

**SOUTHEASTERN CALIFORNIA
CONFERENCE OF SEVENTH-DAY
ADVENTISTS
AND SUBSIDIARIES**

**CONSOLIDATED FINANCIAL STATEMENTS
WITH
INDEPENDENT AUDITORS' REPORT**

**FOR THE YEARS ENDED
DECEMBER 31, 2010 AND 2009, RESTATED**

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Michael R. Adcock, CPA
Shannon M. Carlson, CPA
Linda S. Devlin, CPA
Andrew Steinke, CPA
Of Counsel
Thomas E. Ahern, CPA
Janell M. Fratt, CPA
Nora L. Teasley, CPA
A California Limited Liability Partnership
Certified Public Accountants



Members
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Certified Public Accountants
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Certified Public Accountants

Independent Auditors' Report

To the Executive Committee
Southeastern California Conference of
Seventh-day Adventists and Subsidiaries

We have audited the accompanying consolidated statements of financial position of Southeastern California Conference of Seventh-day Adventists and subsidiaries (the "Conference") as of and for the years ended December 31, 2010 and 2009, and the related consolidated statements of activities and changes in net assets and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Conference's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits 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 consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 audits provide 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 Southeastern California Conference of Seventh-day Adventists and subsidiaries as of December 31, 2010 and 2009, and the changes in its net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Ahern Adcock Devlin LLP

Riverside, California
September 19, 2011

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Consolidated Statements of Financial Position

| | December 31, | 2010 | 2009 |
|---|---------------------|----------------------|----------------------|
| ASSETS | | | |
| Current assets | | | |
| Cash and cash equivalents | \$ | 6,039,054 | \$ 3,665,543 |
| Restricted cash | | | 12,500 |
| Investments, current portion | | 51,995,519 | 47,343,939 |
| Accounts receivable, net current portion | | 10,147,441 | 9,794,574 |
| Interest receivable, current portion | | 280,671 | 294,054 |
| Other receivables | | 6,000 | 12,128 |
| Advances to churches, current portion | | 145,977 | 145,977 |
| Notes receivable, net current portion | | 6,531,665 | 5,572,387 |
| Inventory | | 369,018 | 334,096 |
| Prepaid expenses | | 123,875 | 106,488 |
| Total current assets | | <u>75,639,220</u> | <u>67,281,686</u> |
| | | | |
| Plant assets, net | | <u>210,057,360</u> | <u>197,492,613</u> |
| | | | |
| Other assets | | | |
| Restricted cash equivalents | | 3,123,056 | 10,636,293 |
| Investments, noncurrent portion | | | 1,109,416 |
| Accounts receivable, noncurrent portion | | 789,071 | 423,227 |
| Interest receivable, noncurrent portion | | | 514,261 |
| Advances to churches, noncurrent portion | | 548,883 | 581,383 |
| California annuity reserve investments | | 2,456,582 | 2,489,314 |
| Investments in real estate | | 22,900,284 | 22,793,876 |
| Notes receivable, noncurrent portion | | 69,035,133 | 61,130,605 |
| Assets held in trust | | 17,003,191 | 19,452,172 |
| Receivable for affiliate lease guarantees | | 415,155 | |
| Bond issuance costs, net | | 557,110 | 583,657 |
| Total other assets | | <u>116,828,465</u> | <u>119,714,204</u> |
| | | | |
| Total assets | | <u>\$402,525,045</u> | <u>\$384,488,503</u> |

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

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Consolidated Statements of Financial Position

| | December 31, | 2010 | 2009 |
|---|---------------------|----------------------|----------------------|
| LIABILITIES | | | |
| Current liabilities | | | |
| Accounts payable | | \$ 2,946,918 | \$ 3,302,108 |
| Accrued wages and benefits | | 4,130,297 | 3,594,305 |
| Other accrued liabilities | | 89,685 | 53,789 |
| Deposits | | 239,158 | 238,650 |
| Deferred revenue | | 598,404 | 598,404 |
| Lines of credit | | 2,724,397 | 1,827,600 |
| Notes payable, current portion | | 2,839,161 | 2,381,483 |
| Bonds payable, current portion | | 855,000 | 850,000 |
| Capital lease obligations, current portion | | 72,698 | |
| Refundable advances | | 42,731 | 105,393 |
| Total current liabilities | | 14,538,449 | 12,951,732 |
| Other liabilities | | | |
| Notes payable, noncurrent portion | | 27,279,365 | 26,664,324 |
| Bonds payable, noncurrent portion | | 49,800,000 | 50,655,000 |
| Capital lease obligations, noncurrent portion | | 389,862 | |
| Present value of annuity liability | | 1,971,670 | 1,802,878 |
| Liabilities to depositors | | 915,160 | 864,783 |
| Liabilities held in trust | | 15,305,926 | 16,429,277 |
| Guarantees for affiliate leases | | 415,155 | |
| Other noncurrent liabilities | | 1,865,085 | 321,120 |
| Total other liabilities | | 97,942,223 | 96,737,382 |
| Total liabilities | | 112,480,672 | 109,689,114 |
| NET ASSETS | | | |
| Unrestricted | | | |
| Undesignated | | 230,608,468 | 220,029,169 |
| Designated | | 55,325,996 | 50,512,789 |
| | | 285,934,464 | 270,541,958 |
| Temporarily restricted | | 4,047,577 | 4,195,099 |
| Permanently restricted | | 62,332 | 62,332 |
| Total net assets | | 290,044,373 | 274,799,389 |
| Total liabilities and net assets | | \$402,525,045 | \$384,488,503 |

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Consolidated Statements of Activities and Changes in Net Assets

| | For the Years Ended December 31, | 2010 | 2009 |
|---|---|-----------------|----------------|
| UNRESTRICTED NET ASSETS | | | |
| Revenues, gains, and support | | | |
| Gross tithe income | | \$ 46,047,512 | \$ 46,490,239 |
| Tithe percentages passed on | | (11,875,477) | (12,023,952) |
| Net tithe income | | 34,172,035 | 34,466,287 |
| Offerings and donations | | 164,545 | 83,251 |
| Subsidies | | 924,115 | 652,875 |
| Auxiliary income | | 1,845,310 | 1,641,275 |
| Matured trusts, wills, and bequests | | 1,591,889 | 371,211 |
| Payroll, benefits, and other expense reimbursement | | 27,511,161 | 27,271,892 |
| Tuition | | 1,427,137 | 1,623,459 |
| Other | | 397,283 | 315,394 |
| Revenues, gains, and support before reclassifications | | 68,033,475 | 66,425,644 |
| Released from restrictions | | 4,819,024 | 5,489,291 |
| Revenues, gains, and support after reclassifications | | 72,852,499 | 71,914,935 |
| Expenses | | | |
| Program services | | | |
| Church ministries | | 36,107,646 | 37,684,672 |
| Education | | 36,808,509 | 36,989,071 |
| Outreach ministries | | 2,786,278 | 3,346,563 |
| Auxiliary services | | 1,893,331 | 1,885,908 |
| Total program services | | 77,595,764 | 79,906,214 |
| Supporting services | | | |
| General and administrative | | 6,759,091 | 6,626,380 |
| Fundraising | | 208,281 | 56,311 |
| Total supporting services | | 6,967,372 | 6,682,691 |
| Total expenses | | 84,563,136 | 86,588,905 |
| Change in net assets before nonoperating activity | | \$ (11,710,637) | \$(14,673,970) |

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Consolidated Statements of Activities and Changes in Net Assets

| For the Years Ended December 31, | 2010 | 2009 |
|--|----------------------|----------------------|
| Change in net assets before nonoperating activity | \$ (11,710,637) | \$ (14,673,970) |
| Nonoperating activity | | |
| Donated plant assets and investment real estate | 18,106,407 | 23,194,098 |
| Investment income | 7,363,735 | 9,724,872 |
| Other interest income | | 109,892 |
| Rental income | 9,120,404 | 8,420,797 |
| Rental properties expenses | (3,650,636) | (3,365,717) |
| Net gain (loss) on sale of plant assets and investment real estate | (83,496) | (84,794) |
| Loss on impairment of long-term assets | | (230,229) |
| Bond costs | (907,298) | (870,645) |
| Other expense | (1,469,425) | (950,194) |
| Interest expense | (1,376,548) | (1,317,857) |
| Increase from nonoperating activity | <u>27,103,143</u> | <u>34,630,223</u> |
| Increase in unrestricted net assets | <u>15,392,506</u> | <u>19,956,253</u> |
| TEMPORARILY RESTRICTED NET ASSETS | | |
| Offerings and donations | 1,403,783 | 1,584,717 |
| Subsidies | 3,216,896 | 3,494,254 |
| Investment income | 7,264 | 8,973 |
| Matured trusts, wills, and bequests | 1,769 | 157,974 |
| Other | 41,790 | 100 |
| Total temporarily restricted income | <u>4,671,502</u> | <u>5,246,018</u> |
| Released from restrictions | <u>(4,819,024)</u> | <u>(5,489,291)</u> |
| Decrease in temporarily restricted net assets | <u>(147,522)</u> | <u>(243,273)</u> |
| Increase in net assets | <u>15,244,984</u> | <u>19,712,980</u> |
| Net assets, beginning of year, as previously stated | 274,285,336 | 255,847,148 |
| Prior period adjustments | 514,053 | (760,739) |
| Net assets, beginning of year, as restated | <u>274,799,389</u> | <u>255,086,409</u> |
| Net assets, end of year | <u>\$290,044,373</u> | <u>\$274,799,389</u> |

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

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Consolidated Statements of Cash Flows

| | For the Years Ended December 31, | 2010 | 2009 |
|---|---|------------------|--------------------|
| Cash flows from operating activities | | | |
| Increase in net assets | | \$ 15,244,984 | \$ 19,712,980 |
| Adjustment to reconcile change in net assets to net cash used in operating activities: | | | |
| Depreciation and amortization | | 6,823,642 | 5,706,739 |
| Provision for doubtful accounts | | 456,346 | 804,471 |
| Donated plant assets | | (18,106,407) | (20,936,098) |
| Donated real estate held for investment | | | (258,000) |
| Loss on impairment of long-term asset | | | 230,229 |
| Unrealized loss on swap contracts | | 1,543,965 | 321,120 |
| Loss on sale of plant assets and investment real estate | | 83,496 | 84,794 |
| Unrealized gain on investments | | (3,330,229) | (7,455,428) |
| Realized (gain) loss on sale of investments | | (690,490) | 1,691,235 |
| Unrealized gain on assets held in trust | | (3,547) | (214,099) |
| Unrealized (gain) loss on gift annuities | | 168,792 | (138,445) |
| (Increase) decrease in: | | | |
| Accounts receivable | | (725,678) | (35,801) |
| Interest receivable | | 527,644 | 221,162 |
| Other receivables | | 6,128 | (4,148) |
| Inventory | | (34,922) | (16,639) |
| Prepaid expenses | | (17,387) | 16,139 |
| Increase (decrease) in: | | | |
| Accounts payable | | (355,190) | (350,627) |
| Accrued wages and benefits | | 535,992 | 26,710 |
| Deposits | | 508 | 37,501 |
| Deferred revenue | | | 6,021 |
| Other accrued liabilities | | 35,896 | 2,814 |
| Liabilities to depositors | | 50,377 | 79,391 |
| Refundable advances | | (62,662) | 29,333 |
| Net cash provided by (used in) operating activities | | <u>2,151,258</u> | <u>(2,438,646)</u> |

