Telephone	17,206	2,342	7,553	1,640	9,193
Professional fees	5,288	20,041	28,513	8,081	36,594
Interest expense	-	-	354	-	354
Property taxes	10,862	-	3,083	-	3,083
Conferences, seminars, travel and entertainment	10,915	7,383	13,066	3,936	17,002
Licenses and fees	8,474	4,540	12,358	12,381	24,739
Other expenses	37,470	6,387	13,103	907	14,010
Total expenses before depreciation and amortization	2,535,075	667,895	401,567	490,043	891,610
Depreciation and amortization	232,722	11,256	9,851	3,694	13,545
Total expenses	\$ 2,767,797	\$ 679,151	\$ 411,418	\$ 493,737	\$ 905,155
					\$ 4,352,103

The accompanying notes are an integral part of these financial statements.

WATER STREET MINISTRIES

CONSOLIDATED STATEMENT OF CASH FLOWS

SIX-MONTH PERIOD ENDED JUNE 30, 2011

Cash flows from operating activities:	
Change in net assets	\$ (647,273)
Adjustments to reconcile change in net assets to net cash provided (used) by operating activities:	
Depreciation and amortization	257,523
Donated inventory	96,403
Donated goods and investments	(41,844)
Change in value of annuity obligations	10,765
(Gain) loss on disposal of capital assets	(1,132)
Realized (gain) loss of investments	(24,534)
Unrealized (gain) loss of investments	(169,741)
Changes in:	
Investment income receivable	(254)
Accounts receivable	10,810
Deposits	(28,358)
Prepaid expenses	(20,292)
Bequest and trust income receivable	(197,413)
Beneficial interest in split-interest agreements	(24,081)
Beneficial interest in assets held by others	(68,119)
Inventory	(618)
Accounts payable	30,190
Accrued payroll and employee benefits	13,169
Other current liabilities	7,189
Deferred revenue	<u>33,532</u>
Net cash provided (used) by operating activities	(764,078)
Cash flows from investing activities:	
Purchase of investments	(244,971)
Proceeds from sale of investments	226,796
Purchase of property and equipment	(259,356)
Proceeds from disposal of property and equipment	<u>6,305</u>
Net cash provided (used) by investing activities	(271,226)
Cash flows from financing activities:	
Proceeds from annuity obligations	2,393
Payment of capital lease obligation	(764)
Payment of annuity obligations	<u>(11,141)</u>
Net cash provided (used) by financing activities	<u>(9,512)</u>
Net increase (decrease) in cash and cash equivalents	(1,044,816)
Cash and cash equivalents at beginning of period	<u>1,590,438</u>
Cash and cash equivalents at end of period	<u>\$ 545,622</u>

The accompanying notes are an integral part of these financial statements.

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 1: Summary of Significant Accounting Policies

Nature of Activities

The purpose of Water Street Ministries, a non-profit organization, hereafter referred to as "Water Street," is to advance the kingdom of God through the gospel of Jesus Christ and to do missionary, relief and rescue work of all kinds. Programs include providing food, shelter, clothing and furniture, medical and dental services, youth education, recovery and religious guidance to the poor and homeless men, women and children in south-east and south-central Pennsylvania. Water Street operates sites in Lancaster, Wrightsville, York and Philadelphia.

Contributions from individuals, corporations and foundations in the form of cash, food, medications, medical supplies and services represent a significant portion of support to Water Street. Unpaid volunteers provide a significant amount of their time to perform services for Water Street programs, administration and fundraising activities.

Principles of Consolidation

The accompanying consolidated financial statements include the activities of Water Street Ministries and its affiliate, Water Street Health Services. Water Street Health Services, a non-profit organization, provides health services free of charge to the uninsured of Lancaster County who fall within specific guidelines. Inter-entity activities between Water Street Ministries and Water Street Health Services have been eliminated.

