

THE MOODY FOUNDATION

*Financials*  
2004 — 2005



## Independent Auditors' Report

The Board of Trustees  
The Moody Foundation:

We have audited the accompanying statements of financial position of the Moody Foundation (the Foundation) as of December 31, 2005 and 2004, and the related statements of activities, changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these 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 financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 financial statements referred to above present fairly, in all material respects, the financial position of The Moody Foundation as of December 31, 2005 and 2004, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information included in schedules 1 and 2 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements, and in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

**KPMG LLP**

February 20, 2006

**Statements of Financial Position**

December 31, 2005 and 2004

ASSETS	2005	2004
Cash and cash equivalents	\$ 18,683,000	20,268,000
Investments:		
American National Insurance Company (notes 2 and 3)	488,558,000	451,693,000
Gal-Tex Hotel Corporation (note 3)	9,526,000	9,534,000
Marketable equity securities (note 3)	35,826,000	33,497,000
Bonds and other debt instruments (note 3)	336,685,000	313,321,000
U.S. Treasury obligations (note 3)	9,014,000	9,255,000
Notes receivable (note 5)	11,884,000	11,955,000
Real estate	1,500,000	1,500,000
TOTAL INVESTMENTS	892,993,000	830,755,000
Accrued interest	5,904,000	5,142,000
Assets held for charitable purposes	658,000	658,000
Other assets, net of accumulated depreciation of \$1,627,000 and \$1,618,000 in 2005 and 2004, respectively	82,000	100,000
Assets held in charitable remainder trust (note 4)	915,896,000	801,400,000
TOTAL ASSETS	\$ 1,834,216,000	1,658,323,000
LIABILITIES AND NET ASSETS		
Liabilities:		
Grants payable	\$33,909,000	19,066,000
Deferred tax liability	9,136,000	8,696,000
Accounts payable and accrued liabilities	694,000	548,000
TOTAL LIABILITIES	43,739,000	28,310,000
Commitments and contingencies (notes 10 and 11)		
Net assets:		
Unrestricted	711,320,000	671,430,000
Temporarily restricted (note 6)	457,948,000	400,700,000
Permanently restricted (note 7)	621,209,000	557,883,000
TOTAL NET ASSETS	1,790,477,000	1,630,013,000
TOTAL LIABILITIES AND NET ASSETS	\$ 1,834,216,000	1,658,323,000

See accompanying notes to financial statements.

**Statements of Activities**

Years ended December 31, 2005 and 2004

## Changes in unrestricted net assets:

	2005	2004
Revenues and gains:		
Interest	\$ 21,848,000	19,713,000
Dividends	2,379,000	2,060,000
Net unrealized and realized gains and losses on investments	(10,038,000)	6,939,000
Equity in income of affiliates (note 2)	52,383,000	55,001,000
Net assets released from restriction (note 4)	9,672,000	9,579,000
Other income	1,110,000	261,000
Grants lapsed or withdrawn	19,000	8,705,000
Total unrestricted revenues and gains	77,373,000	102,258,000

## Expenses and losses:

Grant appropriations:		
Community and social services	29,284,000	6,158,000
Health and science	312,000	1,722,000
Education	826,000	1,643,000
Arts, humanities, and religion	243,000	60,000
Total grant appropriations	30,665,000	9,583,000
General and administrative expenses (note 9)	4,190,000	3,969,000
Expenses incurred in the production of revenues and gains	1,313,000	1,179,000
Provision for federal excise taxes (note 8)	1,315,000	1,328,000
Total expenses and losses	37,483,000	16,059,000
Increase (decrease) in unrestricted net assets	39,890,000	86,199,000

## Changes in temporarily restricted net assets:

Change in value of charitable remainder trust (note 4)	66,920,000	75,916,000
Net assets released from restriction (note 4)	(9,672,000)	(9,579,000)
Increase in temporarily restricted net assets	57,248,000	66,337,000

## Changes in permanently restricted net assets:

Change in value of charitable remainder trust (note 4)	66,920,000	75,916,000
Net unrealized and realized gains (losses) on investments	(5,604,000)	3,996,000
Equity in income of ANICO, net of dividends received (note 2)	2,010,000	2,266,000
Increase in permanently restricted net assets	63,326,000	82,178,000
Increase (decrease) in net assets	\$ 160,464,000	234,714,000

See accompanying notes to financial statements.