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Consolidated Statements of Cash Flows

| | For the Years Ended December 31, | 2010 | 2009 |
|--|---|---------------------|---------------------|
| Cash flows from investing activities | | | |
| Change in restricted cash | | \$ 7,525,737 | \$ (2,819,733) |
| Proceeds from sale of investments | | 16,670,850 | 22,455,392 |
| Purchase of investments | | (16,283,005) | (8,918,546) |
| Proceeds from sale of plant assets | | | 1,559,787 |
| Purchase of plant assets | | (240,681) | (103,172) |
| Proceeds from sale of real estate investments | | | 925,413 |
| Purchase of real estate investments | | (90,758) | (5,287,897) |
| Advances to churches | | 32,500 | 710,523 |
| Advances from notes receivable | | (9,680,752) | (16,624,642) |
| Payments received on notes receivable | | <u>1,390,981</u> | <u>649,959</u> |
| Net cash used in investing activities | | <u>(675,128)</u> | <u>(7,452,916)</u> |
| Cash flows from financing activities | | | |
| Principal payments on notes payable | | (120,593) | (113,587) |
| Net change in lines of credit | | 1,066,695 | 1,494,708 |
| Principal payments on bonds payable | | (850,000) | (1,075,000) |
| Principal payments on capital lease obligations | | (55,246) | |
| Proceeds from gift annuities | | 3,627,956 | 2,223,762 |
| Purchase of investments for gift annuities | | (2,775,337) | (1,716,237) |
| Loan costs | | <u>3,906</u> | <u>110,282</u> |
| Net cash provided by financing activities | | <u>897,381</u> | <u>923,928</u> |
| Net increase (decrease) in cash and cash equivalents | | 2,373,511 | (8,967,634) |
| Cash and cash equivalents | | | |
| Balance, beginning of year | | <u>3,665,543</u> | <u>12,633,177</u> |
| Balance, end of year | | <u>\$ 6,039,054</u> | <u>\$ 3,665,543</u> |

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Consolidated Statements of Cash Flows

| | For the Years Ended December 31, | 2010 | 2009 |
|---|---|-------------|-------------|
| Supplemental disclosure | | | |
| Cash paid for interest | | \$1,551,632 | \$1,303,723 |
| Noncash transactions | | | |
| Notes receivable increased by guarantee of related party notes payable | | \$1,791,569 | \$1,361,888 |
| Notes receivable reduced through related party payment on lines of credit | | \$169,898 | \$778,000 |
| Notes receivable reduced through related party payment on bond payable | | | \$537,706 |
| Notes receivable increased by related party notes payable | | \$598,257 | \$2,524,235 |
| Plant assets transferred to investments in real estate | | \$30,533 | \$735,990 |
| Assets held in trust transferred to plant assets | | \$600,000 | |
| Receivable increased by guarantee of related party equipment leases | | \$415,155 | |
| Capital lease incurred for the acquisition of office equipment | | \$517,806 | |

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

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Notes to Consolidated Financial Statements

1. Reporting Entity and Significant Accounting Policies

The Southeastern California Conference of Seventh-day Adventists and subsidiaries (the “Conference”) was formed by Seventh-day Adventist Church congregations within Imperial, Orange, Riverside, San Bernardino and San Diego Counties in 1915. Each congregation elects its own board of directors in addition to a calculated number of delegates to represent the congregation in governing the Conference. The Conference’s primary purpose is the expansion of God’s Kingdom through the preaching, teaching, publishing, and living of the everlasting gospel throughout the cross-cultural communities of its territory.

The Conference supports the operation of all congregations and schools in its territory. The Conference holds title to all denominational property in its territory and performs certain fiduciary duties. As part of the mission of the Conference, 25 schools providing education in a religious school environment are operated for grades ranging from kindergarten through grade twelve. The schools are governed by the board of education which is approved and authorized by the executive committee of the Conference. The board of education develops policy and creates rules and regulations to which the schools must adhere. These consolidated financial statements include the operations of only one school, Calexico Mission School.

The Conference is a member organization of Pacific Union Conference of Seventh-day Adventists; see Affiliated Conferences.

The Conference formed SECC-ECF, LLC on October 17, 2007 as a nonprofit limited liability company. The sole purpose of SECC-ECF, LLC is to provide funding for the educational facilities of the Conference. The sole member is the Conference, and no other members may be admitted.

Consolidation

The accompanying consolidated financial statements include the accounts of the Conference, Calexico Mission School, and SECC-ECF, LLC, all of which are under common control. All significant intercompany transactions and balances have been eliminated in consolidation.

Financial Statement Presentation

The consolidated financial statement presentation follows the recommendations of the Financial Accounting Standards Board in its Statement of Financial Accounting Standards Board Accounting Standards (FASB ASC) No. 958, *Not-for-Profit Entities*. Under FASB ASC No. 958, the Conference is required to report information regarding its financial position and activities according to the following classes of net assets:

Unrestricted net assets include resources that are not temporarily or permanently restricted by the donor and are available for operations of the Conference without limitation.

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Notes to Consolidated Financial Statements

1. Reporting Entity and Significant Accounting Policies (Continued)

Temporarily restricted net assets include those resources whose use is restricted by donor-imposed criteria that either expires with the passage of time or by actions of the Conference.

Permanently restricted net assets include those resources in which donor-imposed stipulations require that the resources be maintained permanently but permit the Conference to use part or all of the income derived from the donor assets for either specified or unspecified purposes.

Cash and Cash Equivalents

The Conference has cash in financial institutions which is insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 at each institution. Beginning December 31, 2010 through December 31, 2012, all noninterest-bearing transaction accounts are fully insured, regardless of the balance of the account, at all FDIC-insured institutions. At various times throughout the year, the Conference may have cash balances in financial institutions which exceed the FDIC insurance limit. Management reviews the financial condition of these financial institutions on a periodic basis and does not believe this concentration of cash results in a high level of risk for the Conference.

The Conference considers all highly liquid investments with an initial maturity date of three months or less to be cash equivalents.

The Conference maintains separate bank accounts for undistributed tax-exempt and taxable bond proceeds, which are represented as noncurrent restricted cash equivalents in the accompanying consolidated statements of financial position. The balance in these accounts at December 31, 2010 was \$3,123,034 and \$22, respectively. The use of this cash is restricted for construction.

Estimations of Fair Values

The following summarizes the major methods and assumptions used in estimating fair values of financial instruments:

Short-term financial instruments are valued at their carrying amounts included in the statements of financial position, which are reasonable estimates of fair value due to the relatively short period to maturity of the instruments. This applies to cash, cash equivalents, receivables, and certain current liabilities.

Marketable securities are valued at quoted market price or other reasonably obtainable market value estimate at the reporting date for those or similar securities. The difference between aggregate market value and historical cost for each type of security is recorded in a valuation account. The change in this account during each period is recognized as an unrealized gain or loss.

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Notes to Consolidated Financial Statements

1. Reporting Entity and Significant Accounting Policies (Continued)

Notes and bonds payable are valued at the amortized amount payable as of the reporting date. Because these loans, by intent and practice, are expected to be amortized to maturity, the carrying amount approximates the discounted value of the future cash flows expected to be paid. Because of the difficulty and inherent subjectivity involved in determining fair values, which is not susceptible to independent substantiation, management has concluded that the amortized face value of loans payable to related or affiliated entities approximates fair value. Further, because a reasonable estimate of fair value could not be made without incurring excessive costs, management has not attempted to estimate the fair value of any loans payable to creditors that are not related or affiliated entities.

Derivative Instruments

The Conference has entered into derivative financial instruments in the form of interest rate swaps to manage its exposure to interest rate risk. Further details of the interest rate swaps are disclosed at Note 13 to the consolidated financial statements. Derivatives are initially recognized at fair value at the date the derivative contract is entered into and are subsequently remeasured to fair value at each balance sheet date.

The resulting gain or loss is recognized in the consolidated statements of activities immediately unless the derivative is designated effective as a hedging instrument. The Conference has not designated its interest rate swaps as hedge instruments. A derivative with a positive fair value is recognized as a financial asset and a derivative with a negative fair value is recognized as a financial liability. If the maturity of the instrument is more than 12 months and it is not expected to be realized or settled within 12 months, the derivative is considered to be noncurrent for financial statement presentation.

Gift Annuities

Gift annuities are recorded using the actuarial method. Under this method, assets are recorded at fair value at the date of the gift. The corresponding credit is to annuities payable for the present value of the future annuity payments based upon acceptable life expectancy tables. Investment income and gains are credited, and the contractual periodic payments to the annuitant and investment losses are charged to the annuities payable liability. The actuarial present value of annuities payable is recalculated periodically based upon revised life expectancies and interest assumptions.

Upon maturity of an annuity, the remaining net assets are generally distributed to current operating funds. The Conference administers numerous gift annuities for residents of California. California statutes allow investments in high grade government and corporate bonds, publicly traded securities on major exchanges, and insured mortgages. The Conference is in compliance with these statutes.

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Notes to Consolidated Financial Statements

1. Reporting Entity and Significant Accounting Policies (Continued)

Split-interest Agreements

The Conference is at least a partial beneficiary in various kinds of trusts, annuities, and/or other split-interest agreements for which it acts as trustee or administrator. Other organizations are partial beneficiaries of some of these agreements. For those agreements that are unconditional and irrevocable, assets are recorded by the Conference at fair value at the date of gift or acceptance of agreement. For agreements that designate other beneficiaries, liabilities are recorded for the present value of amounts due to others. Conservative discount rates are used to compute the present value of such liabilities. Standard actuarial tables and conservative interest rates are used to compute liabilities due to annuitants. The Conference's remainder interest is classified as temporarily restricted. (See Notes 10, 15, and 16.) For those agreements that are revocable, assets are recorded at fair value at date of acceptance or agreement, except for investments which are adjusted to fair value annually.

Affiliated Organizations

The Conference operates through several organizations with which it is affiliated, by reason of economic interest and/or shared membership on the respective governing committees. The financial statements of these organizations are not combined with the Conference. Interorganization transactions carried on in the ordinary course of business are handled through current accounts receivable and payable and are settled on a monthly basis. Other financial transactions involve appropriations, loans, and other long-term financing. Related party transactions are summarized in Note 21. These other organizations are as follows:

General Conference of Seventh-day Adventists (GC)

GC is the world headquarters of the Seventh-day Adventist denomination and as such determines the operating and accounting policies to be followed by church institutions.

North American Division of the General Conference of Seventh-day Adventists (NAD)

NAD is the organization responsible for church activities in North America. NAD determines policies for institutions within North America in accordance with GC policies.

Pacific Union Conference of Seventh-day Adventists (PUC) and Pacific Union Association of Seventh-day Adventists (PUA)

PUC is the organization responsible for church activities in the states of Arizona, California, Hawaii, Nevada, and Utah. PUA determines policies for institutions within the above states in accordance with NAD policies.

La Sierra University (LSU)

The president of the Conference is a member of the board of trustees of LSU.

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Notes to Consolidated Financial Statements

1. Reporting Entity and Significant Accounting Policies (Continued)

Accounts, Notes, Interest, and Other Receivables

Accounts, notes, interest, and other receivables are reported at their net realizable value, less an allowance for uncollectible accounts and notes receivable. The Conference uses the allowance method for the write-off of bad debts. The Conference considers such factors as historical trends for collections and knowledge of financial stability of debtors to establish the allowance for doubtful accounts. Receivables are written off when management determines that the amount will not be collectible.