Change of Fiscal Year

Water Street has operated on a December 31 fiscal year-end from inception through December 31, 2010. During 2011, Water Street elected to change its fiscal year-end to June 30. These financial statements reflect the activity for the six-month period beginning January 1, 2011 and ending June 30, 2011.

Legal Requirements

Water Street was established as a Pennsylvania nonprofit corporation and files annually with the Pennsylvania Bureau of Charitable Organizations.

Income Taxes

Water Street is exempt from federal income taxes under Sec. 501(c)(3) of the Internal Revenue Code and, therefore, no provision for income taxes is included in the accompanying financial statements.

Water Street believes its exempt status will be sustained under audit and believes it does not have any significant uncertain tax positions. No required annual returns for organizations exempt from income tax are currently under examination by taxing jurisdictions. With few exceptions, Water Street is no longer subject to examinations by relevant tax authorities for years prior to fiscal 2008.

WATER STREET MINISTRIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 1: Summary of Significant Accounting Policies (Continued)

Accounting Estimates

The preparation of financial statements in conformity with generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Cash and Cash Equivalents

Highly liquid investments with an original maturity of three months or less are considered to be cash equivalents.

Concentration of Credit Risk

During the six-month period, Water Street's deposit balances with financial institutions exceeded the FDIC insured limit. Management believes that credit risk related to these excess balances is minimal.

Inventory

Inventories consist of food, medications, medical and dental, and general supplies held for future consumption. Inventories are stated at wholesale value and cost is determined on the first-in, first-out (FIFO) method.

Donations of clothing and furniture are received and inventoried for distribution to the local community. Although these items are of value, such values are not readily ascertainable. Therefore, inventories of clothing and furniture donated to Water Street's Outreach Ministries are not reported on the accompanying balance sheets. Management has estimated the values at June 30, 2011 to be \$42,111.

Investments

Investments at June 30, consist of money market funds, fixed income and equity mutual funds, marketable equity and fixed income securities. These investments are stated at market value on the accompanying statements of financial position. Investment income includes interest and dividends, reduced by investment fees, and is included as unrestricted income from activities on the accompanying statements of activities unless restricted by donor or law and the restriction was not met during the current year. Realized and unrealized gains (losses) on investments are excluded from income from activities, but are included as other changes in net assets in the accompanying statement of activities. Management considers all investments to be long-term.

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 1: Summary of Significant Accounting Policies (Continued)

Property and Equipment

Property and equipment is stated at cost, except donated capital assets, which are stated at fair market value at the date of donation. Major improvements and betterments of existing buildings and fixtures are capitalized, while maintenance and repairs that do not improve or extend the life of the respective assets are expensed currently. Property and equipment with a useful life greater than one year is capitalized. Depreciation is provided using the straight-line method over the estimated useful lives of the related assets as follows:

	<u>Years</u>
Computer equipment and software	3-5
Vehicles	5
Furniture and office equipment	10
Machinery and equipment	5-20
Buildings and building improvements	10-40

When properties are retired or otherwise disposed of, the asset and accumulated depreciation accounts are adjusted accordingly. Any resulting gain or loss arising from its disposal is excluded from income from activities, but is included as other changes in net assets.

Net Assets

Net assets of Water Street and changes therein are classified and reported as follows:

Unrestricted net assets - Net assets that are not subject to donor-imposed stipulations.

Temporarily restricted net assets - Net assets subject to donor-imposed stipulations that may or will be met either by actions of Water Street and/or the passage of time.

Permanently restricted net assets - Net assets subject to donor-imposed stipulations that must be maintained permanently by Water Street.

Contributions

Water Street reports gifts of cash, unconditional promises to give, and other assets as unrestricted support. Contributions received with donor restrictions that limit the use of the donated assets, and whose restrictions are satisfied during the period, are reported as unrestricted support in the accompanying statements of activities. All other donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions, including but not limited to beneficial interests in assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the accompanying statements of activities as net assets released from restrictions.

