

STATE OF WASHINGTON  
OFFICE OF THE INSURANCE COMMISSIONER



FINANCIAL EXAMINATION  
OF THE CHARITABLE GIFT ANNUITY BUSINESS  
OF  
SEATTLE CHILDREN'S HEALTHCARE SYSTEM  
SEATTLE, WASHINGTON

September 30, 2011

Order 12-167  
Seattle Children's Healthcare System  
Exhibit A

**SALUTATION**

Seattle, Washington

June 4, 2012

The Honorable Mike Kreidler, Commissioner  
Washington State Office of the Insurance Commissioner (OIC)  
Insurance Building-Capitol Campus  
302 Sid Snyder Avenue SW, Suite 200  
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, an examination was made of the corporate matters and financial records pertaining to the charitable gift annuity (CGA) business of

**Seattle Children's Healthcare System**

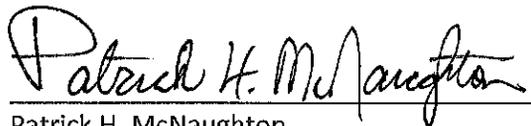
of

Seattle, Washington

hereinafter referred to as "SCHS" at its office, 4300 Roosevelt Way NE, Seattle, Washington 98105. This report of examination is respectfully submitted showing the financial condition and related corporate matters of the CGA business of SCHS as of September 30, 2011.

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify I have read the attached Report of the Financial Examination of the Charitable Gift Annuity Business of the Seattle Children's Healthcare System of Seattle, Washington. This report shows the financial condition of the CGA business and related corporate matters of the Seattle Children's Healthcare System as of September 30, 2011.



Patrick H. McNaughton  
Chief Examiner

6-4-2012

Date

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## **SCOPE OF THE EXAMINATION**

The examination covers the period October 1, 2006 through September 30, 2011. The scope of our examination focused only on the transactions and operations of the CGA business. SCHS'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 CGA business reporting. The results of the examination are commented upon in the various sections of this report. In addition, SCHS's certified public accountant's (CPA's) audit of the September 30, 2011 combined financial statements was reviewed and utilized 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 SCHS by examiners from the state of Washington.

The examiners reviewed SCHS's CGA Annual Reports as part of the statutory examination. This review was performed to determine if SCHS completed the Annual Reports in accordance with the Annual Report Instructions published by the OIC and to verify that SCHS's accounts and records were prepared and maintained in accordance with RCW 48.38.010(10)(a).

## **INSTRUCTIONS**

NONE

## **COMMENTS AND RECOMMENDATIONS**

NONE

## **ORGANIZATION PROFILE**

### **History**

SCHS, formerly known as Children's Health Care System, operates for charitable, scientific and educational purposes. It provides health care services to infants, children and adolescents, and delivers those services through research, education, advocacy, and contributions to or for the benefit of tax-exempt organizations.

### **Territory and Plan of Operation**

SCHS was granted a Certificate of Exemption No. 122 to conduct a CGA business in the state of Washington by the OIC on September 10, 1998. SCHS had 93 in-force annuity contracts as of September 30, 2011.

### Total Net Assets

SCHS's total net assets as of September 30, 2011 were \$509.9 million. This amount included unrestricted net assets of \$420.4 million. The minimum unrestricted net assets requirement was satisfied pursuant to RCW 48.38.010(6).

### Growth

The growth of SCHS for the past five years is reflected in the following schedules. The audited financial statements of SCHS and its affiliates have been presented on a consolidated basis. The schedules below, however, show only the financial information of SCHS as of fiscal years ending September 30, in accordance with the OIC Annual Report Instructions.