Plant Assets and Depreciation

Property, plant, and equipment in excess of \$2,500 and having a useful life in excess of one year are recorded at cost when purchased or fair value at date of gift. Cost includes labor, materials, and indirect charges for such items as engineering, supervision, and transportation. The Conference follows the policy of capitalizing interest as a component of property and equipment constructed for its own use. Depreciation expense is calculated using the straight-line method. Depreciation of land improvements, buildings, and equipment is provided over the estimated useful lives of the respective assets, ranging from 3 to 75 years.

The Conference holds legal title to the real properties used by the Conference, congregations, schools, and academies. The book value of these properties is included in these consolidated financial statements.

Revenue Recognition

The Conference recognizes tithes and offerings when recorded by each congregation. Rental income is recognized as earned.

Expiration of Donor-Imposed Restrictions

The Conference reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is when a stipulated time restriction ends or purpose restrictions are accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activities and changes in net assets as net assets released from restrictions.

The Conference reports contributions of land, buildings, 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 revenues in temporarily restricted net assets. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Conference reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

**SOUTHEASTERN CALIFORNIA CONFERENCE
OF SEVENTH-DAY ADVENTISTS
and Subsidiaries**

Notes to Consolidated Financial Statements

1. Reporting Entity and Significant Accounting Policies (Continued)

Income Tax

The Conference is a religious not-for-profit organization and is exempt from federal income taxes under the provisions of Section 501(c)(3) of the Internal Revenue and Code Section 23701(d) of the California Revenue and Taxation Code. However, income from certain activities not directly related to the Conference's tax exempt purpose is subject to taxation as unrelated business income.

New Accounting Pronouncements

In May 2009, the FASB issued FASB ASC No. 855, *Subsequent Events*, to incorporate the accounting and disclosure requirements for subsequent events into accounting principles generally accepted in the United States of America. FASB ASC No. 855 introduces new terminology, defines a date through which management must evaluate subsequent events, and lists the circumstances under which an entity must recognize and disclose events or transactions occurring after the balance sheet date. FASB ASC No. 855 was effective for annual reporting periods ending after June 15, 2009. The Conference adopted FASB ASC No. 855 for the year ended December 31, 2009, as required.

In June 2009, the FASB issued an accounting pronouncement establishing the FASB Accounting Standards Codification (FASB ASC) as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities. This pronouncement was effective for financial statements issued for annual periods ending after September 15, 2009. On the effective date, all non-SEC accounting and reporting standards were superseded. The Conference adopted this new accounting pronouncement for the year ended December 31, 2009, as required. The adoption did not impact the Conference's financial position and changes in net assets. The Conference has revised its references to pre-Codification accounting principles generally accepted in the United States of America in its consolidated financial statements.

In September 2009, the FASB issued Accounting Standards Update (ASU) 2009-06, *Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities*, which modifies the guidance on uncertain tax positions in FASB ASC No. 740, *Income Taxes* (formerly FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes*). Previously, the Conference had accounted for tax contingencies in accordance with FASB ASC No. 450, *Contingencies*. As required by the uncertain tax position guidance in FASB ASC No. 740, the Conference recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority. At December 31, 2008, the Conference had elected to defer the adoption of the standard. The Conference adopted the provisions of FASB ASC No. 740 on January 1, 2009. The adoption did not have a material impact on the Conference's financial condition and results of operations.

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1. Reporting Entity and Significant Accounting Policies (Continued)

In March 2008, the FASB issued FASB ASC No. 815, *Derivatives and Hedging*, formerly FASB Statement No. 161, *Disclosures about Derivative Instruments and Hedging Activities* (FAS 161). The use and complexity of derivative instruments and hedging activities have increased significantly over the past several years. Constituents have expressed concerns that the existing disclosure requirements in FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* do not provide adequate information about how derivative and hedging activities affect an entity's financial position, financial performance, and cash flows. Accordingly, this FAS 161 requires enhanced disclosures about an entity's derivative and hedging activities and thereby improves the transparency of financial reporting. This statement is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. This statement encourages, but does not require, comparative disclosures for earlier periods at initial adoption. Management has considered the impact of this statement on the Conference's consolidated financial statements and has incorporated the required disclosures in 2009.

In January 2010, the FASB issued Accounting Standards Update (ASU) 2010-06, *Fair Value Measurements and Disclosures (Topic 820) – Improving Disclosures about Fair Value Measurements*, which modifies the guidance on disclosures of fair value measurements of assets and liabilities. The changes provide a greater level of disaggregated information and more robust disclosures about valuation techniques and inputs to fair value measurements. It includes separate information indicating the reasons for changes in level 3 fair value measurements and significant transfers between the three levels, including the reason for the transfers. Management has considered the impact of this statement on the Conference's consolidated financial statements, and there were no significant changes required to disclosures upon adoption in 2010.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and disclosures made in the accompanying notes to the consolidated financial statements. While management believes these estimates are adequate, actual results could differ from those estimates.

Reclassifications and Restatement

Certain reclassifications have been made to the 2009 consolidated financial statements to conform to the 2010 presentation. In addition, the accompanying consolidated financial statements for 2009 have been restated to correct an error made in 2009 for donated assets, resulting in a \$514,053 increase in net assets for 2009. The 2009 presentation was restated to reflect the value of real property held in revocable trusts, resulting in a \$9,416,201 increase in assets held in trust and liabilities held in trust.

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Notes to Consolidated Financial Statements

2. Cash and Cash Equivalents

At December 31, cash was included in the consolidated statements of financial position in the following captions:

| | <u>2010</u> | <u>2009</u> |
|--|--------------------|---------------------|
| Cash and cash equivalents | \$6,039,054 | \$ 3,665,543 |
| Restricted cash – current | | 12,500 |
| Restricted cash equivalents – noncurrent | <u>3,123,056</u> | <u>10,636,293</u> |
| | <u>\$9,162,110</u> | <u>\$14,314,336</u> |

At December 31, cash held by the Conference was comprised of the following:

| | <u>2010</u> | <u>2009</u> |
|-------------------------------|--------------------|---------------------|
| Imprest cash | \$ 11,936 | \$ 10,436 |
| Checking account | 5,426,009 | 3,052,535 |
| Money market savings accounts | <u>3,724,165</u> | <u>11,251,365</u> |
| | <u>\$9,162,110</u> | <u>\$14,314,336</u> |

3. Investments

At December 31, 2010, investments consisted of the following:

| | <u>Cost</u> | <u>Fair Value</u> |
|--|---------------------|---------------------|
| <i>California Annuity Reserve</i> | | |
| Checking accounts | \$ 13,787 | \$ 13,787 |
| Money market savings accounts | 57,344 | 57,344 |
| Fixed income | 1,082,583 | 1,113,896 |
| Equity securities | <u>1,104,945</u> | <u>1,271,555</u> |
| | 2,258,659 | 2,456,582 |
| Unrealized appreciation in value | <u>197,923</u> | |
| Carrying amount at fair value | <u>\$2,456,582</u> | <u>\$2,456,582</u> |
| <i>Other Investments</i> | | |
| Mutual funds | \$ 4,305,403 | \$ 4,361,695 |
| Fixed income mutual funds | 17,124,748 | 17,071,439 |
| Corporate bonds | 501,309 | 500,820 |
| Pacific Union Income Fund | 8,991,367 | 9,190,688 |
| Equity securities | 10,417,018 | 12,257,546 |
| International equity mutual funds | 8,133,512 | 7,599,744 |
| International equities | 375,697 | 57,952 |
| Money market cash funds | <u>955,635</u> | <u>955,635</u> |
| | 50,804,689 | 51,995,519 |
| Unrealized appreciation in value | <u>1,190,830</u> | |
| Carrying amount at fair value | <u>\$51,995,519</u> | <u>\$51,995,519</u> |

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Notes to Consolidated Financial Statements

3. Investments (Continued)

Derivative Instruments

| | | |
|----------------------------------|----------------------|----------------------|
| Interest rate swap | \$ - | \$ - |
| Unrealized depreciation in value | (1,865,085) | (1,865,085) |
| Carrying amount at fair value | <u>\$(1,865,085)</u> | <u>\$(1,865,085)</u> |

At December 31, investments are presented in the consolidated statements of financial position as follows:

| | |
|--|---------------------|
| | <u>2010</u> |
| Investments, current portion | \$51,995,519 |
| California annuity reserve investments | 2,456,582 |
| Other noncurrent liabilities | <u>(1,865,085)</u> |
| | <u>\$52,587,016</u> |

As discussed in Note 4 to these consolidated financial statements, the Conference is required to report its fair value measurements in one of three levels, which are based on the ability to observe in the marketplace the input to the Conference's valuation techniques. Level 1, the most observable level of inputs, is for investments measured at quoted prices in the active markets to identical investments as of December 31, 2010. Level 2 is for investments measured using inputs such as quoted prices for similar assets, quoted prices for the identical asset in inactive markets, and investments measured at net asset value that can be redeemed in the near term. Level 3 is for investments measured using inputs that are unobservable, and is used in situations for which there is little, if any, market activity for the investment.

The following table summarizes the levels in the fair value hierarchy of the Conference's investments at December 31, 2010:

| | <u>Total</u> | <u>Level 1</u> | <u>Level 2</u> |
|-----------------------------------|----------------------|---------------------|----------------------|
| <i>Assets</i> | | | |
| Money market funds | \$ 1,026,767 | \$ 1,026,767 | |
| Mutual funds | 4,361,695 | 4,361,695 | |
| Fixed income mutual funds | 18,185,335 | 18,185,335 | |
| Equity securities | 13,529,100 | 13,529,100 | |
| Corporate bonds | 500,820 | 500,820 | |
| Pacific Union Income Fund | 9,190,688 | | \$9,190,688 |
| International equity mutual funds | 7,599,744 | 7,599,744 | |
| International equities | 57,952 | 57,952 | |
| | <u>\$54,452,101</u> | <u>\$45,261,413</u> | <u>\$9,190,688</u> |
| <i>Liabilities</i> | | | |
| Derivative (interest rate swap) | <u>\$(1,865,085)</u> | | <u>\$(1,865,085)</u> |

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Notes to Consolidated Financial Statements

3. Investments (Continued)

At December 31, 2010, the Conference does not have any investments measured using level 3 inputs.

