

Management Report of Deutscher Caritasverband e. V. for the Financial Year from January 1 to December 31, 2007

Based in Freiburg im Breisgau, Germany, the Deutscher Caritasverband e.V. (DCV) (hereinafter called the German Caritas Association or the DCV) and its members are dedicated to all types of social and charitable work in accordance with the Association's founding statutes. As the umbrella organisation of the individual Caritas associations at federal level, it fulfils the functions of coordination, representation of interests, development of quality, and development of internal structures. The DCV is independent, pursues exclusively charitable and benevolent causes, and is exempt from corporation tax for the 2005 assessment period, as confirmed by the Freiburg tax office in its correspondence dated April 10, 2007.

1. Review of Activities

1.1 Developments in the charity sector and in social and welfare policies

Social policy trends and lobbying activities of the German Caritas Association in 2007

In terms of the focus on a social policy of competency, 2007 was a year in which Caritas lent constructive criticism to the reform efforts and legislative initiatives of the Federal Government. The reforms in the labour market were the main challenge for the lobbying activities of Caritas. The health care reform was enacted and a long-term care reform initiated. Caritas wielded extended lobbying power through the instrument of social monitoring, and was able to participate in the political debate even after the entry into force of social laws. In 2007 the German Caritas Association had overall responsibility within the Bundesarbeitsgemeinschaft der Freien Wohlfahrtspflege (BAGFW) [*Federal Association of Non-Statutory Welfare*], which constituted a particular challenge.

Social labour market for long-term unemployed

The aim of the law on the introduction of the social labour market ("Jobperspektive"), which was passed by the Bundestag in July 2007, is to give people with severe placement handicaps prospects on the employment market. The DCV had been campaigning for years for longer-term public funding for employment. The DCV had been involved right from the outset, from the initial considerations in the Coalition Working Group on the labour market right through to the expert consultation in the Bundestag Committee on Labour and Social Affairs. When the law is enacted, every effort must be made to ensure that those people who are most alienated from the labour market are the ones who

actually benefit from the promotion scheme. They must not be crowded out by people who are less alienated from the employment market. The DCV has appealed against the fact that employment in the social labour market is also subject to the automatic sanctions imposed by SGB II (German Code of Social Law) like any other supply of labour. The DCV had set itself up as case worker, lobbying for a broad scope for decision-making, in order to embrace the target group more fully.

New opportunities for disadvantaged young people

The DCV welcomed the policies adopted by the Bundestag in July 2007 aimed at improving training and the policies governing job prospects for young people with placement handicaps. Temporary combined wages for disadvantaged youth are being introduced, in addition to entry-level vocational qualifications and the extension of careers guidance in schools becoming enshrined in law. The DCV had not asserted its demand for major improvements in this regard in social education mentoring.

Extension of unemployment benefit and the threat of “compulsory retirement”

The DCV has commented extensively on behalf of the BAGFW on the 7th amendment to SGB III (German Code of Social Law). In principle it is a good idea to link a longer period of eligibility for higher-level unemployment benefit (I) to a stronger integration of elderly people in the labour market. The aim of plans for a biannual review of placement options for unemployed persons over the age of 58 should not be to provide additional job placements, however, but should focus more on providing support, especially in the form of further training offers. One positive new ruling in SGB II is the policy that, from the age of 58, unemployed persons may not be forced into early retirement on a reduced pension. The DCV has voiced its criticism in respect of the fact that this is still possible from the age of 63.

Health care reform: proposals for improvement acted on

April 2007 saw the entry into force of a substantial number of reforms to the German Law for Promoting Competition in Statutory Health Insurance which was passed in February 2007. The issues of relevance to Caritas include the introduction of a general obligation to take out health insurance, the extension of the scope of application of home nursing care, the conclusive transfer of curative care services to SGB XI, the introduction of specialist palliative care for outpatients, and reforms for the hospice movement. A number of individual reforms gravitate towards views also defended by the DCV. In terms of health insurance coverage, palliative care, home nursing care, emergency medical services and basic recommendations it was possible to accomplish improvements or to prevent changes for the worse which were brought in by the Bundesrat. Planned increases to the burden on hospitals have been reduced.

Long-term care insurance reform: Caritas adopts differentiated stance on reform

In laying the cornerstones for the long-term care reform in June 2007 and the draft bill on the future development of nursing care legislation at the end of the year, the Federal Government has set out a policy - and one which is to be looked on favourably in many respects - for further development of the care infrastructure, for slimming down bureaucracy in the health care system and for urgently needed improvements in services. The DCV entered the political lobby and issued a statement on the draft bill in close consultation with the Verband katholischer Altenhilfe in Deutschland e.V. (VKAD) [*Catholic Aid Association for Senior Citizens in Germany*], Caritas Behindertenhilfe und Psychiatrie e.V. (CBP) [*Aid Association for the Disabled and Psychiatry*] and the Katholischer Krankenhausverband Deutschlands e.V. (KKVD) [*Catholic Association of Hospitals in Germany*] and the diocesan Caritas associations. In its statement the DCV welcomes the incentives to encourage home nursing care and outpatient care. It emphasises the necessity of introducing case management structures but opposes the dominance of nursing care insurance funds in the plans for care support bases.

Pension reform required

The pension reform adopted by the Federal Cabinet is regarded by the DCV as a necessary means of response to demographic change. Given the continuing rise in life expectancy it is socially justifiable to increase the statutory retirement age by two years over a sufficiently long transition period. There must be an end, however, to older employees being hounded out of the labour market. Otherwise the increase in the retirement age would merely be a stealth cut in pensions. The long transition period should be used to reduce the high levels of discrimination against elderly wage earners on the German labour market.

Social welfare: some changes for the better and some for the worse

There have also been reforms in social welfare (SGB XII). The intervention of the associations prevented the enactment of one of the main reform proposals, namely the change from the gross coverage to the net coverage principle in integration support; this would have incurred a substantial additional administrative burden for integration support agencies. Some of the changes regarded as improvements include the increase in the amount of cash benefits, the payment of rent arrears and the provision of equipment needed by new parents. There are some changes for the worse such as the fact that, under certain circumstances, foreigners may no longer be eligible to claim social welfare. One demand of the Association which was not met was that the regular rate be stipulated not by way of an ordinance but by a parliamentary decision.

