

**STATE OF WASHINGTON  
OFFICE OF THE INSURANCE  
COMMISSIONER**



**FINANCIAL EXAMINATION  
of the Charitable Gift Annuity Business**

of

**Seattle Pacific University  
Seattle, Washington**

**DECEMBER 31, 2005**

Order No. G 07-6  
Seattle Pacific University  
Exhibit A

**SALUTATION**

Seattle, Washington  
January 30, 2007

The Honorable Mike Kreidler, Commissioner  
Washington State Office of the Insurance Commissioner (OIC)  
Insurance Building-Capitol Campus  
302-14<sup>th</sup> Avenue SW  
Olympia, WA 98504

Dear Commissioner Kreidler:

In accordance with your instructions and in compliance with the statutory requirements of Chapter 48.38 RCW, Charitable Gift Annuity Business (CGAB), an examination was made of the corporate affairs and financial records of the CGAB of

**Seattle Pacific University**

of

Seattle, Washington

hereinafter referred to as "SPU" at its office, 3307 Third Avenue West, Seattle, WA 98119.

This report of examination is respectfully submitted showing the condition of the CGAB of SPU as of December 31, 2005.

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify I have read the attached Report of the Financial Examination of the Charitable Gift Annuity Business of Seattle Pacific University of Seattle, Washington. This report shows the financial condition of the Charitable Gift Annuity Business and related matters of Seattle Pacific University as of December 31, 2005.



Patrick H. McNaughton  
Chief Examiner

1-30-2007

Date

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## SCOPE OF THE EXAMINATION

This examination covers the period January 1, 2001 through December 31, 2005. The 2005 Annual Report reflected the balance sheet and statement of revenue and expenses of SPU as of June 30, 2005. The OIC granted SPU permission to present its CGAB Annual Report as of its fiscal year ended June 30, 2005. The examination of the 2005 Annual Report, therefore, covers the period ending June 30, 2005 for the balance sheet and statement of revenue and expenses sections, and the period ending December 31, 2005 for the general interrogatories and charitable gift annuities reserve fund. The financial statements are presented on a consolidated basis for both SPU and Seattle Pacific Foundation (the Foundation). However, the scope of the examination focused only on the transactions and operations of the CGAB. SPU's records, along with various aspects of its operating procedures and financial reports, were reviewed and tested during the course of this examination as necessary to substantiate the CGAB reporting. The results of the examination are commented upon in the various sections of this report. In addition, SPU's certified public accountant's (CPA's) reports were reviewed and utilized, where possible, to facilitate efficiency in the examination.

The examination was conducted in accordance with the statutory requirements contained in the Revised Code of Washington (RCW) and the guidelines recommended by the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook (FCEH). The examination was conducted at the Seattle office of SPU by examiners from the state of Washington.

## INSTRUCTIONS

The examiners reviewed SPU's CGAB Annual Reports as part of the statutory examination. This review was performed to determine if SPU completed its Annual Reports in accordance with the Annual Report Instructions published by the OIC and to verify that SPU's accounts and records were prepared and maintained in accordance with Chapter 48.38 RCW.

The following summarizes the exceptions noted while performing this review.

### **1. Assets of the Separate Reserve Fund**

SPU was not in compliance with the requirements stipulated in RCW 48.38.020(2)(a) because the assets of the annuity reserve fund were not held legally and physically segregated from the other assets of SPU and the Foundation.

The annuity funds are invested on a unitized basis in the Foundation's unitized endowment pool and liquidity pool. As of December 31, 2005, the total fair value of the charitable gift annuity assets was \$4,463,876. The annuity assets were composed of: \$679,332 in the Foundation's unitized endowment pool, \$102,776 in the Foundation's unitized liquidity pool, and a \$3,750,000 Limited Liability Corporation (LLC) interest

which owns property pending a March 2006 sale. Also, the annuity assets account had a negative cash balance of \$68,232.