At December 31, 2009, investments consisted of the following:

| | Cost | Fair Value |
|--|---------------------|---------------------|
| <i>California Annuity Reserve</i> | | |
| Checking accounts | \$ 12,566 | \$ 12,566 |
| Money market savings accounts | 23,968 | 23,968 |
| Mutual funds | 26,622 | 27,051 |
| Fixed income | 1,173,834 | 1,202,761 |
| Equity securities | <u>1,143,892</u> | <u>1,222,968</u> |
| | 2,380,882 | 2,489,314 |
| Unrealized appreciation in value | <u>108,432</u> | |
| Carrying amount at fair value | <u>\$2,489,314</u> | <u>\$2,489,314</u> |
| | | |
| | Cost | Fair Value |
| <i>Other Investments</i> | | |
| Mutual funds | \$ 5,505,108 | \$ 4,800,495 |
| Fixed income mutual funds | 15,893,240 | 15,409,085 |
| Corporate bonds | 1,991,230 | 2,021,354 |
| Pacific Union Income Fund | 8,981,459 | 9,027,719 |
| Equity securities | 11,560,473 | 12,042,912 |
| International equity mutual funds | 6,388,361 | 4,890,691 |
| International equities | 47,778 | 42,947 |
| Money market cash funds | <u>218,152</u> | <u>218,152</u> |
| | 50,585,801 | 48,453,355 |
| Unrealized depreciation in value | <u>(2,132,446)</u> | |
| Carrying amount at fair value | <u>\$48,453,355</u> | <u>\$48,453,355</u> |
| | | |
| <i>Derivative Instruments</i> | | |
| Interest rate swap | \$ - | \$ - |
| Unrealized depreciation in value | <u>(321,120)</u> | <u>(321,120)</u> |
| Carrying amount at fair value | <u>\$(321,120)</u> | <u>\$(321,120)</u> |

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Notes to Consolidated Financial Statements

3. Investments (Continued)

At December 31, investments are presented in the consolidated statements of financial position as follows:

| | |
|--|---------------------|
| | <u>2009</u> |
| Investments, current portion | \$47,343,939 |
| Investments, noncurrent portion | <u>1,109,416</u> |
| | 48,453,355 |
| California annuity reserve investments | 2,489,314 |
| Other noncurrent liabilities | <u>(321,120)</u> |
| | <u>\$50,621,549</u> |

The following table summarizes the levels in the fair value hierarchy of the Conference's investments at December 31, 2009:

| | Total | Level 1 | Level 2 |
|-----------------------------------|---------------------|---------------------|--------------------|
| <i>Assets</i> | | | |
| Money market funds | \$ 254,686 | \$ 254,686 | |
| Mutual funds | 4,827,546 | 4,827,546 | |
| Fixed income mutual funds | 16,611,846 | 16,611,846 | |
| Equity securities | 13,265,880 | 13,265,880 | |
| Corporate bonds | 2,021,354 | 2,021,354 | |
| Pacific Union Income Fund | 9,027,719 | | \$9,027,719 |
| International equity mutual funds | 4,890,691 | 4,890,691 | |
| International equities | <u>42,947</u> | <u>42,947</u> | |
| | <u>\$50,942,669</u> | <u>\$41,914,950</u> | <u>\$9,027,719</u> |
| <i>Liabilities</i> | | | |
| Derivative (interest rate swap) | <u>\$(321,120)</u> | | <u>\$(321,120)</u> |

At December 31, 2009, the Conference did not have any investments measured using level 3 inputs.

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Notes to Consolidated Financial Statements

3. Investments (Continued)

For the years ended December 31, 2010 and 2009 net investment income (loss) is presented in the consolidated statements of activities and changes in net assets as follows:

| | 2010 | | | Total |
|--|---------------------|---------------------------|---------------------------|---------------------|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | |
| Investment income | \$ 3,412,542 | | | \$ 3,412,542 |
| Unrealized gains | 3,445,045 | | | 3,445,045 |
| Realized gains | 614,149 | | | 614,149 |
| Investment fees | (128,287) | | | (128,287) |
| Other | 20,286 | | | 20,286 |
| | <u>7,363,735</u> | \$ - | \$ - | <u>7,363,735</u> |
| Unrealized loss on interest rate swap included in other expense | (1,543,965) | | | (1,543,965) |
| Investment income, net | <u>\$ 5,819,770</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 5,819,770</u> |

| | 2009 | | | Total |
|--|---------------------|---------------------------|---------------------------|---------------------|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | |
| Investment income | \$ 3,990,639 | \$7,710 | | \$ 3,998,349 |
| Unrealized gains | 7,454,165 | 1,263 | | 7,455,428 |
| Realized gains | (1,691,235) | | | (1,691,235) |
| Investment fees | (121,783) | | | (121,783) |
| Other | 93,086 | | | 93,086 |
| | <u>9,724,872</u> | <u>8,973</u> | <u>\$ -</u> | <u>9,733,845</u> |
| Unrealized loss on interest rate swap included in other expense | (321,120) | | | (321,120) |
| Investment income, net | <u>\$ 9,403,752</u> | <u>\$8,973</u> | <u>\$ -</u> | <u>\$ 9,412,725</u> |

The Conference maintains accounts with several stock brokerage firms of which 76.3 percent is held by one broker and 17.7 percent by PUC. The accounts contain cash and securities. Balances held by brokers are insured up to \$500,000 (with a limit of \$100,000 for cash) by the Securities Investor Protection Corporation.

4. Fair Value Measurements

The Conference reports its fair value measures using a three-level hierarchy that prioritizes the inputs used to measure fair value. This hierarchy, established by accounting principles generally accepted in the United States of America, requires that entities maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

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Notes to Consolidated Financial Statements

4. Fair Value Measurements (Continued)

The three levels of inputs used to measure fair value are as follows:

- Level 1 Quoted prices for identical assets or liabilities in active markets to which the Conference has access at the measurement date.
- Level 2 Inputs other than quoted prices included in level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include the following:
- Quoted prices for similar assets or liabilities in active markets;
 - Quoted prices for identical or similar assets in markets that are not active;
 - Observable inputs other than quoted prices for the asset or liability (for example, interest rates and yield curves); and
 - Inputs derived principally from, or corroborated by, observable market data by correlation or by other means.
- Level 3 Unobservable inputs for the asset or liability. Unobservable inputs should be used to measure the fair value to the extent that observable inputs are not available.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2010:

United States government securities: Valued at the closing price reported in the active market on which the individual securities are traded.

Mutual funds: Valued at the net asset value (NAV) of shares held by the Conference at year-end.

Corporate bonds: Valued at the closing price reported on the active market on which the bonds are traded.

Equities: Valued at the closing price reported in the active market on which the individual equities are traded.

Fixed income and international equities mutual funds: Valued at the NAV of shares held by the Conference at year-end.

Pacific Union Income Fund: Valued at the NAV of underlying shares held by a banking institution at year-end.

Interest rate swap: Valued at observable interest rates.

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Notes to Consolidated Financial Statements

4. Fair Value Measurements (Continued)

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Conference 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.

When available, the Conference measures fair value using level 1 inputs because they generally provide the most reliable evidence of fair value. However, level 1 inputs are not available for many of the assets and liabilities that the Conference is required to measure at fair value (for example, in-kind contributions).

The primary uses of fair value measures in the Conference's consolidated financial statements are the following:

- Initial measurement of noncash gifts, including gifts of investment assets and real property,
- Recurring measurement of short-term investments as disclosed in Note 3, and
- Recurring measurement of derivative instruments as disclosed in Note 13.

5. Accounts Receivable

Accounts receivable are recorded at their net realizable value. At December 31, accounts receivable consisted of the following:

| | 2010 | 2009 |
|--------------------------------------|--------------|--------------|
| Congregation tithes and offerings | \$ 8,063,251 | \$ 7,368,176 |
| Congregations other reimbursements | 1,749,792 | 1,308,559 |
| Schools | 1,080,996 | 1,297,065 |
| Rental properties | 128,168 | 123,556 |
| Student accounts | 97,818 | 92,009 |
| Other | 136,844 | 341,825 |
| | 11,256,869 | 10,531,190 |
| Less allowance for doubtful accounts | (320,357) | (313,389) |
| | \$10,936,512 | \$10,217,801 |

At December 31, accounts receivable are presented in the consolidated statements of financial position as follows:

| | 2010 | 2009 |
|--|--------------|--------------|
| Accounts receivable, net current portion | \$10,147,441 | \$ 9,794,574 |
| Accounts receivable, noncurrent portion | 789,071 | 423,227 |
| | \$10,936,512 | \$10,217,801 |

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Notes to Consolidated Financial Statements

6. Advances to Churches

The Conference advanced funds to related parties, which are noninterest bearing and recorded at their net realizable value. At December 31, advances to churches consisted of the following:

| | <u>2010</u> | <u>2009</u> |
|-------------------------------|-------------------|-------------------|
| Rubidoux Spanish Church | \$ 115,977 | \$ 115,977 |
| Yucaipa Valley Spanish Church | 391,383 | 391,383 |
| Campus Hill Church | <u>187,500</u> | <u>220,000</u> |
| | 694,860 | 727,360 |
| Less current portion | <u>(145,977)</u> | <u>(145,977)</u> |
| | <u>\$ 548,883</u> | <u>\$ 581,383</u> |

7. Notes Receivable

The Conference finances activities on behalf of its affiliated organizations. Notes receivable are recorded at their net realizable value, and earned interest is recorded at rates from 3.5 percent to 10.0 percent for the years ended December 31, 2010 and 2009. At December 31, notes receivable consisted of:

| | <u>2010</u> | <u>2009</u> |
|--|---------------------|---------------------|
| Affiliate promissory notes with offsetting lines of credit (See Note 13) | \$ 2,724,397 | \$ 1,827,600 |
| Affiliate promissory notes with offsetting notes payable (See Note 14) | 28,823,844 | 27,630,533 |
| Affiliate promissory notes related to bonds payable (See Note 14) | 44,122,428 | 36,899,352 |
| Other affiliated promissory notes | 348,877 | 348,877 |
| Third party promissory note | <u>619,743</u> | <u>619,743</u> |
| | 76,639,289 | 67,326,105 |
| Less allowance for doubtful accounts | <u>(1,072,491)</u> | <u>(623,113)</u> |
| | 75,566,798 | 66,702,992 |
| Less current portion | <u>(6,531,665)</u> | <u>(5,572,387)</u> |
| | <u>\$69,035,133</u> | <u>\$61,130,605</u> |

Amounts are receivable from the following:

| | <u>2010</u> | <u>2009</u> |
|---------------|---------------------|---------------------|
| Congregations | \$48,110,569 | \$43,461,897 |
| Schools | 27,908,977 | 23,244,465 |
| Third party | <u>619,743</u> | <u>619,743</u> |
| | <u>\$76,639,289</u> | <u>\$67,326,105</u> |

**SOUTHEASTERN CALIFORNIA CONFERENCE
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Notes to Consolidated Financial Statements

8. Plant Assets

Plant assets at December 31, 2010 and 2009 include property, plant, and equipment held and used by the Conference. The Conference also holds title to real estate for the use of certain affiliated organizations, including congregations, schools, and academies. All property donated, including construction in progress, by affiliated organizations is recorded at fair value on the date of donation. Revenue recorded for donated plant assets from affiliated organizations for the years ended December 31, 2010 and 2009 was \$18,106,407 and \$22,936,098, respectively, which included \$209,611 and \$4,770 in donated services and \$523,027 and \$200,968, respectively, in capitalized interest.