Public procurement law in youth and social welfare

In April 2007 the FDP parliamentary party inquired of the Federal Government as to the applicability of public procurement law in youth and social welfare, calling for the procurement by tender of youth welfare services and integration support services. In its reply dated 14 May 2007 the Federal Government clearly declared its belief in the civil right of the service beneficiaries to choose, a right guaranteed by plurality of choice; invitations to tender and consequently the award of contract for social services to one or more service providers could lead to disenfranchisement and disempowerment. The Federal Government referred to the three-sided arrangement (service recipient - service provider - funding agency) as a suitable social legislative framework for safeguarding freedom of choice, economic efficiency and competition among service providers.

Competency initiative helps disadvantaged adolescents

In line with the competency initiative, the German Caritas Association called for better support of children at risk of falling below the poverty line, greater focus of prevention schemes on disadvantaged young people in the areas of health and addiction, and an enhancement in the value of migration-related skills and abilities. One way of achieving a coherent support system for the promotion of training and employment for disadvantaged young people is by easing the transition from school to the world of work. The young people could be better integrated by phasing out legal hurdles to vocational training for young asylum seekers and persons with exceptional leave to remain for humanitarian reasons. Finally the DCV put forward recommendations for combating the implications of debt problems for young people. It also called for unimpeded access to educational establishments for children without legal residence permit status.

Included in its stance on education policy entitled "Equality of educational opportunity for disadvantaged children and young people", the DCV made proposals for strengthening the position of the family in its role as an institution of socialisation and education. Better training opportunities should be opened up for school leavers without even the most basic level of matriculation. Moreover, reference is always made to the contribution of Caritas in these areas. As a result, education policy first became an independent issue pursued by Caritas at federal level.

Social monitoring: talks with Federal Government

2007 saw the continuation of the social monitoring talks between the key non-statutory welfare associations and the Federal Government. The talks focused on the unintentional effects of the social reforms and the joint quest for solutions. The new legislation on basic security for job-seekers (SGB II) and social welfare (SGB XII) formed the background to the talks in 2007 which focused on the impact of these reforms. The major issues centred on in the discussions were the subsistence requirement, the unjust exclusion of groups of persons from SGB II, and the problems in implementing SGB II. Another problem

expounded in the talks was that of the exclusion of young people with an immigrant background, in certain circumstances pertaining to the right of residence, from BAföG [*Federal Law concerning the Promotion of Education*] and SGB II, although this has been largely resolved by the reform of BAföG. In response to the problem that many people are living below the poverty line on account of such atypical regular requirements as non-prescription drugs, the Federal Government has now agreed, for the first time, to look into the solutions proposed by the non-statutory welfare organisations.

Migration and integration

The year was characterised by a variety of initiatives relating to integration and immigration policy. The work which stood out was that done in the context of the National Integration Plan and towards the implementation of the voluntary commitments to integration which were published on 12 July 2007 within the framework of the Second Integration Summit. The DCV has continued to align itself with other welfare associations and refugee organisations in its stance on the revised draft for a law with a view to the implementation of EU directives on rights of residence and asylum. The law has been passed largely unchanged despite the broad base of criticism. Another main focus of the work was the support of voluntarily funded mentoring schemes for disadvantaged children and young people (educational mentors, training mentors, integration and culture guides). Experiences show that this form of participatory citizenship helps to compensate individual children and young people with an immigrant background, making up for deficits and disadvantages in the context of relationships of trust between mentors and those being mentored.

1.2 Income and expenses

1.2.1 Income

The principle sources of financing drawn on by the DCV include subsidies, donations, legacies, membership fees, gains from investing funds not yet utilised, welfare stamp revenues, and proceeds from other activities permitted by the organisation's founding statutes (sale of printed materials, courses, conferences, etc.).

In 2007 the DCV received federal funds, church funds from the Association of German Dioceses (VDD), funds from the European Union (EU), lottery funds as well as subsidies from foundations for the financing of its central office, other offices and its project work. Subsidies increased in 2007 from € 71.0 million to € 75.2 million. The church subsidies and the EU subsidies rose by T€ 350 and T€ 580 respectively and the other subsidies rose by € 3.7 million. The increase in the other subsidies is largely accounted for by higher subsidies from the Misereor German Catholic Bishops' Organisation for

Development Cooperation owing to a new cooperation agreement and by higher subsidies from the Caritas associations from Europe for projects.

Government subsidies decreased, however, by T€ 432. At 59.2%, the proportion of subsidies to overall income is up on the previous year by 1.2 percentage points.

Income by way of donations was down in 2007, decreasing by some 4 % to € 18.2 million (prior year: € 18.9 million). Following the great public appetite for making donations in response to the tsunami disaster at the end of 2004, there is evidence - as in the previous year - of a tendency towards a certain aid fatigue in 2007, a year without any major headline-grabbing catastrophe.

In 2007 we received donations of € 8.2 million for emergency and disaster relief (prior year: € 9.4 million), € 3.0 million for Children's Relief Bethlehem (prior year: € 2.7 million), € 1.1 million for flood victims, € 1.0 million for earthquake victims in general, and € 0.8 million for the victims of the cyclone in Bangladesh. In 2007 the DCV received approximately 169,000 individual donations, as compared to 189,000 the previous year.

A general membership contribution from the diocesan Caritas associations of € 1.524 million was collected in the 2007 financial year. A further € 0.5 million in contributions was raised for the subcommittees of the Labour Law Commission. The amount of both of these contributions is unchanged on the previous year.

Revenue from assets amounted to € 15.6 million, representing an increase of € 1.55 million on the previous year.

The increase in revenue from assets is mainly due to profits realised from the increase in value of securities in the order of € 4.3 million (prior year: € 2.6 million), seen alongside the amortisation of financial assets and securities in current assets, however, which amounted to € 4.9 million (€ 3.8 million of which was written down on the basis of the strict lowest-value principle to securities which are repaid in full on maturity). The DCV essentially applies the strict lowest-value principle to both securities in current assets and securities in fixed assets. Moreover, the option to maintain the value of securities as set out in Art. 253 (5) HGB was exercised. Accordingly no appreciation is calculated for adjustments in capital gains.

The recorded income from rents and leases rose by T€ 45 while the yield on interest dropped by T€ 200. The drop in interest income is essentially due to the € 7.8 million drop in donations for specific purposes. The chart illustrating the "Trend in use/receipt of trust funds" in section 1.2.2 shows the flow of trust funds over the last 10 years.