The Foundation's endowment pool is allocated among several investment classes, including marketable securities, cash and real estate. The liquidity pool is allocated between cash and intermediate-term fixed income securities. The Foundation also manages a broadly diversified unitized trust pool in which the Foundation's portfolio of charitable trusts is invested. At month end, the assets of all pools are revalued and new unit values are established. Also, changes in pool ownership are transacted by the sale of existing pool units or the purchase of additional pool units as in a mutual fund investment. Income is distributed and allocated per unit to participating funds on at least a quarterly basis.

RCW 48.38.020(2) states that: "The assets of the separate reserve fund: (a) Shall be held legally and physically segregated from the other assets of the certificate of exemption holder."

**SPU is instructed to develop a system for legally and physically segregating its charitable gift annuity business to ensure its compliance with RCW 48.38.020(2)(a).**

## **COMMENTS AND RECOMMENDATIONS**

### **Conflict of Interest**

SPU's current Conflict of Interest Policy requires disclosure of potential or actual conflict of interest by key employees. However, it does not include the definition of such conflicts provided in SPU's bylaws nor does it provide for annual reporting and review of compliance by all trustees, officers and key employees. Such annual reporting and review is recommended to ensure compliance with SPU's stated standards.

**It is recommended that a formal conflict of interest policy and annual conflict of interest questionnaire be developed for key employees in addition to the questionnaire currently utilized with the BOT. The policy should include a provision for annual review by the BOT.**

## **ORGANIZATION PROFILE**

**History:** SPU is a private, nonprofit institution of higher education. It was established in 1891 under the name Seattle Seminary and was renamed Seattle Pacific College in 1915. Full accreditation of the College's four-year liberal arts program was awarded in 1936 by the Northwest Association of Schools and Colleges. On June 5, 1977, the College officially became Seattle Pacific University. Today, SPU offers 55 undergraduate majors, 12 master degree programs, and three doctoral programs.

**Territory and Plan of Operation:** On July 30, 1980, the OIC granted SPU a Certificate of Exemption to conduct a CGAB in the state of Washington. There were fifty-three in-force annuity contracts as of December 31, 2005: thirty-four were issued to residents of the state of Washington, fourteen were issued to a resident of the state of Indiana, one was issued to a resident of the state of Montana, and four were issued to a resident of the state of Kansas.

**Total Net Assets:** SPU's total net assets as of June 30, 2005 were \$90,545,000. This amount included an unrestricted net asset of \$56,855,000. The minimum unrestricted net asset requirement pursuant to RCW 48.38.010(6) was satisfied as of June 30, 2005.

**Growth:** The development of SPU for the past five years is reflected in the following schedules. All information was compiled from SPU's financial statements as of fiscal years ending June 30.

**Schedule 1 – Statement of Financial Position**

(In thousands)

<b>Fiscal Year</b>	<b>Assets</b>	<b>Liabilities</b>	<b>Total Net Assets</b>	<b>Total Net Assets Allocated Into:</b>		
				<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>
2005	\$220,731	\$130,186	\$90,545	\$56,855	\$9,212	\$24,478
2004	215,864	130,443	85,421	55,390	13,904	16,127
2003	220,796	140,326	80,470	51,365	13,700	15,405
2002	220,430	134,445	85,985	58,618	12,416	14,951
2001	227,410	138,063	89,347	64,352	10,583	14,412

**Schedule 2 – Statement of Activities and Changes in Net Assets**

(In thousands)

	<b>2005</b>	<b>2004</b>	<b>*2003</b>	<b>2002</b>	<b>2001</b>
Revenues and gains	\$77,040	\$73,979	\$60,868	\$56,530	\$46,455
Expenses	71,916	69,028	65,212	59,892	55,309
Increase (decrease) in net assets	5,124	4,951	(4,344)	(3,362)	(8,854)
Net assets at beginning of period	85,421	80,470	84,814	89,347	98,201
<b>Net assets at end of year</b>	<b>\$90,545</b>	<b>\$85,421</b>	<b>\$80,470</b>	<b>\$85,985</b>	<b>\$89,347</b>

Number of gift annuity contracts at end of year	53	60	59	60	59
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\* Certain reclassifications have been made to the 2002 consolidated financial statements to conform to the classifications used in 2003.