The following are the plant assets for the year ended December 31, 2010:

| | Conference and Subsidiaries | Congregations | Elementary Schools | Academies | Total |
|-------------------------------|-----------------------------------|-----------------------|-----------------------|----------------------|-----------------------|
| Construction in progress | | \$ 25,269,577 | \$ 2,101,338 | \$ 5,641,696 | \$ 33,012,611 |
| Land | \$ 656,641 | 24,052,130 | 1,464,822 | 5,731,231 | 31,904,824 |
| Land improvements | 3,928,746 | 8,069,697 | 1,007,410 | 6,029,881 | 19,035,734 |
| Buildings and improvements | 13,653,172 | 127,671,809 | 6,702,302 | 50,539,804 | 198,567,087 |
| Equipment | 3,607,919 | | | | 3,607,919 |
| Subtotal | 21,846,478 | 185,063,213 | 11,275,872 | 67,942,612 | 286,128,175 |
| Less accumulated depreciation | (10,522,433) | (47,682,063) | (2,545,802) | (15,320,517) | (76,070,815) |
| Plant assets, net | <u>\$ 11,324,045</u> | <u>\$ 137,381,150</u> | <u>\$ 8,730,070</u> | <u>\$ 52,622,095</u> | <u>\$ 210,057,360</u> |

The following are the plant assets for the year ended December 31, 2009, as restated:

| | Conference and Subsidiaries | Congregations | Elementary Schools | Academies | Total |
|-------------------------------|-----------------------------------|-----------------------|-----------------------|----------------------|-----------------------|
| Construction in progress | | \$ 32,839,117 | \$ 2,306,561 | \$ 6,044,921 | \$ 41,190,599 |
| Land | \$ 656,641 | 23,635,823 | 1,464,822 | 5,729,792 | 31,487,078 |
| Land improvements | 4,020,466 | 7,578,475 | 991,903 | 5,941,485 | 18,532,329 |
| Buildings and improvements | 13,571,649 | 109,515,872 | 6,366,595 | 43,795,846 | 173,249,962 |
| Equipment | 3,909,300 | | | | 3,909,300 |
| Subtotal | 22,158,056 | 173,569,287 | 11,129,881 | 61,512,044 | 268,369,268 |
| Less accumulated depreciation | (10,712,210) | (44,043,101) | (2,293,147) | (13,828,197) | (70,876,655) |
| Plant assets, net | <u>\$ 11,445,846</u> | <u>\$ 129,526,186</u> | <u>\$ 8,836,734</u> | <u>\$ 47,683,847</u> | <u>\$ 197,492,613</u> |

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Notes to Consolidated Financial Statements

8. Plant Assets (Continued)

Depreciation expense for the years ended December 31, 2010 and 2009 was \$6,113,428 and \$5,246,717, respectively, which is included in the consolidated statements of activities and changes in net assets as follows:

| | <u>2010</u> | <u>2009</u> |
|----------------------------|--------------------|--------------------|
| Church ministries | \$3,638,962 | \$3,319,389 |
| Education | 1,895,637 | 1,354,284 |
| Auxiliary services | 126,336 | 130,971 |
| General and administrative | <u>452,493</u> | <u>442,073</u> |
| | <u>\$6,113,428</u> | <u>\$5,246,717</u> |

The use of property, plant, and equipment constructed by academies that were financed with the proceeds of Colorado Education and Cultural Facilities Authority-Series 2008 tax-exempt bonds are legally restricted to prohibit the use of the property primarily for religious worship or sectarian instruction. At December 31, 2010 and 2009, the Conference was in compliance with the legal requirement.

At December 31, assets restricted for this purpose were included in the following balances:

| | <u>2010</u> | <u>2009</u> |
|----------------------------|---------------------|---------------------|
| Land | \$ 4,821,280 | \$ 4,821,280 |
| Land improvements | 2,343,367 | 2,343,367 |
| Buildings and improvements | 15,210,416 | 8,640,543 |
| Construction in progress | <u>5,641,696</u> | <u>6,044,921</u> |
| | <u>\$28,016,759</u> | <u>\$21,850,111</u> |

9. Investments in Real Estate

At December 31, investments in real estate were comprised of the following components:

| | <u>2010</u> | <u>2009</u> |
|--|---------------------|---------------------|
| Rental properties | | |
| Land | \$ 9,339,693 | \$ 8,737,929 |
| Land improvements | 421,880 | 380,477 |
| Buildings | 20,032,244 | 19,995,068 |
| Building improvements | 34,803 | 34,803 |
| Equipment | <u>146,009</u> | <u>146,009</u> |
| | 29,974,629 | 29,294,286 |
| Land held for sale | 100,000 | 100,000 |
| Buildings and improvements held for sale | 35,921 | |
| Vacant land | 805,165 | 795,493 |
| Cemetery plots | <u>990</u> | <u>247</u> |
| | 30,916,705 | 30,190,026 |
| Accumulated depreciation | <u>(8,016,421)</u> | <u>(7,396,150)</u> |
| | <u>\$22,900,284</u> | <u>\$22,793,876</u> |

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9. Investments in Real Estate (Continued)

Depreciation expense for investments in real estate for the years ended December 31, 2010 and 2009 was \$614,882 and \$437,380, respectively, and is included in rental properties expense. During 2009, the Conference received \$258,000 in donated property.

Periodically, the Conference assesses the recoverability of its long-lived assets. During 2009, the Conference recorded impairment losses of \$230,229, which is included in the consolidated statements of activities and changes in net assets as unrestricted loss on impairment of long-lived assets. The impairment losses represent the excess of the aggregate carrying amount of vacant land over the aggregate of their fair value which was determined on the basis of prices for similar assets. The impaired assets are part of investments in real estate - vacant land.

Assets held for sale at December 31, 2010 include congregation land, building, and improvements which were not occupied and are actively marketed. Expected disposal is uncertain due to economic factors within the real estate market.

10. Assets Held in Trust

At December 31, 2010, assets held in trust consisted of the following:

| | Revocable Trusts | Irrevocable Trusts | Total |
|---------------------------|---------------------|-----------------------|---------------------|
| Cash and cash equivalents | \$ 1,972,851 | \$1,423,051 | \$ 3,395,902 |
| Investments | 1,204,358 | 3,012,970 | 4,217,328 |
| Notes receivable | 148,560 | 361,903 | 510,463 |
| Real property | 8,445,537 | 311,857 | 8,757,394 |
| PUC trusts | | 122,104 | 122,104 |
| | <u>\$11,771,306</u> | <u>\$5,231,885</u> | <u>\$17,003,191</u> |

At December 31, 2009, assets held in trust consisted of the following:

| | Revocable Trusts | Irrevocable Trusts | Total |
|---------------------------|---------------------|-----------------------|---------------------|
| Cash and cash equivalents | \$2,172,303 | \$1,381,774 | \$ 3,554,077 |
| Investments | 1,118,095 | 2,649,352 | 3,767,447 |
| Notes receivable | 152,785 | 112,476 | 265,261 |
| Real property | 9,416,201 | 1,430,285 | 10,846,486 |
| PUC trusts | | 1,018,901 | 1,018,901 |
| | <u>\$12,859,384</u> | <u>\$6,592,788</u> | <u>\$19,452,172</u> |

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10. Assets Held in Trust (Continued)

The PUC trusts are administered by Western Adventist Foundation and are charitable remainder trusts.

| | <u>2010</u> | <u>2009</u> |
|--|-------------------|-------------------|
| FMV of irrevocable trusts donated | \$1,218,631 | \$ 531,423 |
| Less portion due to others | <u>(620,955)</u> | <u>(452,522)</u> |
| Revenue from irrevocable trusts donated | 597,676 | 78,901 |
| Change in present value | <u>186,686</u> | <u>231,802</u> |
| Net income related to irrevocable trusts | <u>\$ 784,362</u> | <u>\$ 310,703</u> |

This information is reflected in the consolidated financial statements in totals for matured trusts, wills and bequests, and investment income.

11. Accounts Payable

At December 31, accounts payable consisted of the following:

| | <u>2010</u> | <u>2009</u> |
|--------------------------|--------------------|--------------------|
| Pacific Union Conference | \$2,028,774 | \$2,052,516 |
| Affiliated congregations | 243,943 | 32,857 |
| Conference academies | 42,065 | 668,585 |
| Conference schools | 2,711 | 3,284 |
| Other | <u>629,425</u> | <u>544,866</u> |
| | <u>\$2,946,918</u> | <u>\$3,302,108</u> |

12. Lines of Credit

The Conference maintains a \$5,000,000 line of credit with Bank of America of which \$1,000,000 is available for working capital and \$4,000,000 is available for the acquisition or renovation of facilities. The line of credit is unsecured and has a renewal date of May 16, 2011. The Conference pays interest monthly at the BBA LIBOR Daily Floating Rate plus 1.25 percent which was 1.51 and 1.48 percent at December 31, 2010 and 2009, respectively.

On April 14, 2011, the Conference amended the agreement for the \$5,000,000 line of credit with Bank of America, extending the renewal date to April 15, 2012.

At December 31, 2010 and 2009, the outstanding balance was \$2,724,397 and \$1,827,600, respectively.

The line of credit with Bank of America contains covenants pertaining to total debt to net asset balance and liquidity. Specifically, the Conference is required to maintain a total debt to net asset balance not to exceed 0.50:1 and unrestricted liquid assets of at least \$5,000,000. The Conference is also required to submit audited financial statements within 270 days of the end of each year. At December 31, 2010, the Conference was in compliance with these covenants.

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13. Notes Payable and Bonds Payable

In addition to debt acquired for Conference operations, the Conference also obtains or guarantees debt on behalf of affiliated congregations, schools, and academies.

At December 31, notes payable consisted of the following:

| | 2010 | 2009 |
|---|--------------|--------------|
| <u>Notes payable in the name of the Conference</u> | | |
| Bank of America - High Desert Bilingual SDA Church; due October 31, 2015; payable in monthly installments of \$11,514 including interest at 7.35%; balloon payment of \$984,603 as of December 31, 2010 and 2009; secured by property with net book value on December 31, 2010 and 2009 of \$1,787,160 and \$1,864,635, respectively. ⁽¹⁾⁽³⁾ | \$ 1,250,831 | \$ 1,294,424 |
| Farmers & Merchants Bank - Waterman Visayan Filipino SDA Church; due December 8, 2013; payable in monthly installments of \$418 including interest at 5%; secured by property with net book value on December 31, 2009 of \$643,533. ⁽¹⁾ | | 18,493 |
| La Loma Federal Credit Union - Yucaipa Samoan SDA Church; due February 1, 2035; payable in monthly installments of \$2,369 including interest at 5.375%; secured by property with net book value on December 31, 2010 and 2009 of \$881,157 and \$918,088, respectively. ⁽¹⁾⁽³⁾ | 384,725 | 391,638 |
| Paradise Valley Federal Credit Union - Blythe Spanish/English SDA Church; due December 1, 2021; payable in monthly installments of \$5,200 including interest at 6.50%; balloon payment of \$327,891 as of December 31, 2010 and 2009; secured by property with net book value on December 31, 2010 and 2009 of \$1,226,458 and \$1,262,995, respectively. ⁽¹⁾⁽³⁾ | 614,606 | 645,939 |
| Paradise Valley Federal Credit Union - Paradise Valley Spanish SDA Church; due December 1, 2020; payable in monthly installments of \$9,000 including variable interest initially at 6.50% balloon payment of \$796,653 as of December 31, 2010 and 2009; secured by property with net book value on December 31, 2010 and 2009 of \$1,860,348 and 1,897,075, respectively. ⁽¹⁾⁽³⁾ | 1,204,529 | 1,233,215 |

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13. Notes Payable and Bonds Payable (Continued)

| | 2010 | 2009 |
|---|------------|------------|
| Paradise Valley Federal Credit Union - San Diego Academy; due July 1, 2015; payable in monthly installments of \$8,600 including interest at 6.25%; secured by property with net book value on December 31, 2010 and 2009 of \$8,382,892 and \$8,524,931, respectively. ⁽¹⁾⁽³⁾ | \$ 246,490 | \$ 331,383 |
| Paradise Valley Federal Credit Union - San Diego Tierrasanta SDA Church; due March 1, 2020; payable in monthly installments of \$15,008 including interest at 6.25%; secured by property with net book value on December 31, 2010 and 2009 of \$6,662,413 and \$6,811,354, respectively. ⁽¹⁾⁽³⁾ | 504,552 | 1,032,743 |
| Commonwealth Business Bank – Orange Central Korean SDA Church; due May 27, 2012; payable in monthly installments of \$14,126 including variable interest at 5.75% at December 31, 2009; balloon payment of \$2,098,913 as of December 31, 2010 and 2009; secured by property with net book value on December 31, 2010 and 2009 of \$4,377,423 and \$4,489,614, respectively. ⁽¹⁾ | 2,161,429 | 2,200,004 |
| Centro Cristiano de Fe Church; due June 12, 2010; includes interest only monthly installments at 6%; secured by property with net book value of \$725,000 on December 31, 2009; includes one assignment of rents on December 31, 2009 as additional security. ⁽¹⁾ | | 38,000 |
| Paradise Valley Federal Credit Union – Murrieta Springs SDA Church; due March 1, 2019; payable in monthly installments of \$6,375 including interest at 8%; balloon payment of \$505,518 as of December 31, 2009; secured by property with net book value on December 31, 2009 of \$741,808. This note was consolidated with the note below in 2010. The due date was extended as listed below. ⁽¹⁾⁽³⁾⁽⁴⁾ | | 740,598 |
| Paradise Valley Federal Credit Union – Murrieta Springs SDA Church; due April 10, 2020; payable in monthly installments of \$8,000 through June 1, 2020 including interest of 7.5%; and a balloon payment of \$674,399 as of December 31, 2010, secured by property with a net book value of \$4,879,602 on December 31, 2010; includes one assignment of rents effective March 9, 2010 as additional security. This note was consolidated with the preceding note in 2010. ⁽¹⁾⁽³⁾ | 978,412 | |