As in the prior year, the distribution of welfare stamps was managed on a trust basis on behalf of the DCV by the Gesellschaft für Anstaltskredit mhH and the Diakona GmbH under the trust known as Wohlfahrtsbriefmarkenvertrieb für Kirche und Caritas, Rendsburg. In 2007 revenues amounted to € 8.6 million (prior year: € 8.3 million), of which

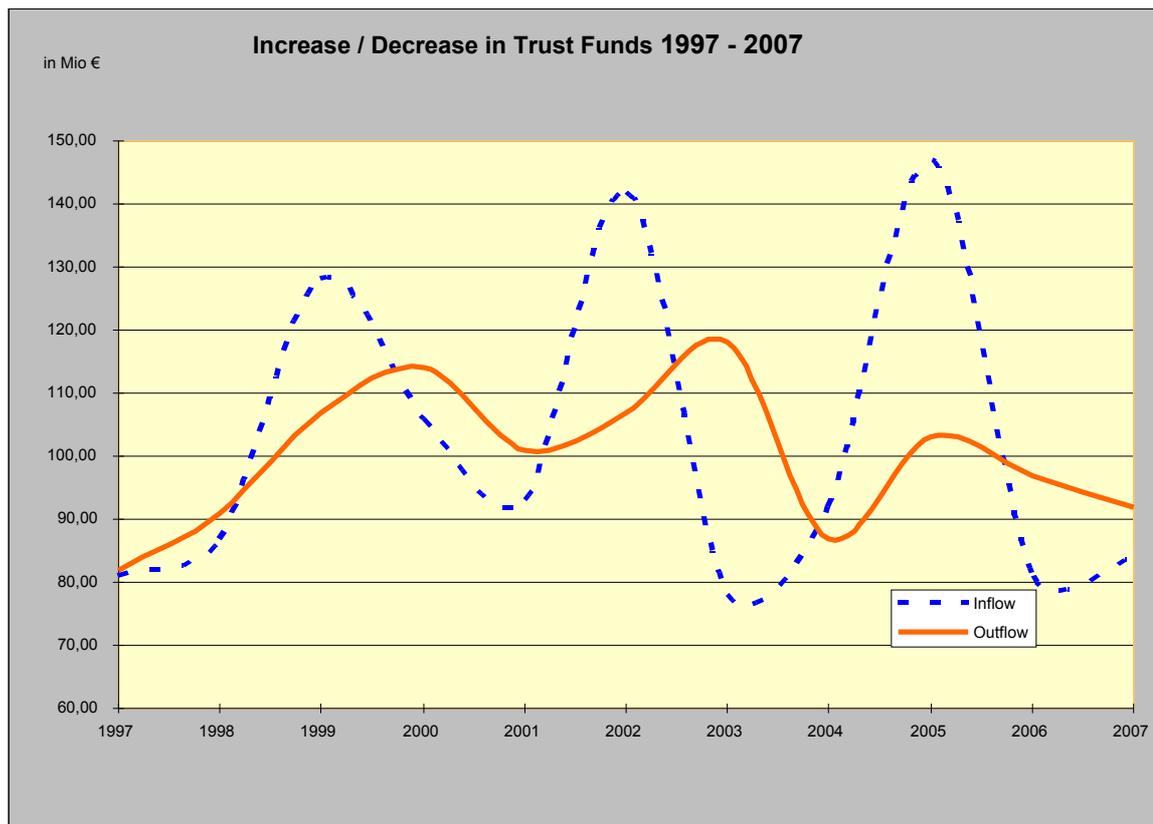
€ 7.5 million (prior year: € 7.1 million) were due to sales of welfare stamps and € 1.1 million (prior year: € 1.2 million) were due to proceeds from surcharges. After deduction of expenses the DCV is left with a surplus of T€ 543 (prior year: T€ 610).

1.2.2 Expenses

In 2007 a total of € 83.3 million was paid out in national and international aid as compared to € 87.9 million in the previous year. This includes aid of € 6.3 million (prior year: € 11.7 million) for the benefit of victims of the tsunami at the end of 2004.

The funds from donations are allocated to individual initiatives depending on the progression of projects. The following chart illustrates how fund outflows (€ 91.9 million in 2007) always exceed fund inflows (€ 84.1 million in 2007) until the trend is reversed by major headline-grabbing disasters.

Funds for specific purposes decreased by € 7.8 million as shown on the balance sheet as at December 31, 2007.



The movements in Funds for specific purposes are presented under point 2.1 Net assets. Personnel costs including pension contributions totalled € 17.8 million (prior year: € 17.3 million), with the number of employees on the payroll at the reporting date converted to 289.51 full-time units (prior year: 283).

The increase in project-related positions accounts for the fact that the number of employees at the reporting date is up on the previous year.

Administration and advertising costs cover all expenses which cannot be directly assigned to the purposes eligible for tax relief which are specified in the founding statutes. The percentage of administration and advertising costs to total expenditure for 2007, according to the guidelines published by the German Central Institute for Social Issues (DZI), is calculated as follows:

Deutscher Caritasverband e.V.		2007	
		€	%
Project expenses	direct expenses under the terms of the statutes (including project expenses)	95,750,964.96	
	Project promotion	2,067,911.06	
	Project mentoring	2,804,133.18	
	Campaigns, education, and information under the terms of the statutes	1,188,292.39	
Total project expenses		101,811,301.59	91.40
	Administration	7,059,888.60	
	Advertising and general PR	2,525,349.85	
Total expenses advertising and administration		9,585,238.45	8.60
Total expenses*		111,396,540.04	100.00

* Expenses relating to business operations and asset management are not factored in when calculating the administration cost ratio because there is a surplus after netting out with income.

The DZI provides a graduated scale for spending on advertising and administration as an orientation guide, with up to 35 % on advertising and administration regarded as a reasonable outlay. Under 20 % on the same scale is regarded as adequate and less than 10 % as low. At 8.60 % the DCV's administration cost ratio in 2007 is in the low increment. This meets the criteria of the DZI in respect of the administration cost ratio.

1.3 Investments

The large conference room in Lorenz-Werthmann-Haus located in Karlstraße 40 in Freiburg was completely renovated. The renovation work included fitting a new ventilation and air-conditioning system and modernising the fixtures and fittings.

Alterations and renovations were made in respect of the ongoing building maintenance. There were no other major investments in 2007.

1.4 Employees and employment benefits

Personnel costs and the number of employees have already been covered in 1.2.2. 2/3 of these employees are women and 1/3 are men. Just under 40 % of all the employees work part-time.