WATER STREET MINISTRIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 1: Summary of Significant Accounting Policies (Continued)

Contributions (Continued)

Unconditional promises to give are recognized when Water Street is notified of the promise to give. Management recognizes an allowance for uncollectible amounts based on prior experience and analysis of specific promises made.

Water Street reports gifts of property and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, Water Street reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service. These contributions are recorded at their estimated values on the date of receipt.

Donated Assets and Services

Donated assets are reflected as contributions in the accompanying financial statements at their estimated market values on the date of receipt except for donations of clothing and furniture that are valued when distributed to the community. Water Street is the recipient of significant quantities of donated food, medications and medical and general supplies.

Professional services and fees contributed are recognized at fair market value. The total value recognized as revenue (contributions) and expense (donated services and professional fees) for the six-month period ended June 30, 2011 was \$155,822.

A substantial number of unpaid volunteers contribute their time to Water Street's programs, fundraising and administrative activities. For the six-month period ended June 30, 2011, 15,522 hours were contributed. No amount has been recognized in the accompanying financial statements for this time because the criteria for recognition under generally accepted accounting principles has not been met.

Certain religious organizations allow Water Street use of their facilities for Water Street programs. No amounts have been recognized in the accompanying financial statements for the use of these facilities.

Bequests

Bequests are gifts made through a will at the donor's death. These gifts may be unrestricted or restricted for specific purposes. Bequests are recorded at the time such proceeds are measurable. During the six-month period ended June 30, 2011, Water Street recognized \$323,917 as contributions from bequests.

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 1: Summary of Significant Accounting Policies (Continued)

Allocation of Expenses

The cost of providing various programs and supporting activities of Water Street have been summarized on a functional basis in the statement of functional expenses. Accordingly, certain costs have been allocated among program and supporting services based upon management estimates.

Promotional and Advertising Costs

Promotional and advertising costs are charged to expense when incurred.

NOTE 2: Inventory

Inventory at June 30, 2011 is comprised of the following:

Food	\$ 87,045
General supplies	10,772
Medical supplies and medications	178,199
Dental supplies	<u>133,997</u>
	<u>\$410,013</u>

Inventory includes both donated and purchased items.

NOTE 3: Investments

Investments are stated at market value. Following is a summary of investments held at June 30, 2011:

Cash and cash equivalents	\$ 384,918
Fixed income securities	1,978,722
Equity investments	<u>3,190,274</u>
	<u>\$5,553,914</u>

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

- JUNE 30, 2011

NOTE 3: Investments (Continued)

Investment income and gains (losses) for cash and cash equivalents and investments are comprised of the following for the six-month period ended June 30, 2011:

Interest and dividend income	\$ 53,447
Less: investments fees	<u>(19,368)</u>
Investment income, net of investment fees	<u>\$ 34,079</u>
Other changes:	
Realized gain (loss) of investments	\$ 24,534
Unrealized gain (loss) of investments	<u>169,741</u>
Net realized and unrealized gain (loss) of investments	<u>\$194,275</u>

NOTE 4: Property and Equipment

A summary of property and equipment at June 30, 2011 is as follows:

Computer equipment and software	\$ 643,822
Vehicles	337,078
Furniture and office equipment	189,610
Machinery and equipment	602,343
Buildings and building improvements	11,138,102
Land and land improvements	1,222,848
Development costs	<u>3,625</u>
	14,137,428
Less accumulated depreciation and amortization	<u>(5,344,776)</u>
Property and equipment, net	<u>\$ 8,792,652</u>

Depreciation and amortization expense for the six-month period ended June 30, 2011 amounted to \$257,523.