**AFFILIATED ORGANIZATIONS**

SPU has a controlling financial interest in the Foundation through direct ownership of the majority voting interest in the Foundation. SPU's Board of Trustees appoints and has delegated to the Foundation directors the responsibility for the overall investment management of all SPU endowment funds, annuity funds and charitable trust of which SPU or the Foundation are trustee. The financial statements of SPU and the Foundation

have been presented on a consolidated basis and transactions between these entities are eliminated upon consolidation.

### MANAGEMENT AND CONTROL

**Management:** According to the restated Articles of Incorporation and Bylaws (as amended to and including May 20, 2005), the responsibility for the governance and control of SPU rests exclusively with the Board of Trustees (BOT). The BOT consists of not less than twelve or more than fifteen persons, all of whom are elected by the BOT.

**Board of Trustees:** The BOT as of fiscal year 2005-2006 are:

Mr. A. Gary Ames	Mr. David J. McIntyre, Jr.
Rev. John P. Clark	Mr. Victor C. Moses
Rev. Harvey Drake, Jr.	Mr. Barry L. Rowan
Dr. Philip W. Eaton	Mr. Frederick J. Stabbert
Mr. Roger H. Eigsti	Mr. Bruce A. Walker
Mr. David R. Goodnight	Mr. Dennis M. Weibling
Mr. Edward B. Kibble	Rev. Matthew H. Whitehead
Dr. Donald A. MacPhee	

**Officers:** The Corporate Bylaws of SPU state that the officers of the corporation are the president, chair, treasurer, and secretary of the BOT. In addition to its officers, SPU's executive administrators include the president, who is elected by the BOT, and vice presidents, who are appointed by the president, with the approval of the BOT. The president is a member of the BOT and the chief executive officer (CEO) of SPU. The officers as of Fiscal Year 2005-2006 are:

Philip W. Eaton, Ph.D., President and CEO  
Roger Eigsti, Chair of Trustees  
Frederick Stabbert, Treasurer  
Matthew Whitehead, Secretary  
Les L. Steele, Ph.D., Vice President for Academic Affairs  
Marjorie R. Johnson, M.A., Vice President for Administration and University Relations  
Donald W. Mortenson, M.B.A., CPA (inactive), Vice President for Business and Planning  
Robert D. McIntosh, Vice President for University Advancement

**Tax Status:** SPU is a Washington nonprofit institution and is exempt from income tax under Section 501(c)(3) of the Internal Revenue Code.

**Conflict of Interest:** SPU has a conflict of interest policy which is a part of its Standards of Conduct. However, the policy does not provide for implementation of all the requirements and procedures stipulated in its Bylaws. (See COMMENTS AND RECOMMENDATIONS)

## **CORPORATE RECORDS**

The BOT meets at least four times a year to discuss business which is pertinent to SPU. Minutes of the meetings of the trustees documented the approval of SPU's transactions and events. No exceptions were noted.

## **STATEMENT OF ACTUARIAL OPINION**

A consulting actuary with Milliman, Inc., reviewed the adequacy of the annuity reserves and issued a Statement of Actuarial Opinion (SAO) which stated that he is a member of the American Academy of Actuaries and meets its qualification standards. His SAO states that SPU's annuity contract reserves as computed under RCW 48.38.020(3)(a) and (b) of the Washington Insurance Code should be \$3,253,764. This amount, plus the 10% surplus required by RCW 48.38.020(3)(c), was properly reported as CGAB liabilities in the SPU financial statements.

## **ANNUITY ASSETS CUSTODIAL FUNCTION**

The separate reserve fund assets were not held legally and physically segregated from the other assets of SPU. (See INSTRUCTION No. 1) Total annuity assets, as shown in the Annual Report, were \$4,463,875 as of December 31, 2005.

## **SUBSEQUENT EVENTS**

No material events impacted SPU between the examination date and the last day of our field work.