The guidelines for employment contracts in the institutions of the German Caritas Association (AVR) apply. Employees are entitled to additional pension benefits with the Church Supplementary Pension Fund (KZVK). Employees who entered into service prior to August 1, 1998 are entitled to assistance in cases of illness, childbirth and death. Employees who entered into service prior to January 1, 1976 are entitled to a retirement pension according to the company's own pension policy which was in force until then, as are employees who obtained entitlements within five years of this cut-off date.

The internal in-service training scheme was continued and enhanced, offering a wide range of opportunities for staff to develop their professional expertise and social skills. The Lorenz-Werthman-Haus received basic certification as a family-friendly workplace from the non-profit Hertie Foundation. The three-year auditing process which goes hand-in-hand with this certification has overseen further additions to the existing family-friendly working conditions. These include setting up an office with a children's play area, introducing a scheme for keeping in contact with staff on parental leave, adopting procedures and policies to ease the transition for employees into family life as occasioned by pregnancy and parental leave, setting up a childcare facility staffed by volunteers for cases of emergency, and allocating a quota of places in a childcare facility.

The Board of the German Caritas Association is made up of Dr. Peter Neher, President, Prof. Dr. Georg Cremer, Secretary General, and Niko Roth, Financial and Personnel Director. The remuneration of the members of the Board is based on Pay Regulation B. The three members of the Board receive a combined gross annual income of T€ 358 including social insurance contributions (prior year: T€ 353) or TE 299.5 excluding social insurance contributions (prior year: T€ 297).

1.5 Review of activities

The Board is satisfied with the course of operations in 2007. The balance sheet total is € 243 million as compared to € 251 million in the previous year. The € 8 million decrease in the balance sheet total is primarily due to the decline in income by way of donations and the continued phase-out of funds for special purposes.

The number of donations in 2007 is roughly on a par with the average in years without any major headline-grabbing disaster.

The balance sheet profit of € 0.2 million (prior year: € 2.5 million) resulted in a 0.4% increase in equity. T€ 439 in reserves was added, but offset by the use of construction and investment reserves amounting to T€ 340, resulting in a T€ 99 increase in the inventory of reserves as at 31.12.2007.

The decision of the tax authorities regarding the DCV's appeal concerning a VAT group consisting of the German Caritas Association and the Federal Catholic charity associations is still outstanding. As a result of the tax audit relating to the period 1989 to 1996, which was finalised in 2001, this VAT group was disallowed. Additional tax assessments were issued in 2002, against which the DCV appealed. This appeal was rejected by the tax authorities in 2003, prompting the DCV to appeal in July 2003 to the Finanzgericht Baden-Württemberg, Außensenate Freiburg [*Baden-Württemberg Tax Court, Freiburg Division*].

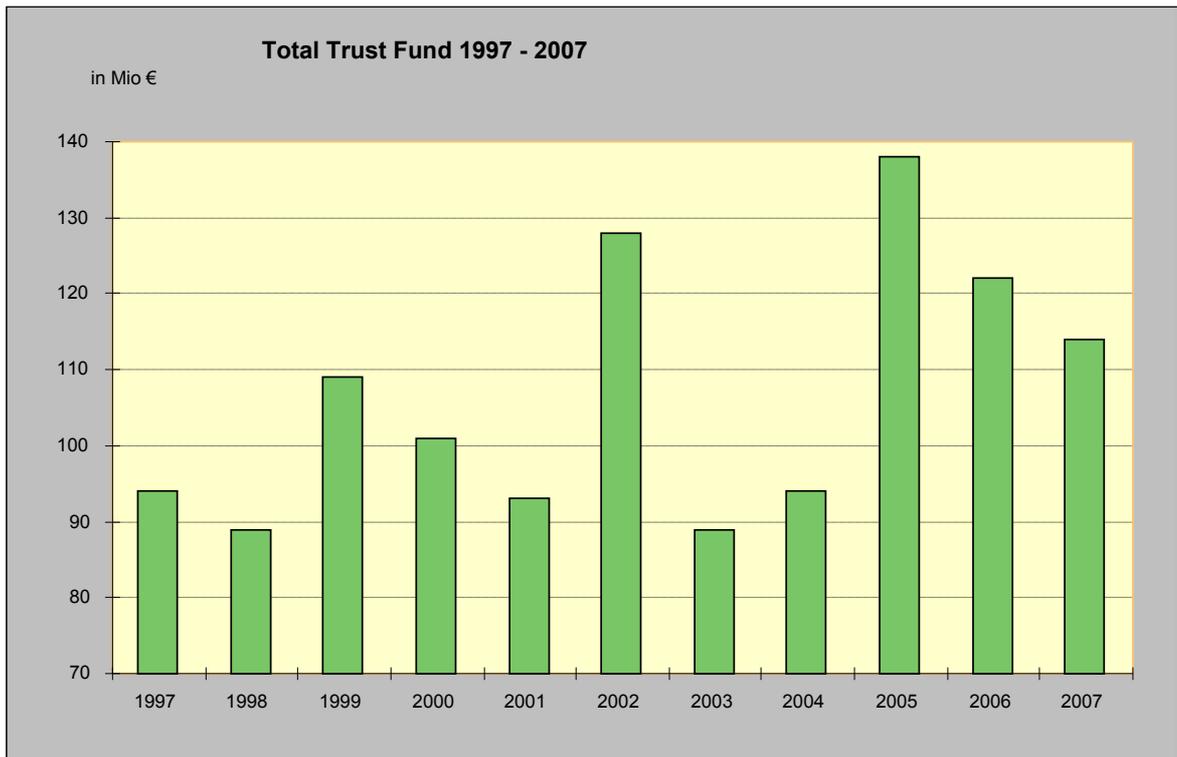
In 2007 the tax authorities completed their audit of the tax assessments from 2000 to 2002 but the audit report has yet to be issued. The audit for 2003 to 2005 has been requested and is expected to begin in April 2008.

2. Review of Net Assets, Financial Position and Earnings

2.1 Net assets

The decrease in the balance sheet total is primarily due to the many relief efforts. In total, the Funds for special purposes on the liabilities side of the balance sheet were down on the previous year by € 7.8 million to € 114.4 million. The funds disclosed under the item Funds for special purposes serve to finance projects and are allocated to the individual projects depending on the progress being made.