**Statements of Changes in Net Assets**

Years ended December 31, 2005 and 2004

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Net assets, December 31, 2003	\$ 585,231,000	334,363,000	475,705,000	1,395,299,000
Increase in net assets	86,199,000	66,337,000	82,178,000	234,714,000
Net assets, December 31, 2004	671,430,000	400,700,000	557,883,000	1,630,013,000
Increase in net assets	39,890,000	57,248,000	63,326,000	160,464,000
Net assets, December 31, 2005	\$ 711,320,000	457,948,000	621,209,000	1,790,477,000

See accompanying notes to financial statements.

**Statements of Cash Flows**

Years ended December 31, 2005 and 2004

	2005	2004
Cash flows from operating activities:		
Change in net assets	\$ 160,464,000	234,714,000
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Distributions received from charitable remainder trust	9,672,000	9,579,000
Net realized losses on investments, permanently restricted	1,046,000	1,481,000
Net unrealized (gains) losses on investments	16,688,000	(4,053,000)
Equity in income of affiliates	(55,398,000)	(58,268,000)
Change in value of charitable remainder trust	(133,840,000)	(151,832,000)
Deferred tax expense (benefit)	440,000	875,000
Depreciation	62,000	89,000
(Increase) decrease in other assets	(762,000)	96,000
(Decrease) increase in grants payable	14,843,000	(56,745,000)
(Decrease) increase in other liabilities	146,000	533,000
Net cash provided by (used in) operating activities	13,361,000	(23,531,000)
Cash flows from investing activities:		
Proceeds from the sale or maturity of investments	59,398,000	73,288,000
Purchase of investments	(101,538,000)	(89,403,000)
Capital expenditures for property and equipment	(44,000)	(35,000)
Cash received on notes receivable	71,000	20,000
Dividends received from affiliates	18,541,000	18,479,000
Net cash provided by (used in) investing activities	(23,572,000)	2,349,000
Cash flows from financing activities:		
Restricted distributions received from charitable remainder trust	9,672,000	9,579,000
Net realized losses on investments, permanently restricted	(1,046,000)	(1,481,000)
Net cash provided by financing activities	8,626,000	8,098,000
Net (decrease) in cash and cash equivalents	(1,585,000)	(13,084,000)
Cash and cash equivalents, beginning of year	20,268,000	33,352,000
Cash and cash equivalents, end of year	\$ 18,683,000	20,268,000
Supplemental disclosure of cash flow information:		
Cash paid during the year for excise taxes	\$ 781,000	385,000

See accompanying notes to financial statements.

## Notes to Financial Statements

December 31, 2005 and 2004

### (1) Organization and Summary of Significant Accounting Policies

#### (a) Organization

The Moody Foundation (the Foundation) is a private charitable foundation created in 1942 by W.L. Moody, Jr. and his wife, Libbie Rice Shearn Moody. The purpose of the Foundation is to promote and fund projects in the charitable areas that include but are not limited to humanities, arts, religion, education, health, science, community, and social services in the state of Texas.

#### (b) Financial Statement Presentation

The financial statements are presented using the accrual basis of accounting. Assets received from the estate of W.L. Moody, Jr. were recorded in the financial statements at market value on the date of receipt.

Net assets and revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Foundation and changes therein are classified and reported as follows:

- *Unrestricted net assets* - net assets that are not subject to donor-imposed restrictions.
- *Temporarily restricted net assets* - net assets that are subject to donor-imposed restrictions that require the passage of time or the occurrence of a specific event.
- *Permanently restricted net assets* - net assets required to be maintained in perpetuity with only the interest and dividend income to be used for the Foundation's activities due to donor-imposed restrictions.

#### (c) Cash and Cash Equivalents

Cash and cash equivalents include amounts on deposit at financial institutions and highly liquid overnight investments.

#### (d) Investments and Investment Income

The Foundation accounts for investments in equity securities with readily determinable fair values and all investments in debt securities at fair value, except for those accounted for under the equity method, with gains and losses included in the statement of activities.

The Foundation owns 23% and 34% of the outstanding voting stock of the American National Insurance Company (ANICO) and Gal-Tex Hotel Corporation (Gal-Tex), respectively. These investments are accounted for using the equity method of accounting. The Foundation annually evaluates its investments in ANICO and Gal-Tex to determine whether the investments are impaired and records adjustments if appropriate.

Realized and unrealized gains or losses on investments, is recorded based on donor imposed restrictions. Dividends and interest income are available for unrestricted use. The permanently restricted portion of equity in income of ANICO is recorded net of dividends that are available for unrestricted use.