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Notes to Consolidated Financial Statements

13. Notes Payable and Bonds Payable (Continued)

| | 2010 | 2009 |
|---|------------|------------|
| Paradise Valley Federal Credit Union – New Hope SDA Church; due May 1, 2035; payable in monthly installments from June 1, 2005 through May 31, 2010 of \$1,775 including interest at 6%, from June 1, 2010 through May 31, 2015 of \$1,872 including interest at 6.5%, from June 1, 2015 through May 1, 2035 of \$1,961 including interest at 7%; secured by property with a net book value of \$463,043 and \$468,793 on December 31, 2010 and 2009, respectively; includes one assignment of rents on December 31, 2010 and 2009 as additional security. ^{(1) (3)} | \$ 272,057 | \$ 277,378 |
| Paradise Valley Federal Credit Union – New Hope SDA Church; due May 1, 2020; payable in monthly installments of \$488 including interest at 8%; secured by property with a net book value of \$463,043 and \$468,793 on December 31, 2010 and 2009, respectively; includes one assignment of rents on December 31, 2010 and 2009 as additional security. ^{(1) (3)} | 34,034 | 37,284 |
| Paradise Valley Federal Credit Union – Vista Spanish SDA Church; due April 10, 2020; payable in monthly installments of \$1,430 through March 10, 2020 and a final installment of \$1,294, including interest of 6%; secured by property with a net book value of \$227,276 and \$243,244 on December 31, 2010 and 2009, respectively; includes one assignment of rents effective March 9, 2010 as additional security. ^{(1) (3)} | 121,510 | 130,334 |
| Pacific Union Conference Church and School Loan Fund – Calexico Mission School; due October 22, 2014; payable in monthly installments of \$7,495 including interest at 6% at December 31, 2010 and 2009; balloon payment of \$12,538 and \$16,594 as of December 31, 2010 and 2009, respectively; secured by property with net book value including building on December 31, 2010 and 2009 of \$1,201,494 and \$1,236,320, respectively. ⁽²⁾ | 311,370 | 380,507 |
| SDA Layman’s - Yucaipa Samoan SDA Church; due June 1, 2010; payable in monthly installments of \$1,582 including interest at 5%; balloon payment of \$149,513; unsecured. ^{(1) (2) (3)} | 154,246 | 154,246 |

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Notes to Consolidated Financial Statements

13. Notes Payable and Bonds Payable (Continued)

| | 2010 | 2009 |
|--|------------|--------------|
| Pacific Union Conference Revolving Fund; due October 7, 2023; payable in monthly installments of \$9,315 including interest at 6.25% at December 31, 2010 and 2009; secured by property with net book value of \$2,850,000 and \$2,887,500 on December 31, 2010 and 2009, respectively. ⁽²⁾ | \$ 983,311 | \$ 1,034,767 |
| | 9,222,102 | 9,940,953 |

Notes payable guaranteed by the Conference

| | | |
|--|-----------|-----------|
| Pacific Union Conference Church and School Fund Loans guaranteed by Conference; maturity dates vary; variable interest rate at 6% at December 31, 2010 and 2009; secured by property with net book value on December 31, 2010 and 2009 of \$26,852,511 and \$24,112,524, respectively; includes eight assignment of rents on December 31, 2009 and nine assignment of rents on December 31, 2010 as additional security. ⁽¹⁾⁽²⁾ | 5,935,772 | 5,692,694 |
|--|-----------|-----------|

| | | |
|--|------------|------------|
| Pacific Union Conference Income Fund Loans; maturity dates vary; variable interest rate at 6.75% at December 31, 2010 and 2009; secured by property with net book value on December 31, 2010 and 2009 of \$46,350,473 and \$24,377,580, respectively; includes 13 assignment of rents on December 31, 2010 and 2009 for additional security. ⁽¹⁾⁽²⁾ | 14,960,652 | 13,412,160 |
|--|------------|------------|

| | | |
|----------------------|--------------|--------------|
| | 20,896,424 | 19,104,854 |
| | 30,118,526 | 29,045,807 |
| Less current portion | (2,839,161) | (2,381,483) |
| | \$27,279,365 | \$26,664,324 |

At December 31, bonds payable consisted of the following:

| | | |
|---|--------------|--------------|
| Colorado Educational and Cultural Facilities Authority – adjustable rate demand tax exempt revenue bonds Series 2008; variable weekly interest rate; monthly interest-only payments; annual principal payments beginning June 1, 2025 and maturing June 1, 2038; secured by irrevocable letter of credit issued by Bank of America and property with a net book value of \$47,138,339 and \$44,291,256 on December 31, 2010 and 2009, respectively. | \$32,330,000 | \$32,330,000 |
|---|--------------|--------------|

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Notes to Consolidated Financial Statements

13. Notes Payable and Bonds Payable (Continued)

| | 2010 | 2009 |
|---|--------------|--------------|
| Southeastern California Conference of Seventh-day Adventists – adjustable rate demand taxable revenue bonds, Series 2008; variable weekly interest rate; monthly interest-only payments; annual principal payments beginning June 1, 2009 and maturing June 1, 2025; secured by irrevocable letter of credit issued by Bank of America property with a net book value of \$47,138,339 and \$44,291,256 on December 31, 2010 and 2009, respectively. | \$18,325,000 | \$19,175,000 |
| | 50,655,000 | 51,505,000 |
| Less current portion | (855,000) | (850,000) |
| | \$49,800,000 | \$50,655,000 |

Future maturities of long-term debt and related party obligations at December 31, 2010 were as follows:

| Year Ending December 31, | With Related Note Receivable | Other Notes Payable | Bond Issue | Total |
|--------------------------|------------------------------------|------------------------|---------------|--------------|
| 2011 | \$ 2,711,653 | \$ 127,508 | \$ 855,000 | \$ 3,694,161 |
| 2012 | 3,939,685 | 135,372 | 900,000 | 4,975,057 |
| 2013 | 5,946,150 | 143,722 | 955,000 | 7,044,872 |
| 2014 | 4,852,561 | 142,715 | 1,005,000 | 6,000,276 |
| 2015 | 4,328,025 | 68,933 | 1,060,000 | 5,456,958 |
| Thereafter | 7,045,771 | 676,431 | 45,880,000 | 53,602,202 |
| | \$28,823,845 | \$1,294,681 | \$50,655,000 | \$80,773,526 |

Interest Rate Swaps

As a means to achieve a greater level of interest rate stability in connection with the Series 2008 taxable and tax-exempt revenue bonds, the Conference entered into two interest rate swaps in February 2009 (2009-1 Swap and 2009-2 Swap), a third in March 2009 (2009-3 Swap), and a fourth in July 2010 (2010-1), all of which effectively change the interest rate on the bonds to synthetic fixed rates.

The interest rate swaps are, among other things, subject to credit, basis, and termination risk. The credit and termination risks have been mitigated with collateral posting requirements by the counterparty in the event of a ratings downgrade below a specified threshold. The swaps are subject to basis risk should the relationship between the variable rates applicable to the swaps converge with that of the bonds which would change the synthetic interest rate on the bonds.

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13. Notes Payable and Bonds Payable (Continued)

The swap policy adopted by the Conference requires determination of the fair termination values of its swaps at least annually. The calculation of the fair termination value takes into consideration the prevailing interest rate environment, the specific terms and conditions of a given transaction, and any upfront payments that were received, if any. Fair valuations of termination values are realized only if the swaps were to be terminated at the valuation date, and only the Conference retains the right to optionally terminate the transactions.

As of December 31, 2010 and 2009, the net negative fair values for the swaps were estimated to be \$1,865,085 and \$321,120, respectively, which would approximate the amount the Conference would have paid to Bank of America as a termination payment if the swaps had been terminated at December 31, 2010 and 2009, respectively, and are a result of the change in interest rate levels and certain interest rate relationships. The net fair values of the swaps are recorded as a part of other noncurrent liabilities in the consolidated statements of financial position at December 31, 2010 and 2009. The change in fair values from inception of the swaps through December 31, 2010 and 2009 was \$1,543,965 and \$321,120, respectively, and is recorded as part of other expense in the consolidated statements of activities and changes in net assets as of December 31, 2010 and 2009.

The terms, fair values, and credit ratings of the outstanding swaps as of December 31, 2010 are as follows:

| Associated Debt Issue | Counter-party | Notional Amount | Effective Date | Fixed Rate to be Paid | Variable Rate to be Received | Fair Value | Swap Termination Date | Counterparty Credit Rating |
|--------------------------------|-----------------|---------------------|----------------|-----------------------|------------------------------|----------------------|-----------------------|----------------------------|
| 2008 Taxable Revenue Bonds | Bank of America | \$18,325,000 | 02/10/2009 | 3.249 % | One-Month LIBOR | \$ (627,965) | 02/01/2019 | Aa3/A+/A+ |
| 2008 Non-Taxable Revenue Bonds | Bank of America | 16,525,000 | 02/10/2009 | 2.56% | SIFMA | (767,182) | 02/03/2014 | Aa3/A+/A+ |
| 2008 Non-Taxable Revenue Bonds | Bank of America | 9,000,000 | 03/23/2009 | 2.71% | SIFMA | (400,064) | 04/01/2016 | Aa3/A+/A+ |
| 2008 Non-Taxable Revenue Bonds | Bank of America | <u>6,800,000</u> | 07/16/2010 | 2.82% | SIFMA | <u>(69,874)</u> | 07/01/2020 | Aa3/A+/A+ |
| | | <u>\$50,650,000</u> | | | | <u>\$(1,865,085)</u> | | |

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13. Notes Payable and Bonds Payable (Continued)

The terms, fair values, and credit ratings of the outstanding swaps as of December 31, 2009 are as follows:

| Associated Debt Issue | Counter-party | Notional Amount | Effective Date | Fixed Rate to be Paid | Variable Rate to be Received | Fair Value | Swap Termination Date | Counterparty Credit Rating |
|--------------------------------|-----------------|---------------------|----------------|-----------------------|------------------------------|--------------------|-----------------------|----------------------------|
| 2008 Taxable Revenue Bonds | Bank of America | \$19,175,000 | 02/10/2009 | 3.249% | One-Month LIBOR | \$ 247,064 | 02/01/2019 | Aa3/A+/A+ |
| 2008 Non-Taxable Revenue Bonds | Bank of America | 16,525,000 | 02/10/2009 | 2.56% | SIFMA | (436,292) | 02/03/2014 | Aa3/A+/A+ |
| 2008 Non-Taxable Revenue Bonds | Bank of America | <u>9,000,000</u> | 03/23/2009 | 2.71% | SIFMA | <u>(131,892)</u> | 04/01/2016 | Aa3/A+/A+ |
| | | <u>\$44,700,000</u> | | | | <u>\$(321,120)</u> | | |

Interest charged to expense during the years ended December 31, 2010 and 2009 was \$1,468,231 and \$1,392,384, respectively, with \$31,359 and \$5,460 included in general and administrative expense, \$60,324 and \$69,067 in rental properties expense, and \$1,376,548 and \$1,317,857 in interest expense, respectively.