## **ACCOUNTING RECORDS AND PROCEDURES**

The records and source documentation supported the data and amounts presented in the annual reports and financial statements.

## FINANCIAL STATEMENTS

The following financial information summarizes the consolidated financial statements of SPU and the Foundation as of June 30, 2005:

### Balance Sheet

	<b>Balance Per Annual Report</b>	<b>Adj.</b>	<b>Examination Adjustment</b>	<b>Adjusted Balance</b>
<b><u>ASSETS</u></b>				
Cash and cash equivalents	\$19,463,000			\$19,463,000
Investments	59,602,125			59,602,125
CGA assets*	4,463,875			4,463,875
Other assets	137,202,000			137,202,000
<b>Total Assets</b>	<b><u>\$220,731,000</u></b>		<b><u>\$0</u></b>	<b><u>\$220,731,000</u></b>
<b><u>LIABILITIES</u></b>				
Trust obligations	\$4,985,860			\$4,985,860
CGA reserves*	3,579,140			3,579,140
Other liabilities	121,621,000			121,621,000
<b>Total Liabilities</b>	<b><u>130,186,000</u></b>		<b><u>0</u></b>	<b><u>130,186,000</u></b>
<b><u>NET ASSETS</u></b>				
Unrestricted	56,855,000			56,855,000
Temporarily restricted	9,212,000			9,212,000
Permanently restricted	24,478,000			24,478,000
<b>Total Net Assets</b>	<b><u>90,545,000</u></b>		<b><u>0</u></b>	<b><u>90,545,000</u></b>
<b>Total Liabilities and Net Assets</b>	<b><u>\$220,731,000</u></b>		<b><u>\$0</u></b>	<b><u>\$220,731,000</u></b>

\*The distribution of the annuity assets and statutory reserves are based on the Annual Report and Statement of Actuarial Opinion as of December 31, 2005.

### Statement of Activities and Changes in Net Assets

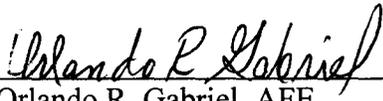
	<b>Balance Per Annual Report</b>	<b>Adj.</b>	<b>Examination Adjustments</b>	<b>Adjusted Balance</b>
Total revenues	\$77,040,000			\$77,040,000
Total expenses	71,916,000			71,916,000
Increase (decrease) in net assets	5,124,000			5,124,000
Net assets at beginning of year	85,421,000			85,421,000
Changes in net assets per examination				
<b>Net assets at end of year</b>	<b><u>\$90,545,000</u></b>		<b><u>\$0</u></b>	<b><u>\$90,545,000</u></b>

## ACKNOWLEDGMENT

Acknowledgment is hereby made of the cooperation extended to the examiners by the officers and employees of SPU and the Foundation during the course of this examination.

In addition to the undersigned, Michael V. Jordan, CPA, CFE, MHP, Assistant Chief Examiner; John Gaynard, CPA, CFE, FLMI, Life and Disability Field Supervising Examiner; and Richard Bologna, Certified Fraud Examiner, and Insurance Examiner from the Washington State Office of the Insurance Commissioner, participated in the examination and the preparation of this report.

Respectfully submitted,



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Orlando R. Gabriel, AFE  
Examiner-in-Charge  
State of Washington

**AFFIDAVIT**

STATE OF WASHINGTON        }  
  } ss  
COUNTY OF KING            }

Orlando R. Gabriel, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

He attests that the examination of SPU's CGAB was performed in a manner consistent with the standards and procedures required or prescribed by the Washington State Office of the Insurance Commissioner and the National Association of Insurance Commissioners (NAIC).

*Orlando R. Gabriel*  
Orlando R. Gabriel, AFE  
Examiner-in-Charge  
State of Washington

Subscribed and sworn to before me on this 30<sup>th</sup> day of January, 2007.

*Colleen Jansen*  
Notary Public in and for the  
State of Washington,  
Residing at Seattle.