**Notes to Financial Statements (*continued*)**December 31, 2005 and 2004

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**(e) Depreciable Assets**

Depreciable assets are recorded at cost and are depreciated using the straight-line method based on estimated useful lives ranging from three to eight years.

**(f) Grant Appropriations**

The Foundation recognizes unconditional grant appropriations as expenses at the time grants are committed to the recipient organizations. The Foundation recognizes conditional grant appropriations as expenses when the conditions on which they depend have been substantially met. Scholarship program grants are paid over a four-year period.

**(g) Income Taxes**

The Foundation qualifies as an exempt organization under Section 501(c)(3) of the Internal Revenue Code (the Code) and is exempt from federal income tax under Section 501(a) of the Code on income from related activities.

Deferred excise tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective excise tax bases. Deferred excise tax assets and liabilities are measured using enacted excise tax rates expected to apply in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred excise tax assets and liabilities of a change in excise tax rates is recognized in income in the period that includes the enactment date.

**(h) 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 reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of changes in net assets during the reporting period. Actual results could differ from those estimates.

**(2) ANICO**

The Foundation had a 23% interest in ANICO as of December 31, 2005 and 2004.

ANICO offers insurance coverages, including individual and group life, health and annuities, personal lines, property and casualty, and credit insurance. It also offers a variety of other financial products, including mutual funds, variable life insurance, and variable annuities. ANICO conducts business in the United States, the District of Columbia, Puerto Rico, and American Samoa. Through its subsidiary, American National Compañía de Seguros de Vida, ANICO is authorized to sell its products in Mexico.



**Notes to Financial Statements (continued)**

December 31, 2005 and 2004

Summarized combined financial information for ANICO is as follows as of and for the years ended December 31:

	2005	2004
Revenue	\$ 3,045,474,000	2,879,336,000
Net income	235,879,000	255,593,000
Total assets	\$ 17,516,881,000	16,570,827,000
Total liabilities	\$ 14,143,231,000	13,275,069,000
Stockholders' equity	3,373,650,000	3,295,758,000
Total liabilities and stockholders' equity	\$ 17,516,881,000	16,570,827,000

**(3) Fair Value of Financial Instruments**

Grants payable are obligations that are noninterest bearing and generally are paid within one year; therefore, their carrying value approximates fair value.

The Foundation estimates the fair value of publicly traded stocks, bonds, U.S. Treasury obligations, and other debt instruments based on quoted market prices. The estimated fair value of Gal-Tex common stock is \$9,534,000 at December 31, 2005.

Estimated fair values of marketable equity and debt securities and gross unrealized gains and losses at December 31, 2005 and 2004 are as follows:

December 31, 2005			
Basis	Gross unrealized		Estimated market value
	Gains	Losses	
Stocks with published quotations:			
ANICO (6,208,434 common shares)	\$ 488,558,000	237,767,000	726,325,000
Other	20,573,000	15,253,000	35,826,000
Bonds and other debt instruments	343,605,000	6,920,000	336,685,000
U.S. Treasury obligations	9,325,000	311,000	9,014,000
	\$ 862,061,000	253,020,000	7,231,000
			1,107,850,000

**Notes to Financial Statements (*continued*)**

December 31, 2005 and 2004

	December 31, 2004			
	Basis	Gross unrealized		Estimated market value
		Gains	Losses	
Stocks with published quotations:				
ANICO (6,208,434 common shares)	\$ 451,693,000	194,977,000	—	646,670,000
Other	17,435,000	16,062,000	—	33,497,000
Bonds and other debt instruments	304,645,000	8,676,000	—	313,321,000
U.S. Treasury obligations	9,325,000	—	70,000	9,255,000
	<u>\$ 783,098,000</u>	<u>219,715,000</u>	<u>70,000</u>	<u>1,002,743,000</u>

The cost and estimated market value of debt securities at December 31, 2005, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Cost	Estimated market value
Due in one year or less	\$ 1,530,000	1,501,000
Due after one year through five years	24,491,000	23,217,000
Due after five years through ten years	37,260,000	34,027,000
Due after ten years	183,310,000	182,542,000
	<u>246,591,000</u>	<u>241,287,000</u>
Mortgage-backed securities	97,014,000	95,398,000
	<u>\$ 343,605,000</u>	<u>336,685,000</u>

**(4) Interest in Libbie Shearn Moody Trust**

The Foundation has recorded its beneficial interest in the Libbie Shearn Moody Trust (the Trust) based on the estimated fair value of the assets contributed by the donor less the present value of the payments expected to be made to other life estates. The present value method for measuring the fair value of the contribution considers (a) the estimated return on the invested assets during the expected term of the Trust, (b) the contractual payment obligations under the Trust, (c) life expectancies of remaining life estate interests, and (d) an interest rate of 7.5%.