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 5: Beneficial Interest in Split-Interest Agreements - Temporarily Restricted Net Assets

Water Street is a recipient of split-interest agreements in which Water Street is named as a beneficiary. Under a split-interest agreement, a donor makes an initial gift in which Water Street has a beneficial interest but is not the sole beneficiary. Generally, the assets of a split-interest agreement are administered by a trustee or a fiscal agent, and distributions are made to a beneficiary or beneficiaries during the life of the agreement. At the end of the split-interest agreement's life, the remaining assets covered by the agreement are distributed to Water Street and other beneficiaries. Management's estimated value of these split-interest agreements is based on the year-end fair market value of the agreement's assets multiplied by Water Street's beneficial interest and discounted for the agreement's estimated life in the statement of financial position. Accordingly, they are reported as a component of temporarily restricted net assets.

NOTE 6: Beneficial Interest in Assets Held by Others in Perpetual Trust - Permanently Restricted Net Assets

Water Street is the beneficiary of trusts where the corpus of the trusts is required to be invested in perpetuity and income is to be distributed to Water Street at least annually. Management's estimated value of the beneficial interest in assets held by others in perpetual trust is based on the fair market value of the trusts' assets. Water Street has no rights to the trusts' assets, only to a percentage of income of the trusts. Accordingly, they are reported as a component of permanently restricted net assets in the statement of financial position.

The following schedule summarizes the income from beneficial interests in assets held by others in perpetual trust at June 30, 2011:

Distributions received by Water Street	\$ 86,900
Adjustment for change in value - gain (loss)	<u>68,119</u>
Total income (loss) in beneficial interest in assets held by others in perpetual trust	<u>\$155,019</u>

NOTE 7: Annuity Obligations

Water Street has entered into charitable gift annuity agreements with individuals to provide quarterly payments during the remainder of the individual's life in return for a charitable gift to Water Street. A portion of the amount received represents an obligation by Water Street to make the quarterly payments and the remainder represents a contribution. The obligation to make payments terminates only upon the donor's death.

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 7: Annuity Obligations (Continued)

Any change in the obligation is recorded in the accompanying statements of activities as a change in value of annuity obligations. Water Street uses a 7% discount rate and the IRS life expectancy tables to value annuity obligations. At June 30, 2011, Water Street's maximum future required annual payments to annuitants under existing agreements were \$22,471.

NOTE 8: Obligations Under Capital Lease

Capital lease obligation at June 30 is as follows:

Capital lease obligation payable, Toshiba America Business Solutions, Inc., bearing interest at 7.4%, monthly payments of \$372, final payment due June 2013

\$18,632

Less current maturities

(3,198)

\$15,434

A schedule of the future minimum lease payments for the years ended June 30 is as follows:

2012	\$ 4,469
2013	4,469
2014	4,469
2015	4,469
2016	<u>4,469</u>
	22,345
Amount representing interest	<u>(3,713)</u>
	<u>\$18,632</u>

Amortization on assets held under capital leases is included in depreciation and amortization expense. The gross amount of assets held under capital leases is \$19,396 and the accumulated amortization thereon is \$970 at June 30, 2011.

NOTE 9: Net Assets - Unrestricted - Designated by Board

The Board of Water Street Ministries has designated a portion of unrestricted net assets for funding capital improvements and a reserve for general operations. At June 30, 2011, the amounts designated by the Board totaled \$3,315,870.

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 10: Temporarily Restricted Net Assets

Temporarily restricted net assets at June 30, 2011 are available for the following purposes:

Interest in split-interest agreements	\$599,372
2011 Fall Food Drive	7,000
PA Free Clinic Grant	28,358
Transitional housing	100,000
Mental health care to the homeless	100,000
Educational endowment	<u>6,625</u>
	<u>\$841,355</u>

NOTE 11: Permanently Restricted Net Assets

Permanently restricted net assets consist of endowment funds and beneficial interest in assets held by others in perpetual trust. Only the income generated from these amounts are expendable for Water Street's operations.

The following schedule summarizes permanently restricted net assets at June 30, 2011:

Endowment funds:	
Operating	\$ 293,200
Educational	285,521
Beneficial interest in assets held by others in perpetual trust	<u>4,371,296</u>
	<u>\$4,950,017</u>

NOTE 12: Risk Management

Water Street is exposed to various risks of loss, including but not limited to theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. Water Street purchases commercial insurance to cover significant losses. Water Street monitors insurance coverage and adjusts when warranted.