### Schedule 1 – Statement of Financial Position (In Thousands)

Year	Assets	Liabilities	Total Net Assets	Total Net Assets Allocated Into:		
				Unrestricted	Temporarily Restricted	Permanently Restricted
*2011	\$508,086	(\$1,885)	\$509,971	\$420,496	\$18,053	\$71,422
2010	510,630	12,279	498,351	405,447	20,668	72,236
2009	469,810	4,430	465,380	377,653	17,312	70,415
2008	518,925	31,837	487,088	394,261	12,285	80,542
2007	563,984	27,497	536,487	424,083	29,025	83,379

### Schedule 2 – Statement of Activities and Changes in Net Assets (In Thousands)

	<u>*2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Total revenues	\$19,367	\$39,695	\$20,904	\$5,332	\$117,855
Total expenses	7,531	7,133	8,806	3,183	10,119
Increase (decrease) in net assets	11,836	32,562	12,098	2,149	107,736
Other changes in net assets	(216)	410	(33,807)	(51,548)	(30,933)
Net assets at beginning of year	498,351	465,379	487,088	536,487	459,684
<b>Net assets at end of year</b>	<b>\$509,971</b>	<b>\$498,351</b>	<b>\$465,379</b>	<b>\$487,088</b>	<b>\$536,487</b>
Number of gift annuity contracts at end of year	93	95	92	96	93

\*The 2011 balances included examination adjustments. (See Note 1 to the Financial Statements.)

### AFFILIATED ORGANIZATIONS

SCHS is the parent organization to the following corporations: Seattle Children's Hospital, Seattle Children's Hospital Foundation, Seattle Children's Hospital Guild Association, Seattle Children's Retail, Children's Physicians, Seattle Children's Research Holdings LLC, and Seattle Children's Research Investors LLC.

## MANAGEMENT AND CONTROL

### **Management**

SCHS is governed by a Board of Trustees (BOT), consisting of between 20 and 30 voting trustees and three non-voting trustees. The BOT selects and employs the Chief Executive Officer (CEO). The CEO is responsible for the overall management of SCHS's operations and for implementing the BOT policies.

### **Board of Trustees**

The following individuals were trustee as of September 30, 2011:

#### Voting Trustees

Dean Allen	James Ladd
Elizabeth Armintrout	Sandra Madrid
Robert Bakemeier	Susan Mask
Joel Benoliel	Teresa Moore
Jane Blair	Jeffrey Nitta
Ross Bogue	Gloria Northcroft
Patricia Char	Laurie Oki
Michael Delman	Nancy Senseney
Mary Ann Flynn	Pete Shimer
Robert Flowers	Michele Smith
Judith Holder	Charles Stevens
Cynthia Huffman	

#### Non-Voting Trustees

David Fisher, M.D.  
Thomas Hansen, M.D.  
Robert Roskin, M.D.

### **Officers**

The following individuals were officers as of September 30, 2011:

Robert Flowers, Chairman  
James Ladd, Chairman  
Thomas Hansen, M.D., Chief Executive Officer  
Michael Delman, Treasurer  
Cynthia Huffman, Secretary

### **Tax Status**

SCHS is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code.

### **Conflict of Interest**

The BOT adopted and implemented a written conflict of interest policy that includes guidelines for the resolution of any existing or apparent conflict of interest. The Audit and Corporate Responsibility

Committee has general responsibility for oversight of the conflict of interest disclosure process. Based on our review of the submitted disclosure statements, no exceptions were noted.

#### **ORGANIZATION RECORDS**

The BOT met nine times in 2011 to discuss any pertinent business to SCHS. BOT meeting minutes documented the approval of SCHS's transactions and events.

#### **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. The SAO indicated that SCHS's annuity contract reserves as computed under RCW 48.38.020(3)(a) and (b) should be \$2,438,259 for 93 in-force annuity contracts as of September 30, 2011. This amount was properly reported in SCHS's 2011 Annual Report.

#### **ANNUITY ASSETS CUSTODIAL FUNCTION**

The separate reserve fund assets were held legally and physically segregated from the other assets of SCHS as required by RCW 48.38.020(2)(a). The market values of the annuity investments as of September 30, 2011 were \$2,972,115 and consisted of money market and mutual funds. The annuity investments were properly reported in the financial statements at market value.