The Foundation receives distributions from the Trust applicable to its 75% remainderman interest in the income attributable to certain expired life estate interests in the Trust. One half of these distributions is permanently restricted, and the remaining funds are temporarily restricted until distributions are made. Upon expiration of all life estates, the Foundation will receive 75% of the assets of the Trust.

Approximately 93% of the assets of the Trust are 9,949,585 shares of ANICO common stock with a fair market value of \$1,164,002,000 and \$1,036,349,000 at December 31, 2005 and 2004, respectively.

**Notes to Financial Statements (continued)**

December 31, 2005 and 2004

**(5) Temporarily Restricted Net Assets**

Notes receivable at December 31, 2005 and 2004 are as follows:

	2005	2004
Unsecured 6% note receivable from Moody Gardens	\$ 11,700,000	11,700,000
Other	184,000	255,000
	<u>\$ 11,884,000</u>	<u>11,995,000</u>

The unsecured 6% note receivable from a grant recipient is due in semiannual principal payments of approximately \$433,000 through February 1, 2015. The grant recipient may defer payments of principal and interest if its net cash flow does not exceed the amount of the principal and interest payments. The principal payments due in 2005 and 2004 were deferred.

**(6) Temporarily Restricted Net Assets**

Temporarily restricted net assets were \$457,948,000 and \$400,700,000 as of December 31, 2005 and 2004, respectively, and consisted of estimated future distributions from the Trust. Assets are released from restriction when time restrictions are met.

**(7) Permanently Restricted Net Assets**

Permanently restricted net assets consist primarily of the beneficial interest in the Trust, investments to be invested in perpetuity, and paintings to be held in perpetuity. Changes in permanently restricted net assets includes the permanently restricted portion of equity in income of ANICO less dividends that are available for unrestricted use. Pursuant to donor restrictions, 338,522 of the 6,208,434 shares of ANICO common stock are permanently restricted.

**(8) Federal Excise Tax**

The Foundation is exempt from federal income taxes under Section 501(a) of the Internal Revenue Code of 1986, as amended, as an organization described in Section 501(c)(3). Accordingly, the Foundation is not subject to federal income tax, except to the extent that it has unrelated business taxable income. The Foundation did not have unrelated business income in 2005 or 2004. However, the Foundation is classified as a private foundation under Section 509(a) and, as such, is subject to a federal excise tax of 2% on net investment income, unless certain conditions are met, in which case the federal excise tax is reduced to 1%. In 2005 and 2004, the Foundation was subject to an excise tax on net investment income of 1% and 2%, respectively. Deferred excise taxes are provided for on the unrealized increase in the fair value of the Foundation's investment assets at a 2% rate. The following information is for the year ended December 31:

	2005	2004
Current expense	\$ 875,000	453,000
Deferred expense (benefit)	440,000	875,000
Total excise tax expense	<u>\$ 1,315,000</u>	<u>1,328,000</u>



**Notes to Financial Statements (continued)**

December 31, 2005 and 2004

The Foundation is also required to make certain minimum qualifying distributions of its assets in accordance with formulas provided by federal law. In addition to satisfying its minimum distribution requirements, the Foundation had an excess distribution carryover of \$72,407,000 at December 31, 2004 and it is expected that the foundation will utilize approximately \$7,982,000 of the excess distribution carryover in 2005.

**(9) Related-Party Transactions**

Members of the board of trustees and certain employees of the Foundation hold various positions with organizations that provide services to or receive grants from the Foundation. In addition, the Foundation's investment portfolio includes investments in other entities in which the Trust and other related parties have common investments. The Foundation has a number of recurring transactions with such entities. However management believes such transactions are conducted on an arms-length basis.

During 2005, Moody Gardens, Inc. and Transitional Learning Community were awarded grant appropriations of \$810,000 and \$38,110,000, respectively.

The Moody National Bank of Galveston (the Bank) leases office space to the Foundation and provides the Foundation with general banking services, general bookkeeping services, and physical custody of records and marketable securities. Total payments to the Bank were approximately \$364,000 and \$342,000 during the years ended December 31, 2005 and 2004, respectively. The Bank also serves as trustee for the Trust.