Any losses incurred have not exceeded insurance coverage limits for the current fiscal year. Water Street has no unfunded liability relating to prior losses exceeding insurance coverage.

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 13: Supplemental Disclosure of Cash Flow Information

Cash paid for interest for the six-month period ended June 30, 2011 was \$354.

Noncash investing and financing activities for the six-month period ending June 30, 2011 are as follows:

Gifts of vehicle and equipment received	\$11,815
Gifts of investments received	<u>14,458</u>
	<u>\$26,273</u>
Computer equipment purchased under capital lease	<u>\$19,396</u>

NOTE 14: Pension Plan

Water Street maintains a defined contribution pension plan for all employees meeting certain eligibility requirements. Water Street contributes a specified dollar amount for each eligible employee. The plan allows voluntary employee contributions. Water Street matches contributions up to a certain percent of compensation. Pension expense for the six-month period ended June 30, 2011 was \$42,016.

NOTE 15: Contingencies

Water Street is involved in various claims and legal proceedings in the course of its activities. Although the ultimate disposition of these claims and proceedings cannot be predicted with certainty, it is the present opinion of Water Street's management that the outcome of any claim that is pending or threatened will not have a materially adverse effect on Water Street's financial position.

Water Street was a recipient of a \$500,000 subsidy to create low income housing through the Affordable Housing Program of the Federal Home Loan Bank of Pittsburgh. Water Street has agreed to be bound by the Affordable Housing Program's regulations, guidelines and requirements until July 27, 2022.

If Water Street does not continue to meet the subsidy's requirements, such as a sale of the project prior to the end of the retention period, the full amount of the subsidy may be required to be repaid.

NOTE 16: Endowment Funds

Water Street's endowment funds consist of a few donor-restricted permanent funds. The endowment funds of Water Street have been pooled with Water Street's other marketable investments. See Note 1 for a description of the types of investments utilized for endowment funds.

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 16: Endowment Funds (Continued)

Water Street's investments are invested in accordance with investment policies set out by a finance committee which has been appointed by the Board. Water Street's management is responsible for the day-to-day management of the portfolio including identifying, selecting and monitoring of the external investment manager to implement the strategic asset allocation set forth by the finance committee. Water Street's investment portfolio may include marketable securities that it intends to hold for an indefinite period of time.

The Commonwealth of Pennsylvania has not adopted the Uniform Management of Institutional Funds Act (UMIFA) or the Uniform Prudent Management of Institutional Funds Act (UPMIFA). Rather, the Pennsylvania Uniform Principal and Income Act (Pennsylvania Act) governs the investment, use and management of Water Street's endowment funds.

The Pennsylvania Act does not require the preservation of the fair value of a donor's original gift as of the gift date of a donor-restricted endowment fund, absent explicit donor stipulations to the contrary. However, based on its interpretation of the Pennsylvania Act and relevant accounting literature, Water Street classifies as permanently restricted net assets for reporting purposes: (i) the original value of gifts donated to the permanent endowment; (ii) the original value of subsequent gifts to the permanent endowment; and (iii) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Water Street.

Water Street has elected to follow an investment policy seeking a total return for the investment held, whether the return is derived from appreciation of capital or earnings and distributions with respect to capital or both. This policy is designed to take advantage of investment opportunities that provide a reasonable and dependable stream of income and continued growth of the funds, while not subjecting the principal of the endowment funds to undue risk of loss. Water Street's spending policy allows for annual disbursements from the account of 3.0% of the fair market value for the preceding year ending December 31.