#### **SUBSEQUENT EVENTS**

There were no additional material events which impacted SCHS between the examination date and the last day of our field work.

#### **FOLLOW UP ON PREVIOUS EXAMINATION FINDINGS**

All previous report instructions and comments have been addressed and corrected.

#### **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 statements show the unconsolidated financial condition of the Seattle Children's Healthcare System as of September 30, 2011:

Statement of Financial Position

Statement of Activities and Changes in Net Assets

**Seattle Children's Healthcare System**  
**Statement of Financial Position**  
**September 30, 2011**  
(In Thousands)

	<u>Balance Per Annual Report</u>	<u>Examination Adjustments</u>	<u>Balance Per Examination</u>	<u>Notes</u>
<b>Assets</b>				
Investments, assets whose use is limited	\$360,663	(\$2,850)	\$357,813	1
CGA investments	2,972		2,972	
Other assets	147,301		147,301	
<b>Total Assets</b>	<b><u>\$510,936</u></b>	<b><u>(\$2,850)</u></b>	<b><u>\$508,086</u></b>	
<b>Liabilities and Net Assets</b>				
Current liabilities	\$8,539	\$0	\$8,539	
CGA liabilities	2,011		2,011	
Payable to SCHS	(21,021)		(21,021)	
Other liabilities	8,586		8,586	
<b>Total Liabilities</b>	<b><u>(1,885)</u></b>	<b><u>0</u></b>	<b><u>(1,885)</u></b>	
<b>Net Assets</b>				
Unrestricted	422,341	(1,845)	420,496	1
Temporarily restricted	19,058	(1,005)	18,053	1
Permanently restricted	71,422		71,422	
<b>Total Net Assets</b>	<b><u>512,821</u></b>	<b><u>(2,850)</u></b>	<b><u>509,971</u></b>	
<b>Total Liabilities and Net Assets</b>	<b><u>\$510,936</u></b>	<b><u>(\$2,850)</u></b>	<b><u>\$508,086</u></b>	

**Seattle Children's Healthcare System**  
**Statement of Activities and Changes in Net Assets**  
**For the Year Ended September 30, 2011**  
(In Thousands)

	<u>Balance Per Annual Report</u>	<u>Examination Adjustments</u>	<u>Balance Per Examination</u>	<u>Notes</u>
Total revenues	\$21,233	(\$1,866)	\$19,367	1
Total expenses	7,000	531	7,531	1
Increase (decrease) in net assets	14,233	(2,397)	11,836	
Other changes in net assets	237	(453)	(216)	1
Net assets at beginning of year	498,351		498,351	
<b>Net assets at end of year</b>	<b><u>\$512,821</u></b>	<b><u>(\$2,850)</u></b>	<b><u>\$509,971</u></b>	

**NOTES TO THE FINANCIAL STATEMENTS**

Examination adjustments to SCHS's Annual Report are as follows:

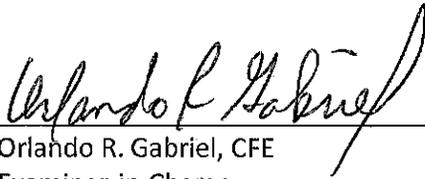
1. To reflect generally accepted accounting principles adjustments from the unaudited estimated financial information that was permitted to be reported to the OIC prior to completion of the audited financial statements. The adjustments were made in the audited financial statements by SCHS after the Annual Report was submitted to the OIC.

**ACKNOWLEDGMENT**

Acknowledgment is hereby made of the cooperation extended to the examiners by the officers and employees of the Seattle Children's Healthcare System during the course of this examination.

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

Respectfully submitted,

A handwritten signature in black ink, reading "Orlando R. Gabriel", written over a horizontal line.

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