Loan agreements with Bank of America contain covenants pertaining to debt to net asset balance and liquidity. Specifically, the Conference is required to maintain a total debt to net assets balance of no more than 0.5:1, and unrestricted liquid assets of at least \$5,000,000. The Conference is also required to submit audited financial statements within 270 days of the end of each year. At December 31, 2010 and 2009, the Conference was in compliance with these covenants.

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13. Notes Payable and Bonds Payable (Continued)

On June 26, 2008 the Conference issued \$52,580,000 in adjustable rate demand revenue bonds through its limited liability company, SECC-ECF, LLC. The bonds were issued in two series: taxable and tax-exempt. The taxable bond issue totaled \$20,250,000 and will mature June 1, 2025; proceeds are in the process of being used to finance and refinance the costs of the acquisition, construction, renovation, installation, and equipping of certain church and/or educational facilities and to pay costs incurred in connection with the issuance of bonds. The tax-exempt bond issue totaled \$32,330,000 and will mature June 1, 2038, and proceeds are in the process of being used to finance and refinance the costs of certain cultural facilities and K-12 educational facilities and to pay costs incurred in connection with the issuance of bonds. The bonds are subject to conversion to a term interest rate. The repayments of interest and principal initially will be supported by irrevocable direct draw letters of credit which will automatically terminate September 26, 2011 unless renewed or terminated sooner.

The letters of credit contain covenants regarding audited financial statements, debt service ratio, and liquidity. Specifically, the Conference is required to submit audited financial statements within 180 days of the end of each year and quarterly financial statements within 45 days of the end of each quarter, maintain a debt service ratio of not less than 1.25:1.00 at June 30 and December 31, and maintain an unrestricted liquid assets to total debt percentage of at least 80 percent measured each June 30 and December 31. The Conference complied with these covenants as of December 31, 2010 with the exception of the timely submission of audited financial statements within 180 days of year-end. The bond purchase agreement also requires the Conference to provide audited comparative financial statements to the bond underwriter within 270 days of the end of each year. Bank of America waived the covenant regarding receipt of audited financial statements within 180 days of year-end for the year ended December 31, 2010.

⁽¹⁾The note was incurred on behalf of and is offset by a note receivable from congregation, school or academy within the Conference.

⁽²⁾Related party. See Note 21.

⁽³⁾The note reflects the Conference and the congregation, school, or academy as parties to the note.

⁽⁴⁾Amount refinanced during the year ended December 31, 2010.

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14. Capital Leases

Minimum future lease payments under capital leases as of December 31, 2010 for each of the next five years and aggregate are:

| | <u>2010</u> |
|---|-------------------|
| Year ending December 31, | |
| 2011 | \$ 131,353 |
| 2012 | 131,850 |
| 2013 | 131,850 |
| 2014 | 131,850 |
| 2015 | 108,698 |
| Thereafter | <u>10,134</u> |
| Total minimum lease payments | 645,735 |
| Less amount representing interest | <u>(183,175)</u> |
| Present value of net minimum lease payments | <u>\$ 462,560</u> |

The interest rate on capital leases is 6.23 percent. Lease agreements contain purchase options which are either at fixed prices or at prices representing the expected fair value of the property at the expiration of the lease term.

The cost and accumulated depreciation of the equipment under capitalized leases included on the consolidated statements of financial position for 2010 are \$517,807 and \$48,264, respectively.

15. Liabilities to Depositors

At December 31, 2010 and 2009, liabilities to depositors consisted of \$915,160 and \$864,783, respectively, in investments held on behalf of affiliated congregations.

16. Liabilities Held in Trust

At December 31, liabilities held in trust consisted of the following:

| | <u>2010</u> | <u>2009</u> |
|---|---------------------|---------------------|
| Liabilities to remainder beneficiaries | \$ 1,872,233 | \$ 1,928,036 |
| Present value of payments to income beneficiaries | <u>1,662,387</u> | <u>1,641,857</u> |
| Liabilities under irrevocable trusts | 3,534,620 | 3,569,893 |
| Liabilities under revocable trusts | <u>11,771,306</u> | <u>12,859,384</u> |
| | <u>\$15,305,926</u> | <u>\$16,429,277</u> |

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17 Net Assets

At December 31, unrestricted net assets designated by the board of directors included the following:

| | <u>2010</u> | <u>2009</u> |
|-----------------------------|---------------------|---------------------|
| Quasi endowments | \$53,143,767 | \$49,189,287 |
| Property insurance reserves | <u>2,182,229</u> | <u>1,323,502</u> |
| | <u>\$55,325,996</u> | <u>\$50,512,789</u> |

At December 31, temporarily restricted net assets were available for the following purposes:

| | <u>2010</u> | <u>2009</u> |
|---------------------|--------------------|--------------------|
| Church ministries | \$2,334,582 | \$2,418,005 |
| Education | 949,975 | 802,983 |
| Auxiliary services | 29,012 | 70,728 |
| Outreach ministries | 70,624 | 240,651 |
| Other | <u>663,384</u> | <u>662,732</u> |
| | <u>\$4,047,577</u> | <u>\$4,195,099</u> |

At December 31, permanently restricted net assets consisted of the following:

| | <u>2010</u> | <u>2009</u> |
|---|-----------------|-----------------|
| Junior Camp | \$10,000 | \$10,000 |
| San Marcos Seventh-day Adventist Church | <u>52,332</u> | <u>52,332</u> |
| | <u>\$62,332</u> | <u>\$62,332</u> |

18. Employee Benefit Plans

Defined Benefit Plan

The Conference participates in a noncontributory, defined benefit retirement plan known as the Seventh-day Adventist Retirement Plan for North America (the "Defined Benefit Plan"). The Defined Benefit Plan is administered by the General Conference of Seventh-day Adventists in Silver Spring, Maryland and is exempt from the Employee Retirement Income Security Act of 1974 as a plan of a church-related agency. The Conference contributed \$3,422,712 and \$3,572,234 to the Defined Benefit Plan for the years ended December 31, 2010 and 2009, respectively, for general retirement benefits.

The Defined Benefit Plan is defined by the Financial Accounting Standards Board as a multi-employer plan. As such, it is not required, nor is it possible, to determine the actuarial present value of accumulated benefits or plan net assets for employees of the Conference apart from other plan participants. However, based on the latest actuarial evaluation of the Defined Benefit Plan, as of December 31, 2009, the actuarially computed value of accumulated plan benefits exceeded the estimated market value of plan assets.

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18. Employee Benefit Plans

The Conference contributed \$1,246,800 and \$1,230,506 for the years ended December 31, 2010 and 2009 to the Health Care Assistance Plan for Participants in the Seventh-day Adventist Retirement Plan of the North American Division (the "Healthcare Plan") on behalf of retired employees participating in the Defined Benefit Plan. Additional information regarding the Healthcare Plan is outlined in Note 19 to the consolidated financial statements.

In January 2000, the Defined Benefit Plan was left as an option for those close to retirement who wanted to remain on this plan. At this time, a new 403(b) plan was put in place for all new employees and nonvested employees.

Defined Contribution Plan

Effective January 1, 2000, the Conference participates in a defined contribution retirement plan known as "The Adventist Retirement Plan" (the "Defined Contribution Plan"). The Defined Contribution Plan, which covers substantially all employees of the Conference, is administered by the General Conference of Seventh-day Adventists in Silver Spring, Maryland and is exempt from the Employee Retirement Income Security Act of 1974 as a plan of a church-related agency. Employer contributions are made directly to the employee's retirement account managed by Variable Annuity Life Insurance Conference (VALIC). In addition to this benefit, employees are also able to contribute to their account maximum amounts allowed by current tax laws and the Conference will match according to maximum amounts approved on the Adventist retirement policy and tax laws. This new plan is intended to replace the older one incrementally and is available to all North American Division employees participating in the Defined Benefit Plan. The Conference contributed \$1,896,216 and \$1,961,754 under the basic requirements and \$655,972 and \$552,935 as employer matching to the Defined Contribution Plan for the years ended December 31, 2010 and 2009, respectively.

19. Self-Insurance

The Conference is self-insured for dental, vision, chiropractic, and wellness programs. The Conference expended \$1,057,121 and \$970,069 during the years ended December 31, 2010 and 2009.

The Conference participates in a Worker's Compensation Self-Insurance Pool (the "Plan") that is coordinated by the PUC. PUC is considered to be a "fully participating member" of the Plan and is not required to arrange for a security deposit or surety bond. The Plan calculates an annual assessment which is billed to each organization for their prorated portion of the assessment. The amount of the annual contributions to the Plan, including contributions for affiliated organizations, are calculated based on prior year's claims, and totaled \$747,875 and \$759,425 for the years ended December 31, 2010 and 2009, respectively.

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Notes to Consolidated Financial Statements

20. Operating Leases

The Conference bought out its noncancelable leases for several copiers in 2010 which were replaced with capital leases in Note 14. Total expense for operating leases was approximately \$84,036 for the year ended December 31, 2009.

The Conference is the lessor under operating leases which allow limited use of real property and expire in various years through 2014. Property held for lease is described in Note 9.

Minimum future rentals to be received on noncancelable leases as of December 31, 2010 for each of the next five years and in the aggregate are as follows:

| | |
|-------------------------|--------------------|
| Year ended December 31, | |
| 2011 | \$ 647,574 |
| 2012 | 588,986 |
| 2013 | 377,953 |
| 2014 | 257,384 |
| 2015 | <u>119,158</u> |
| | <u>\$1,991,055</u> |

As noted in Note 21, the Conference appropriates the associated revenues to the affiliate church or school which shares in the use of the property.

21. Related Party Transactions

As described in Note 1, the Conference is associated with various Seventh-day Adventist organizations. At December 31, 2010 and 2009, and the years then ended, the Conference had the following transactions with related parties. The following represents assets and liabilities held with related parties at December 31:

| | 2010 | | | |
|--|---------------------|--------------------------|-----------------------|---------------------|
| | Congregations | Schools and Academies | PUC | Total |
| Accounts receivable (Note 5) | \$ 9,813,043 | \$ 1,080,995 | | \$10,894,038 |
| Investments (Note 3) | | | \$ 9,190,688 | 9,190,688 |
| Interest receivable | 84,150 | 80,166 | | 164,316 |
| Advances to churches (Note 6) | 694,860 | | | 694,860 |
| Receivable for guarantees of equipment leases | 313,175 | 101,980 | | 415,155 |
| Notes receivable (Note 7) | 48,110,569 | 27,908,977 | | 76,019,546 |
| Accounts payable (Note 11) | (243,943) | (44,776) | (2,028,774) | (2,317,493) |
| Guarantees of equipment leases | (313,175) | (101,980) | | (415,155) |
| Notes payable (Note 13)* | (154,247) | | (22,191,104) | (22,345,351) |
| Accrued wages and benefits (retirement) | | | (718,115) | (718,115) |
| | <u>\$58,304,432</u> | <u>\$29,025,362</u> | <u>\$(15,747,305)</u> | <u>\$71,582,489</u> |

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21. Related Party Transactions (Continued)

| | 2009 | | | Total |
|--|---------------------|--------------------------|-----------------------|---------------------|
| | Congregations | Schools and Academies | PUC | |
| Accounts receivable (Note 5) | \$ 8,676,735 | \$ 1,297,065 | | \$ 9,973,800 |
| Investments (Note 3) | | | \$ 9,027,719 | 9,027,719 |
| Interest receivable | 560,331 | 48,725 | | 609,056 |
| Advances to churches (Note 6) | 727,360 | | | 727,360 |
| Notes receivable (Note 7) | 43,461,897 | 23,244,465 | | 66,706,362 |
| Accounts payable (Note 11) | (32,857) | (671,869) | (2,052,516) | (2,757,242) |
| Notes payable (Note 13)* | | | (20,520,128) | (20,520,128) |
| Accrued wages and benefits (retirement) | | | (712,559) | (712,559) |
| | <u>\$53,393,466</u> | <u>\$23,918,386</u> | <u>\$(14,257,484)</u> | <u>\$63,054,368</u> |

*See detail of notes payable held by PUC on page 42.