The movements in these Funds for special purposes are illustrated on the following chart:



By contrast, the equity on the liabilities side of the balance sheet increased by € 0.2 million to € 86.3 million as a result of the balance sheet profit. The equity ratio on the balance sheet now amounts to 35.5 % (prior year: 34.2 %).

The provisions for pensions and similar obligations decreased by € 0.6 million to € 9.8 million due to deaths, increases in age and changes to entitlement. Other provisions decreased by € 0.1 million. The percentage of long-term capital in 2007 is 45.5 % of the balance sheet total (prior year: 44.4%).

On the assets side, extensive relief efforts effected a € 7.9 million decrease in bank balances to € 21.5 million, while securities in current assets increased by € 3.9 million to € 105.8 million.

Securities in financial assets increased by € 1.2 million to € 68.4 million on account of the restructuring of assets. The total decline recorded in tangible and intangible fixed assets was € 3.5 million. The decrease resulted from scheduled depreciation of € 2.0 million over the financial year and the transfer of € 2.2 million to building and real property assets for the Benedict Kreutz Foundation which was set up in 2006. Seen alongside the depreciation and the drop in fixed assets, however, are investments of € 0.8 million in tangible and intangible assets. Fixed assets are down on the previous year by € 2.7 million to € 107.5 million although their proportion of the balance sheet total has risen from 44.0 % in the previous year to 44.3 %. Fixed assets are financed exclusively by long-term capital.

2.2 Financial position

In 2007 regular operating activities resulted in net cash outflows of T€ 733 (prior year: net cash outflow of € 14.9 million), investment activity led to cash outflows of € 1.0 million (prior year: € 2.9 million), and financing activity led to an outflow of T€ 478 (prior year: inflow of € 1.8 million). Overall, financing funds decreased by € 4 million.

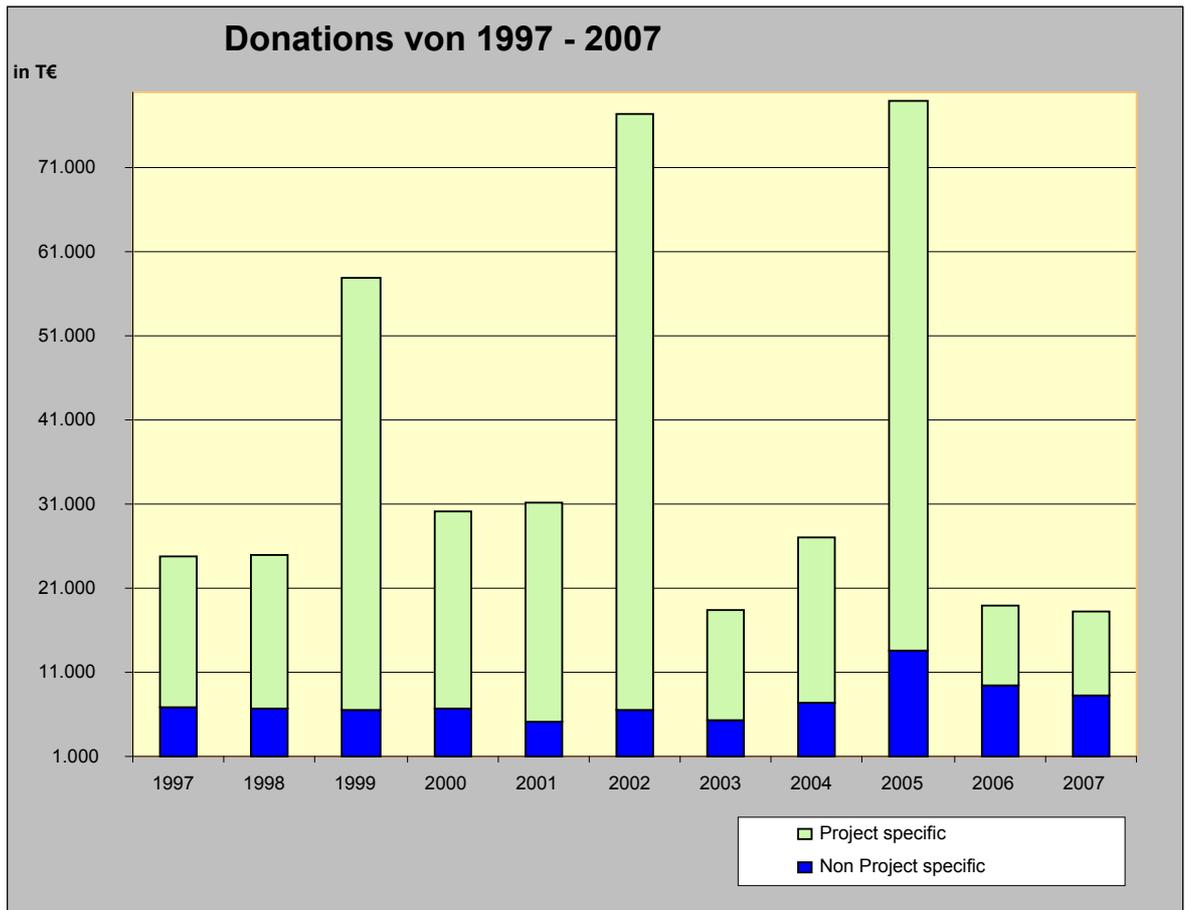
In 2007 earmarked cash reserves amounted to € 28.4 million as compared to € 31.4 million in the prior year (financing funds of € 127.4 million plus receivables, other assets and inventories of € 7.2 million, the surplus of financial assets over pension fund commitments of € 2.6 million and less short-term debt of € 16.9 million and funds for specific purposes of € 91.9 million going out at short notice). They cover the average monthly financing requirements (1/12 of the annual expenses less depreciation and expenses from the addition of liabilities) for roughly three months as was the case in the previous year. The Association was financially solvent for the entire financial year.

2.3 Results of operations

The movements in proceeds during 2007 have already been presented in section 1.2.1 and movements in expenses in section 1.2.2.

The trend in donations is largely dependent on disasters which get high levels of media coverage, leading to major fluctuations in donation proceeds for Caritas international. Like the previous year, the year under review was devoid of any major headline-grabbing disasters, which resulted in donations being significantly down on 2004 and 2005 (tsunami disaster).

The annual fluctuations in donation income can be seen in the following graph:



In 2007 and 2006 the donations were comparable to those received in 2003, the year after the record flooding in East Germany and in Central and South-East Europe. Years with major headline-grabbing disasters and above-average donation proceeds are often followed by years with significantly fewer incoming donations. The graph also shows non-project-specific donations. These donations can be used by Caritas international for projects which do not receive direct media attention. It still tends to be difficult to attract donors for general emergency and disaster aid in other regions not covered by the media.