The components of endowment net assets at June 30, 2011 are as follows:

	<u>Original Gift Value</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted:				
Operating	\$268,036	\$ -	\$293,200	\$293,200
Educational	<u>267,087</u>	<u>6,625</u>	<u>285,521</u>	<u>292,146</u>
	<u>\$535,123</u>	<u>\$ 6,625</u>	<u>\$578,721</u>	<u>\$585,346</u>

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 16: Endowment Funds (Continued)

Changes in endowment net assets for the six-month period ended June 30, 2011 are as follows:

	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>		
	<u>Education</u>	<u>General Operating</u>	<u>Education</u>	<u>Total</u>
Endowment net assets - January 1, 2011	\$ 2,470	\$284,493	\$276,972	\$563,935
Investment return:				
Investment income, net of investment fees	-	1,678	1,648	3,326
Net realized and unrealized gain (loss)	-	<u>11,260</u>	<u>11,056</u>	<u>22,316</u>
Total investment return		12,938	12,704	25,642
Amounts released for program expenditures	4,155	-	(4,155)	-
Amounts appropriated to current operations	-	<u>(4,231)</u>	-	<u>(4,231)</u>
Endowment net assets - June 30, 2011	<u>\$ 6,625</u>	<u>\$293,200</u>	<u>\$285,521</u>	<u>\$585,346</u>

NOTE 17: Fair Value of Financial Instruments

Financial Instruments

The following methods and assumptions were used by Water Street in estimating its fair value disclosures for financial instruments:

- Investments - long-term: The fair value of investments are based on quoted market prices for those or similar investments.
- Beneficial interests in split-interest agreements: The fair value is based on quoted market prices for those or similar investments covered by the agreement multiplied by Water Street's beneficial interest discounted using IRS life expectancy tables and applying a discount rate of 7%. Management feels this approach reasonably estimates the fair value of its split-interest agreements.

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 17: Fair Value of Financial Instruments (Continued)

Financial Instruments (Continued)

- Beneficial interests in assets held by others in perpetual trust: The fair value is based on quoted market prices for those or similar investments held in trust. Management feels this approach reasonably estimates the fair value of its beneficial interest.

The preceding valuation methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although Water Street 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 estimated fair value of Water Street's financial instruments at June 30, 2011 is as follows:

	<u>Carrying Amount</u>	<u>Fair Value</u>
Financial assets:		
Investments, long-term	\$5,553,914	\$5,553,914
Beneficial interest in split-interest agreements	599,372	599,372
Beneficial interest in assets held by others in perpetual trust	4,371,296	4,371,296
Financial liabilities:	-	-

Fair Value Measurements

The following table presents Water Street's fair value hierarchy for the financial instruments measured at fair value on a recurring basis:

	<u>Fair Value Measurements at Reporting Date Using</u>		
	<u>Fair Value</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
<u>June 30, 2011</u>			
Financial Assets:			
Investments, long-term	\$ 5,553,914	\$ 5,553,914	\$
Beneficial interest in split-interest agreements	599,372		599,372
Beneficial interest in assets held by others in perpetual trust	4,371,296		4,371,296

WATER STREET MINISTRIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2011

NOTE 17: Fair Value of Financial Instruments (Continued)

Fair Value Measurements

Financial instruments measured at fair value on a recurring basis using significant unobservable inputs:

Financial assets:

Beneficial interest in split-interest agreements -

Fair value at January 1, 2011	\$556,265
Receipt of split-interest agreements	19,026
Adjustment due to change in value of split-interest agreements	<u>24,081</u>
Fair value at June 30, 2011	<u>\$599,372</u>

Beneficial interest in assets held by others in perpetual trust -

Fair value at January 1, 2011	\$4,303,177
Adjustment due to change in value of beneficial interest in assets held by others in perpetual trust	<u>68,119</u>
June 30, 2011	<u>\$4,371,296</u>

Adjustments due to changes in the value of split-interest agreements and in beneficial interest in assets held by others in perpetual trust are reported in the statement of activities as a component of other changes.

NOTE 18: Subsequent Events

Subsequent events have been evaluated through September 29, 2011, which represents the date the accompanying financial statements were available to be issued.