Reflected in the consolidated statement of activities are the following related party revenues (expenses) for the years ended December 31:

| | 2010 | | | Total |
|---|-----------------------|--------------------------|-----------------------|-----------------------|
| | Congregations | Schools and Academies | PUC | |
| Tithe percentage passed on Subsidies | | | \$(11,875,477) | \$(11,875,477) |
| Payroll, benefits and other expense reimbursements | \$ 5,699,940 | \$ 21,629,458 | 3,902,682 | 27,329,398 |
| Donated plant assets | 11,493,926 | 6,612,481 | | 18,106,407 |
| Investment income | | | 489,858 | 489,858 |
| Interest income | 38,053 | | | 38,053 |
| Payroll and benefits | (16,207,632) | (19,428,448) | | (35,636,080) |
| Appropriations | (840,084) | (3,571,934) | (1,777,463) | (6,189,481) |
| Rental income appropriations | (2,556,003) | (89,456) | | (2,645,459) |
| Interest expense | | | (81,127) | (81,127) |
| | <u>\$ (2,371,800)</u> | <u>\$ 5,152,101</u> | <u>\$ (9,341,527)</u> | <u>\$ (6,561,226)</u> |

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21. Related Party Transactions (Continued)

| | 2009 | | | Total |
|--|-----------------------|--------------------------|-----------------------|-----------------------|
| | Congregations | Schools and Academies | PUC | |
| Tithe percentage passed on Subsidies | | | \$(12,023,952) | \$(12,023,952) |
| | | | 3,892,500 | 3,892,500 |
| Payroll, benefits and other expense reimbursements | \$ 5,595,075 | \$ 21,676,817 | | 27,271,892 |
| Donated plant assets | 15,324,193 | 7,097,852 | | 22,422,045 |
| Investment income | | | 329,256 | 329,256 |
| Interest income | 108,892 | | | 108,892 |
| Payroll and benefits | (17,043,981) | (19,973,564) | | (37,017,545) |
| Appropriations | (3,538,838) | (3,073,940) | (1,856,301) | (8,469,079) |
| Rental income appropriations | (2,631,521) | (89,454) | | (2,720,975) |
| Interest expense | | | (88,133) | (88,133) |
| | <u>\$ (2,186,180)</u> | <u>\$ 5,637,711</u> | <u>\$ (9,746,630)</u> | <u>\$ (6,295,099)</u> |

Within accounts receivable balance at December 31, 2010, there is one congregation that represents more than 10 percent of the total balance and that accounts for more than 10 percent of annual gross tithe revenue. Additionally, there are two academies which each represent more than 10 percent of the total note receivable balance at December 31, 2010.

Tithe percentages passed on represents the portion of tithe revenue received by the Conference which is allocable to affiliate organizations in accordance with policy. *Subsidies* represent amounts received in support of Conference operations or specific education or evangelism projects. *Payroll, benefits, and other expense reimbursements* represents those costs incurred by the Conference for which the affiliate congregation or schools is responsible for reimbursing the Conference. Under the guidelines of the Seventh-day Adventist denomination, churches and schools are not to own real property. As such, acquired or constructed plant assets by an affiliated church or school are donated to the local conference and are included in *donated plant assets*. In turn, the Conference allows the affiliated church or school to use the property at no cost. *Appropriations* represents amounts paid to affiliates for operations or other support; whereas, *rental income appropriations* represent the amount of rental income for use of Conference-owned property from which the Conference allows the affiliate to collect from third parties and retain. The Conference provides faculty and administration personnel for the schools, as well as ministerial and administrative staff for affiliate churches within its territories. Of the total payroll and related benefit expenses, the affiliate school or church may be responsible for a portion of the associated personnel costs. Reimbursements of personnel related costs are included in payroll, benefits, and other expense reimbursements.

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Notes to Consolidated Financial Statements

21. Related Party Transactions (Continued)

Notes payable held by the PUC are as follows:

| | 2010 | 2009 |
|---|--------------|--------------|
| PUC Church and School Loan Fund - Calexico Mission School | \$ 311,370 | \$ 380,507 |
| PUC Revolving Fund – Seacoast Property | 983,311 | 1,034,767 |
| | 1,294,681 | 1,415,274 |
| Loans received by affiliate schools and academies from Pacific Union Conference of Seventh-day Adventists, guaranteed with Conference fixed assets* | | |
| Church and School Fund loans | 5,935,772 | 5,692,694 |
| Income Fund loans | 14,960,651 | 13,412,160 |
| | 20,896,423 | 19,104,854 |
| Total | \$22,191,104 | \$20,520,128 |

*The Conference has guaranteed these notes until repaid by the schools and academies as detailed in Note 13. In the event the schools or academies default on repayment, the Conference would be required to repay the remaining debt balance. In the event the parties default on these loans, the Conference has no recourse; however, the Conference believes the loans will be fully repaid by the related parties.

On September 1, 1986, the Conference entered into an agreement with Loma Linda University, a Seventh-day Adventist University, for the Conference to lease land from Loma Linda University for a nominal amount, which is in turn sublet to the Loma Linda University Church, an affiliated congregation, for a nominal value, to be used by the congregation as a children’s center. The lease expires on August 31, 2085.

Besides the Calexico Mission School which has been consolidated by the Conference due to common control, the Conference is affiliated with 25 other schools and academies (“the institutions”) throughout Imperial, Orange, Riverside, San Bernardino, and San Diego counties. The institutions are supported and governed by the Seventh-day Adventist churches appointed by the Conference. However, the Conference provides all of the facilities, employs all the school administration and faculty, as well as, sets the curriculum for each institution. As a result, the Conference has control and financial interest in the institutions but has no ownership in the institutions and no majority voting rights over their governance. Under FASB ASC No. 951-810, the Conference has the option but not the requirement to consolidate the institutions but has elected not to consolidate the institutions as of December 31, 2010 or 2009. The schools have a June 30 fiscal year-end; as such, there are timing differences between the school financial data provided below and the Conference’s consolidated financial statements.

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Notes to Consolidated Financial Statements

21. Related Party Transactions (Continued)

The financial data provided for the affiliate schools is as follows:

| | <u>Unaudited, June 30,</u> | |
|----------------------|----------------------------|-----------------------|
| | <u>2010</u> | <u>2009</u> |
| Total assets | \$14,533,408 | \$20,111,447 |
| Total liabilities | <u>24,084,746</u> | <u>22,709,577</u> |
| Net assets (deficit) | <u>\$ (9,551,338)</u> | <u>\$ (2,598,130)</u> |
| | | |
| Total revenue | \$41,409,062 | \$38,219,156 |
| Total expenses | <u>39,923,580</u> | <u>44,061,385</u> |
| Net income (loss) | <u>\$ 1,485,482</u> | <u>\$ (5,842,229)</u> |

See Notes 3, 5, 6, 7, 8, 10, 11, 12, 13, 15 and 19 for investments, accounts receivable, advances to churches, notes receivable, plant assets, assets held in trust, accounts payable, lines of credit, notes payable, liabilities to depositors, and insurance, respectively, for additional information.

22. Prior Period Adjustments

In the consolidated financial statements for the year ended December 31, 2009, errors were made in accounting for donated assets.

These errors have been corrected and have had the following effect on the beginning net assets for the year ended December 31, 2010:

| | <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Permanently Restricted</u> | <u>Total</u> |
|---|----------------------|-----------------------------------|-----------------------------------|----------------------|
| Beginning net assets, as previously reported | <u>\$270,027,905</u> | <u>\$4,195,099</u> | <u>\$62,332</u> | <u>\$274,285,336</u> |
| Adjustments - donated assets | <u>514,053</u> | | | <u>514,053</u> |
| Increase in net assets | <u>514,053</u> | <u>-</u> | <u>-</u> | <u>514,053</u> |
| Beginning net assets, as restated | <u>\$270,541,958</u> | <u>\$4,195,099</u> | <u>\$62,332</u> | <u>\$274,799,389</u> |

In the consolidated financial statements for the year ended December 31, 2008, errors were made in accounting for donated assets, deferred revenue, and accounts payable.

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Notes to Consolidated Financial Statements

22. Prior Period Adjustments (Continued)

These errors have been corrected and have had the following effect on the beginning net assets for the year ended December 31, 2009:

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|--|---------------|---------------------------|---------------------------|---------------|
| Beginning net assets, as previously reported | \$251,320,599 | \$4,464,217 | \$62,332 | \$255,847,148 |
| Adjustments: | | | | |
| Reclassification of funds from temporarily restricted to unrestricted | 25,845 | (25,845) | | |
| Donated assets | (168,356) | | | (168,356) |
| Church ministries - appropriation | (588,495) | | | (588,495) |
| Rental income | 34,452 | | | 34,452 |
| Interest expense | (38,340) | | | (38,340) |
| Decrease in net assets | (734,894) | (25,845) | - | (760,739) |
| Beginning net assets, as restated | \$250,585,705 | \$4,438,372 | \$62,332 | \$255,086,409 |

23. Commitments and Contingencies

The Conference sold property which included fuel tanks. At December 31, 2010, the Conference was evaluating the soil for potential environmental remediation requirements. The cost, if any, was undeterminable as of December 31, 2010.

As reflected in Note 13, the Conference guarantees certain notes payable and equipment leases of affiliate churches and schools. The Conference's maximum credit risk associated with these notes payable guarantees and equipment guarantees totaled \$20,896,424 and \$415,155, respectively, at December 31, 2010.

On January 22, 2010, the Conference was named as a co-defendant in a lawsuit by a third-party for damages associated with a physical injury. Claims and litigation are inherently unpredictable. The probable outcome of this matter is not determinable at this time. The Conference believes that damages, if any, will be covered within insurance limits.

24. Subsequent Events

In 2011, the Conference increased related party notes receivable by \$2,137,606. The amounts were derived in conjunction with qualified construction draws from the tax-exempt bonds funds.

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24. Subsequent Events (Continued)

In 2011, the Conference guaranteed note payable with Pacific Union Conference on behalf of seven affiliates which total \$4,034,862. To date, \$2,351,800 has been drawn on these notes. Additionally, the Conference loaned affiliates an additional \$2,447,606 in conjunction with related draws against the existing line of credit.

In the preparation of these consolidated financial statements, the Conference considered subsequent events through September 19, 2011 which is the date these consolidated financial statements were issued.