Interest and dividend income was down to € 7.4 million, representing a decrease of € 0.2 million on the previous year. Capital gains of € 4.3 million were realised (prior year: € 2.6 million). The capital gains were offset by capital losses of € 0.4 million (prior year: € 0.4 million) and depreciation of € 4.9 million (prior year: € 2.9 million).

€ 3.8 million of the depreciation of € 4.9 million is essentially the consequence of applying the strict lower-value principle to bonds, which account for the majority stake in the DCV securities account. (Composition of portfolio as at 31.12.07: 86% bonds and 14% equity funds, property funds and commodities). The general interest rate trend and the increase in risk premiums on the capital market led to falling bond prices (predominantly with medium-term and long-term bonds) although the bonds are repaid back at face value on

maturity. Approximately T€ 650 of the depreciation is due to the crisis in the American sub-prime market which has exerted sustained pressure on the financial markets. However, the DCV has no direct investments in securities directly affected by the sub-prime crisis. As the crisis has led to a negative market performance overall, however, the DCV is indirectly affected by the resulting markdowns.

The DCV benefited from the favourable trend in the stock markets in 2007, realising capital gains at the end of the year by selling equity funds.

The balance sheet profit in 2007 of T€ +202 (prior year: € + 2.5 million) is made up of the net surplus for the year of T€ 301 (prior year: € 2.5 million) and an allocation to reserves of T€ 99 (balance of funds withdrawn and injected).

The following factors must be taken into consideration when reviewing the overall result for the year:

- Transfer of funds for asset endowment of the Benedict Kreutz Foundation (€ 2.2 million: building and real property assets transfer).
- Depreciation of financial assets and current securities of € 4.9 million due to the general trend in the capital market (interest rate trend and sub-prime crisis) and capital losses of € 0.4 million, albeit alongside capital gains of € 4.3 million.

2.4 Opportunities and risks in respect of future development

The “Developments in the charity sector and in social and welfare policies” set out at the beginning of this report (section 1.1) emphasise that changes in the sector have an impact not only on needy individuals but also on services and institutions, including the DCV as an umbrella organisation. The further assessment of future trends refers only to the immediate financial and economic sphere of the DCV in its remit as an umbrella association. This report does not cover the trend anticipated in services, institutions and the organisations of the Association.

The basic framework for the activities of umbrella organisations is set out in Article 6 of the founding statutes of the German Caritas Association. In a bid to focus even more on this framework, the Board developed strategic goals in collaboration with the department managers and these goals were approved by the Caritas Council on November 22, 2006. The strategic goals serve as a general guide, define the priorities, and specify perspectives on behalf of the Board together with the central office and main representative bodies. At the same time, they form a basis for the planning of enterprise and human resources. The following goals were set:

- By the end of 2011 we want the DCV to have developed a theologically inspired profile reflected in its ethical stance and to have shaped its identity as a key player in the quest for a welfare-oriented church.
- We want the German Caritas Association to be an efficient and powerful association by 2011 and one with which its organisations and members can identify.
- By the end of 2011 we want the German Caritas Association to be taking an active part in shaping a preventive and empowering welfare policy and to have consolidated its involvement in the realm of civil society.
- By the end of 2011 we want the German Caritas Association to have developed a stance established in regulatory policy and in the legal profession towards structuring the social services markets, with strategies and instruments as to how the Caritas enterprises might develop in these markets having been promoted.

Each goal has several sub-goals on schedule for attainment in 2007 and 2008. The regular review and adjustment of the strategic goals is one task in the strategic process which has been established as a long-term process in the central office. The strategic goals and their level of attainment are reviewed in the quarterly strategy workshops attended by the Board and the departmental heads, where strategic projects are also assessed and evaluated. The following sub-goal came to fruition in 2007: "The issue of equality of education has been developed as a legislative and political sphere of activity of the individual Caritas associations. The specific contribution of Caritas has been identified and highlighted". The sub-goal expressed as follows: "The aspect of prevention has been effectively represented in the political debate on the reform of the coverage of the health and long-term care risk" was included in the operational labour and positioning of the DCV.

The Caritas Council was briefed for the first time on November 21, 2007 about the progress of the strategic goals. Possible adjustments to the strategic goals in the wake of developments in 2008 will be submitted to the Caritas Council in November 2008 for consultation and approval.

The development of the Association was described as an important step in the last management report. An agreement on the professional and political tasks and responsibilities was concluded with other professional associations. Under the Federalism Reform adopted by the Bundestag and the Bundesrat, social tasks will also be shifted to the states and partially to municipalities. The Association needs to make technical and organisational changes to its political lobbying in the light of this development. The Board has responded by initiating the project entitled "Federalism and decentralisation: consequences for the Caritas associations" which deals with the Federalism Reform and decentralisation in two separate groups.

A balanced budget was passed for 2007 and a balanced medium-term financial forecast adopted for 2008 to 2010.

It was evident from the figures that personnel costs are rising year on year while income remains more or less static. The additional annual costs can only be met by increased use of investment income. The Caritas Council therefore issued the following statement on the adoption of the 2007 budget: "The Caritas Council, upon the recommendation of the Finance Commission, hereby acknowledges and approves the medium-term financial forecast for 2008 - 2010 subject to measures being taken in this period to ensure a balanced operating budget in the future through independent investment income (according to the retention of actual value). This will also need to be reviewed as part of the medium-term financial planning for 2008 - 2011."

In consideration of this development, the Board had already presented its "Strategic considerations of the Board on the Association's operating budget, medium-term financial forecast, staffing schedule, and on the use of surpluses from assets" in the July 2006 meeting of the Caritas Council. One of the ways in which the Board sought to achieve this target was by establishing the following criteria: "The annual increase in personnel costs of approximately € 325,000 per annum (average) could be met in the following ways:

- a) Moderate decrease in established posts which become vacant due to retirement or other reasons (fluctuation). This measure requires a personnel development strategy. The crucial factors in this are the fulfilment of the tasks outlined in the statutes and the strategic goals of the Board which are yet to come to fruition.
- b) Savings in cost of materials and/or an increase in other income and revenue.
- c) Moderate use of income from assets."

These proposals were fundamentally approved by the Caritas Council.