Insurance premiums paid to ANICO under a medical stop-loss insurance plan were approximately \$369,000 and \$196,000 for the years ended December 31, 2005 and 2004, respectively.

ANICO administers the Foundation's defined benefit pension plan. Fees paid to ANICO for administration of the plan were approximately \$2,000 during each of the years ended December 31, 2005 and 2004.

**(10) Pension Plan**

The Foundation has a defined benefit pension plan covering substantially all full-time employees with one or more years of service with benefits based on years of service and average compensation. The Foundation's general funding policy is to contribute annually at least the minimum required contribution. Contributions are intended to provide for benefits attributed to service rendered to date and for those benefits expected to be earned in the future.

The Plan's funded status and related amounts recognized in the statements of financial position at December 31, 2005 and 2004 are as follows:

	2005	2004
Projected benefit obligations for service rendered to date	\$ (3,300,000)	(2,985,000)
Plan assets at fair value, primarily U.S. listed stocks and bonds	2,805,000	2,563,000
Plan assets less than projected benefit obligation	\$ (495,000)	(422,000)
Accrued benefit cost recognized in the statements of financial position and statements of activities	\$ —	—

**Notes to Financial Statements (continued)**

December 31, 2005 and 2004

The accumulated benefit obligation exceeded the fair value of plan assets by \$291,000 and \$48,000 at December 31, 2003.

Components of net pension cost for the years ended December 31, 2005 and 2004 are as follows:

	2005	2004
Service costs:		
Benefits earned during the year	\$ 78,000	85,000
Interest cost on projected benefit obligation	164,000	119,000
Actual return on plan assets	(145,000)	(123,000)
Net amortization and deferral	24,000	25,000
Net amortization and deferral	30,000	—
Net periodic benefit cost	\$ 151,000	106,000
Contributions made during the year	\$ 161,000	343,000
Benefits paid during the year	—	—

In 2005 and 2004, the weighted average discount rate and rate of increase in future compensation levels used in determining the actuarial present value of the projected benefit obligation were 5.5% and 5.5%, respectively. The expected long-term rate of return on plan assets was 5.5% and 5.5% in 2005 and 2004, respectively.

The following table sets forth the plan's funded status as of the most recent actuarial valuation dates of December 31, 2005 and 2004:

	2005	2004
Accumulated benefit obligation	\$ (3,097,000)	(2,815,000)
Projected benefit obligation	(3,300,000)	(2,985,000)
Change in plan assets:		
Fair value of plan assets at beginning of year	2,563,000	2,062,000
Actual return on plan assets	81,000	158,000
Employer contributions	161,000	343,000
Benefits paid	—	—
Fair value of plan assets at end of year	\$ 2,805,000	2,563,000
Reconciliation of funded status:		
Projected benefit obligation in excess of plan assets	(495,000)	(422,000)
Unrecognized prior service costs	54,000	79,000
Unrecognized net loss not reflected in the fair value of assets	788,000	680,000
Unrecognized net transition obligation at December 31, 1990 being recognized over 25 years started January 1, 1990	—	—
Accrued pension cost at December 31, 2004 and 2003	347,000	337,000

**Notes to Financial Statements (*continued*)**

December 31, 2005 and 2004

The investment strategy consist of long-term, risk controlled approach using diversifie investment options with minimal exposure to volatile investment options like derivatives. The target asset allocation for the Plan is as follows for 2004:

	2005	2004
Equity securities	36%	36%
Debt securities	30	33
Real estate	19	13
Other	15	18
Total	100%	100%

The relationship between assets and liabilities uses a diversified allocation of equity, debt, and real estate exposures that are customized to the plan's cash flow benefit needs.

Based on current data and assumptions, the following benefit payments, which reflect expected future service, as appropriate, are expected to be paid over the next 10 fiscal years:

	Benefits Paid
Year ending:	
2006	\$ —
2007	722,000
2008	—
2009	—
2010	—
2011-2015	221,000

**(11) Contingencies**

The Foundation is currently undergoing an audit by the IRS for calendar years 1998 through 2001. The IRS has completed its information gathering but has not issued its final report. Management believes that any adjustments resulting from the audit will not have a material adverse effect on the Foundation's financial position or results of operations.

From time to time, the Foundation has pending and threatened litigation and claims incurred in the ordinary course of business. Management believes that the probable resolution of such contingencies will not exceed insurance coverages and will not materially affect the financial position of the Foundation or the results of its operations.