On this basis the Board updated and substantiated its strategic considerations and submitted a human resources planning policy up to 2011. This is to be adopted and will be updated on an annual basis in the light of the medium-term financial forecast. The Caritas Council will bring an annual report on progress. The Board has also developed scenarios factoring in the potential financial collapse of major income items. One general observation is that the DCV is increasingly dependent on its assets to fulfil its brief as an umbrella organisation at federal level, European level and worldwide. The principle of retaining the real value of property assets and capital assets therefore applies to the administration and handling of its assets. The financial investment guidelines adopted by the Finance Commission apply to the investment of the capital assets. These are also observed by the companies in which the DCV is the sole investor and by the foundations of the DCV. The real estate assets are to be kept, maintained and used in such a way as to maximise appreciation and added value.

The central office of the DCV is mainly financed by subsidies from the Catholic Church and the Federal Government, membership contributions from the diocesan Caritas

associations, the sale of welfare stamps, lottery funding, and investment income. The Federal Government subsidy according to Individual Plan 17, Chapter 1702, Title 684.04 remains unchanged and is not index-linked. This and other Federal Government subsidies for project work in Germany and abroad are subject, like many other items, to annual budget policy reviews. The DCV must take account of this in its financial planning and observe the principle of prudence.

The DCV receives a so-called global subsidy from church tax funds as well as subsidies for specific projects in Germany and abroad. The so-called global funds decreased from 2004 to 2006 by a total of 15.9%. There were no further decreases in 2007, nor for 2008. Here, too, the principle of prudence applies to further financial planning.

The "Aktion Mensch", "GlücksSpirale", and "Deutsches Hilfswerk" lotteries are an important source of financing for services and institutions, for the associations with national remits, and for the DCV. The Board has been issuing a lottery report on behalf of the entire association since 2005, bringing these services into view and underlining the importance of the lotteries. Special joint activities with other major non-statutory welfare associations are required for the GlücksSpirale. In contrast to the other two (television) lotteries, the GlücksSpirale lacks an effective broadcast and a personality to promote the aims and concerns of the lottery in public.

The welfare stamps are another source of financing the tasks of the umbrella organisation, especially the work on policies, projects and models. For local institutions and services they constitute an effective means of support for projects and tasks which are divided into small sections. The welfare stamps should therefore be regarded as one part of a fundraising strategy. The postal monopoly still exists despite the political expectations in 2007. The implications feared at that time in respect of the sale of the welfare stamps have not materialised. The political debate on the abolition of the postal monopoly rages on. It is important in this respect to lay prudent financial plans and to work on developing new ideas and strategies to preserve the welfare stamps and similar products.

The DCV and its relief organisation "Caritas international" are reliant on donations to fund the international emergency and disaster relief. Following the overwhelming response and the unprecedented amount donated in the wake of the tsunami disaster in 2004/05, there has been a persistent decline in donations since 2006. There has been no corresponding decrease, however, in worldwide poverty, natural disasters and armed conflicts. As a fundraising organisation the DCV is reliant on the support of the media. The aim must therefore be to cooperate with the media, reporting on the necessary relief projects and calling for donations.

Developments on the capital markets offer both opportunities and risks with regard to investment income. The DCV pursues its investment transactions on the basis of its financial investment guidelines. These guidelines were amended on March 17, 2006 in

response to market conditions. The investment policy laid down in these guidelines predominantly excludes investment transactions with currency risks.

The DCV is nevertheless subject to the interest rate risk and the risk of changes in market conditions.

Since erupting in the summer of 2007, the crisis in the real estate and financial markets in the USA (sub-prime crisis) has sent out a second shock wave onto the international capital markets and stock markets which is reflected in the movements and fluctuations in prices, some of them quite dramatic, in many asset classes. The fears of a US recession led to another stampede to the prime sector in the first few weeks of 2008, switching of higher-risk assets into lower-risk assets, an escalation in volatility on the stock markets and/or a reduction in leveraged loans and derivatives.

The risk reassessment process started in the summer of 2007 is still going on. The US stock market - still the benchmark for the majority of stock purchases - is expected to fluctuate between the negative fallout from the sub-prime crisis and the positive effects of interest rate cuts and of the weak US dollar, and will probably remain volatile in 2008. Write-downs at banks and the reassessment of liabilities will put further pressure on the markets. We are assuming that the repercussions of the sub-prime crisis will persist and are therefore expecting further amortisation of the securities which are indirectly affected. The investment strategy adopted by the DCV is therefore currently being affected in terms of its financial investment guideline in the light of increased security (rating) criteria and diversification factors.

The valuation levels on the stock markets have slumped. This combined with stable global market fundamentals ought to assist the markets in the medium to long-term. The stock markets should be able to override the current uncertainties although it is important for the high levels of volatility to subside for the time being. An end to the sub-prime crisis would herald new opportunities to enter the market, most notably the stock market.

The European Central Bank (ECB) has left the key interest rate for the eurozone at 4 % for the tenth time in succession. Despite the financial crisis and increasing growth risks, it currently sees no scope for interest rate cuts on account of the high level of inflation. The assumption on the basis of a 12-month projection is a reduction in interest rates for the eurozone to 3.25% in the short term. 10-year bonds in the eurozone are expected to bring increasing returns of between 4.25 and 4.75%.

While the economic crisis persists, the future outlook is for further high risk premiums and therefore markdowns on corporate bonds with high credit standing.

Further depreciation is to be expected by the end of 2008 on account of this situation in the capital markets. This risk has been largely factored in by the fact that the duration in the annuities sector is between three and four years and the equity exposure is kept low.

The DCV is not a corporate group but an umbrella organisation of legally independent Catholic charitable bodies including their facilities and services. As such, it does not have access to their financial statements and balance sheets. The Caritas "brand" has a "good reputation" in the public perception, as corroborated by surveys, benefiting all its services and institutions. This also explains why the image of the entire association and of the central office of the DCV can be damaged by the malpractice of individual legal entities or their services and institutions, but also by the misconduct of individual directors, especially if it becomes public. Any such damage to the organisation's image can have political, ecclesiastical and also financial consequences. The Board of the DCV cannot take any direct action to prevent such situations. Its monitoring and sanctioning options are limited. Against this background, the Board will persist in reminding the legal entities of their autonomy and responsibility and in pursuing the creation of suitable monitoring and supervisory structures. Valuable advice for these entities was published by the German Bishops' Conference in its support material declaration 182 entitled "Soziale Einrichtungen in katholischer Trägerschaft und wirtschaftliche Aufsicht" [*Welfare services funded by the Catholic Church and supervised by industry*], a work which came about with substantial input from the DCV and which was republished in 2007 with minor changes. The progress in applying this support material is to be evaluated in 2008 in collaboration with the diocesan Caritas associations.

The immediate risks to which the DCV is exposed as a result of its federal and international remit have been recorded, assessed and documented in a risk report within the framework of the risk management system since 2006. This report is submitted to the Board every quarter. The Board has also set up an internal audit system and has commissioned Solidaris Revisions-GmbH Freiburg to conduct the audits. The Board has approved an annual inspection and audit schedule and, in addition to the written reports, it has arranged for delivery of regular verbal reports several times a year by the internal audit body.

3. Significant Events in the Year

The Board embarked upon pursuing the strategic goals, their having been approved by the Caritas Council in March 2006. The results are presented in section 2.4.

The structural and organisational changes introduced with the reform of the statutes are making an impact. In the political sphere and in the media the Association is viewed as an informed expert on the basis of its statements and stances on social and welfare policy. This is clear from the accounts given in section 1.1 "Developments in the charity sector".

Assembly of Delegates

The four committees on "Social Policy and Society", "Caritas Profile", "Caritas Finances" and "Working with Caritas" brought extensive reports to the Assembly of Delegates in October 2007 and in some cases tabled their first submissions ready to be voted on at the Assembly. These committees have an important role in shaping opinion in the Association and they prepare the professional and political submissions for the Assembly of Delegates.

Association rules

The Assembly of Delegates passed the second part of the Association rules in October 2007, the first part having been adopted one year earlier. This completes the Association rules.

German Caritas Association employment law and collective bargaining law

The future of the services and facilities of Caritas will be determined by their competitiveness. In order to be competitive, it is also necessary for the personnel costs, which are an important cost factor, to be able to compete with those of the competitors. There is a need, on the basis of the third way (consensus principle), to obtain more flexibility which is to be achieved by shifting the negotiation and decision-making levels from federal to regional or association level. The goal is to create a framework policy that no longer excuses the creation of subsidiaries of companies or company units for pay scale classification reasons. There is an urgent need, on the one hand, for adherence to the Basic Church Order and the Association rules. On the other hand, it is important to retain jobs and to safeguard the existence of the services and institutions in order to be able to continuing fulfilling the remit as a charity. What is needed is an "umbrella policy on pay scales" providing coverage for all the services and institutions. If Caritas is guided by benchmark rates in future and if the salary trends are to be regarded in close connection with refinancing terms and conditions then the necessary expertise is required on the Labour Law Commissions and in the preparatory work for these commissions. This is to be achieved, as before, by the exemption quotas and also by the formation of a "Rate Institute".

In March 2007 in Frankfurt the extraordinary Assembly of Delegates of the German Caritas Association adopted a “Code for the Labour Law Commission”, the regulations for the election of the employer and employee representatives, and the “Guidelines on Pay Scale Policy”. The ordinary Assembly of Delegates in Erfurt in October 2007 approved the funding policy for the Labour Law Commission and set out the financial framework for four years (legislative period of the Labour Law Commission). As the labour legislator for Caritas, the DCV has thus laid all the legal, organisational and financial foundations for effective and sustainable labour law. The Federal Commission and the six Regional Commissions were elected in the autumn of 2007.

The Labour Law Commission, whose term of office ended on 31.12.2007, did not achieve its aim of enacting a new set of employment contract guidelines (“AVR-neu”). It is not possible for the executive bodies of the DCV to influence these decisions. They adhere to the principles of the “third way” and the independence of the Labour Law Commission. This puts all the more pressure on the two sides in the Labour Law Commission to make the urgently needed decisions.

Financial transparency

Financial transparency is becoming more and more important. This is also becoming evident in the discussion on the reform of the charity sector law. The DCV promotes this transparency and leads by example. Its financial report, complete with balance sheet, income statement and management report, is published on the internet and is thus available for general public consumption. Excerpts are also published in the Caritas yearbook and in the brochure “Einblicke” [*Insights*]. In 2007 the DCV was again cited as an example of this form of transparency in the book “Deutsche Standards - beispielhafte Geschäftsberichte” [*German Standards - Exemplary Financial Reports*]. The best 100 companies were commended in this book for exemplary standards and professional excellence in reporting. The German Caritas Association was ranked sixth out of 43 participating organisations in the 2007 Transparency Award issued by audit and consultancy firm PricewaterhouseCoopers (PwC) and judged by the University of Göttingen in terms of professionalism and content.

4. Outlook

In its meeting on 20./21.11.2007 the Caritas Council approved the 2008 operating budget estimate and the medium-term financial forecast for 2009 - 2011. The preliminary estimate indicates a balanced operating budget for 2008. Risks in connection with the movements in income - especially in subsidies - are addressed and documented in the Board's risk management system.

The financial forecast for 2009 - 2011 shows that the financing of the future operating budgets is balanced and the necessary resources thus guaranteed. Annual wage rises and other increases can essentially be met by additional investment income.

In its human resources planning policy (see 2.4) the Board has taken measures to cap the use of investment income in the following years. The aim is the long-term preservation of assets and the hedging of risk.

The assumption made when drawing up the project budget for 2008 and the medium-term financial forecast for 2009 - 2011 is that there will be no changes in the trend in donations and in the level of subsidies. Following the allocation of € 47 million to international aid projects in 2007, the projected allocation of funds for 2008 is some € 44 million.

In 2007 € 31.8 million was spent on domestic aid projects (migration and integration, child and youth welfare, assistance for the elderly and disabled, health promotion, etc.), which are largely financed by third-party funding. The level of deployment of funds in this area is expected to remain constant in the following years. The execution of projects is, however, dependent on the consent of the donor.

5. Significant Events After the End of the Financial Year

New Caritas labour law

The Federal Commission and the six Regional Commissions elected in the fourth quarter of 2007 were constituted in the first quarter of 2008 or are in the process of constituting. In its meeting on 04.03.2008 and 05.03.2008 the Caritas Council passed the articles of association for the Rate Institute. The contract was also authenticated by a notary on 05.03.2008 so that the supervisory board can be set up and then the management appointed.

Freiburg i. Br., April 10, 2008

Dr. Peter Neher
President

Prof. Dr. Georg Cremer
Secretary General

Niko Roth
Finance and
Personnel Director