The Moody Foundation

Financial Statements
and Independent Auditors' Report
for the years ended December 31, 2017 and 2016

Independent Auditors' Report

To the Board of Trustees of
The Moody Foundation:

We have audited the accompanying financial statements of The Moody Foundation (the Foundation), which comprise the statements of financial position as of December 31, 2017 and 2016 and the related statements of activities and of cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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 our audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis for Qualified Opinion

As discussed in Note 2 of the financial statements, in 2016 the Foundation changed its method of accounting for certain investments from the equity method to fair value and restated previously reported net assets. In our opinion, based upon the fact that the Foundation's ownership of these entities exceeds 20%, accounting principles generally accepted in the United States of America require that these investments be reported using the equity method of accounting. The impact on the financial statements that results from this departure from generally accepted accounting principles is not reasonably determinable.

Qualified Opinion

In our opinion, except for the matter described in the Basis for Qualified Opinion paragraph, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Foundation as of December 31, 2017 and 2016 and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Blazek & Vetterling

July 11, 2018

The Moody Foundation

Statements of Financial Position as of December 31, 2017 and 2016 *(in thousands)*

	2017	2016
ASSETS		
Cash equivalents *(Note 3)*	$ 13,346	$ 16,738
Investment income receivable	2,703	2,627
Federal excise tax receivable *(Note 6)*	361	614
Other assets	4,629	1,103
Investments, at fair value *(Note 3)*	1,674,004	1,571,356
Other investments:		
Program notes receivable *(Note 5)*	12,333	12,388
Real estate	1,500	1,500
Interest in charitable remainder trust *(Notes 3 and 7)*	1,145,062	1,190,212
TOTAL ASSETS	$ 2,853,938	$ 2,796,538
LIABILITIES AND NET ASSETS		
Liabilities:		
Grants payable *(Note 8)*	$ 59,287	$ 47,580
Deferred federal excise tax *(Note 6)*	11,047	10,458
Total liabilities	70,334	58,038
Net assets:		
Unrestricted	1,237,131	1,197,845
Temporarily restricted *(Note 9)*	572,532	595,107
Permanently restricted *(Note 9)*	973,941	945,548
Total net assets	2,783,604	2,738,500
TOTAL LIABILITIES AND NET ASSETS	$ 2,853,938	$ 2,796,538

See accompanying notes to financial statements.

The Moody Foundation

Statement of Activities for the year ended December 31, 2017 *(in thousands)*

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
REVENUE:				
Change in interest in charitable remainder trust *(Note 7)*		$ (5,586)	$ (5,586)	$ (11,172)
Net realized and unrealized gain on investments in marketable securities	$ 52,118		33,979	86,097
Interest and dividends	41,706	1,110		42,816
Oil and gas royalties	19,563			19,563
Investment management expenses	(2,347)			(2,347)
Net investment income	111,040	(4,476)	28,393	134,957
Grant reversion	4,735			4,735
Total revenue	115,775	(4,476)	28,393	139,692
Net assets released from restrictions:				
Expenditures for programs	18,099	(18,099)		
Total	133,874	(22,575)	28,393	139,692
EXPENSES:				
Program expenses:				
Grants awarded	89,354			89,354
Program management	2,085			2,085
Total program expenses	91,439			91,439
Management and general	1,637			1,637
Federal excise tax expense *(Note 6)*	1,512			1,512
Total expenses	94,588			94,588
CHANGES IN NET ASSETS	39,286	(22,575)	28,393	45,104
Net assets, beginning of year	1,197,845	595,107	945,548	2,738,500
Net assets, end of year	$ 1,237,131	$ 572,532	$ 973,941	$ 2,783,604

See accompanying notes to financial statements.

The Moody Foundation

Statement of Activities for the year ended December 31, 2016 *(in thousands)*

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
REVENUE:				
Change in interest in charitable remainder trust *(Note 7)*		$ 148,866	$ 148,866	$ 297,732
Net realized and unrealized gain on investments in marketable securities	$ 142,725		25,455	168,180
Interest and dividends	37,024	1,105		38,129
Oil and gas royalties	19,470			19,470
Investment management expenses	(2,458)			(2,458)
Net investment income	196,761	149,971	174,321	521,053
Other income	865			865
Federal excise tax benefit *(Note 6)*	1,784			1,784
Total revenue	199,410	149,971	174,321	523,702
Net assets released from restrictions:				
Expenditures for programs	18,397	(18,397)		
Total	217,807	131,574	174,321	523,702
EXPENSES:				
Program expenses:				
Grants awarded	50,719			50,719
Program management	1,769			1,769
Total program expenses	52,488			52,488
Management and general	1,779			1,779
Total expenses	54,267			54,267
CHANGES IN NET ASSETS	163,540	131,574	174,321	469,435
Net assets, beginning of year, as adjusted *(Note 2)*	1,034,305	463,533	771,227	2,269,065
Net assets, end of year	$ 1,197,845	$ 595,107	$ 945,548	$ 2,738,500

See accompanying notes to financial statements.

The Moody Foundation

Statements of Cash Flows for the years ended December 31, 2017 and 2016 *(in thousands)*

	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	$ 45,104	$ 469,435
Adjustments to reconcile changes in net assets to net cash used by operating activities:		
Change in interest in charitable remainder trust	11,172	(297,732)
Distributions from charitable remainder trust	16,989	17,293
Net realized and unrealized gain on investments in marketable securities	(86,097)	(168,180)
Depreciation	210	209
Change in federal excise tax assets and liabilities	842	(2,258)
Changes in operating assets and liabilities:		
Investment income receivable and other assets	(3,811)	(205)
Grants payable	11,707	(18,782)
Net cash used by operating activities	(3,884)	(220)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments in marketable securities	(308,033)	(495,256)
Proceeds from sales of investments in marketable securities	292,603	380,918
Net change money market mutual funds held as investments	(1,122)	77,532
Proceeds from distributions from charitable remainder trust	16,989	17,293
Proceeds from repayment of notes receivable	55	389
Purchase of property		(58)
Net cash provided (used) by investing activities	492	(19,182)
NET CHANGE IN CASH EQUIVALENTS	(3,392)	(19,402)
Cash equivalents, beginning of year	16,738	36,140
Cash equivalents, end of year	$ 13,346	$ 16,738

Supplemental disclosure of cash flow information:		
Taxes paid	$670	$442
Grants paid with stock	$86	$89

See accompanying notes to financial statements.

NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

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. For more than 70 years, the Foundation has funded projects and programs that better communities in the State of Texas. 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.

Federal income tax status – The Foundation is exempt from federal income tax under §501(c)(3) of the Internal Revenue Code (the Code) and classified as a private foundation under §509(a). The Foundation is exempt from federal income tax on income from related activities under §501(a). The Foundation is subject to a 1% or 2% excise tax on its net investment income.

Investments in marketable securities are reported at fair value. Realized gains and losses on securities sold are determined using the specific identification method and original cost. Purchases and sales of marketable securities are reported on a trade-date basis. Unrealized gains and losses on securities arise from increases or decreases in fair value and include the effect of currency translation with respect to transactions and holdings of foreign securities. Interest and dividends are recognized when earned.

Investment in real estate is carried at cost.

Program notes receivable are reported at the net present value of amounts expected to be collected in the future.

Interest in charitable remainder trust – The beneficial interest in the Libbie Shearn Moody Trust (the Trust) is recorded based on the estimated fair value of the Foundation's percentage remainderman interest held by the Trust, less the present value of the payments expected to be made to other life estates.

Net asset classification – Revenue and the related net assets are classified based on the existence or absence of donor-imposed restrictions in accordance with the provisions of the Foundation's trust indenture, as follows:

- *Unrestricted net assets* include those net assets whose use is not restricted by donor-imposed stipulations even though their use may be limited in other respects such as by contract or board designation.
- *Temporarily restricted net assets* include revenue and dividend and interest income restricted by the donor for specific purposes or time periods. When a purpose restriction is accomplished or a time restriction ends, temporarily restricted net assets are released to unrestricted net assets.
- *Permanently restricted net assets* include revenue and contributions that donors have restricted in perpetuity with only income available to support specified programs of the Foundation.

Grants approved are recognized as expense when the Foundation approves an unconditional commitment to a grant recipient. Commitments made but not yet funded are reported as grants payable. Grants payable in more than one year are reported at the present value of their future cash outflows using a risk-free rate-of-return applicable to the year the grant was made, if material.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts of reported revenue and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

Recent financial accounting pronouncement – In August 2016, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The amendments in this ASU are aimed at providing more useful information to users of not-for-profit financial statements. Under this ASU, net assets will be presented in two classes: *net assets with donor restrictions* and *net assets without donor restrictions*. New or enhanced disclosures will be required about the nature and composition of net assets, and the liquidity and availability of resources for general operating expenditures within one year of the balance sheet date. Expenses will be required to be presented by both nature and function and investment return will be presented net of external and direct internal investment expenses. Absent explicit donor stipulations, restrictions on long-lived assets will expire when assets are placed in service. The Foundation is required to adopt this ASU for fiscal year 2018. Adoption of this ASU will impact the presentation and disclosures of the financial statements.

NOTE 2 – DEPARTURE FROM GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

The Foundation reports their investment in American National Insurance Company (ANICO) and Gal-Tex Hotel Corporation (Gal-Tex) at fair value. The Foundation's ownership of each of these investments exceeds 20% and should be accounted for using the equity method of accounting.

NOTE 3 – INVESTMENTS AND FAIR VALUE

Generally accepted accounting principles require that certain assets and liabilities be reported at fair value and establishes a hierarchy that prioritizes inputs used to measure fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In accordance with ASU 2015-07*, Fair Value Measurements,* investments for which fair value is measured at net asset value per share (or its equivalent) using the practical expedient have not been categorized in the fair value hierarchy. The three levels of the fair value hierarchy are as follows:

- *Level 1* – Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the reporting date. The types of investments included in Level 1 are securities traded and valued based upon a public exchange.
- *Level 2* – Inputs are quoted prices in nonactive markets or in active markets for similar assets or liabilities, or inputs which are either directly or indirectly observable with observable market data at the reporting date.
- *Level 3* – Inputs are not observable and are based on the reporting entity's assumptions about the inputs market participants would use in pricing the asset or liability.

Assets measured at fair value at December 31, 2017 are as follows (in thousands):

	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Marketable securities:				
Common stock ownership interests exceeding 20%:				
American National Insurance Company (a)	$ 784,546			$ 784,546
Gal-Tex Hotel Corporation			$ 33,900	33,900
Mutual funds:				
Domestic equity:				
Large-cap	237,682			237,682
Small-cap	55,961			55,961
Mid-cap	54,819			54,819
International equity	34,569			34,569
Money market	17,124			17,124
Bond	5,717			5,717
Corporate debt securities		$ 185,829		185,829
U. S. Government agency securities		131,446		131,446
U. S. Treasury securities	119,315			119,315
Common stock:				
Large-cap	11,447			11,447
Municipal obligations		1,649		1,649
Total investments measured at fair value	1,321,180	318,924	33,900	1,674,004
Assets held in charitable remainder trust			1,145,062	1,145,062
Cash equivalents:				
Money market mutual funds	13,346			13,346
Total assets measured at fair value	$ 1,334,526	$ 318,924	$ 1,178,962	$ 2,832,412

Assets measured at fair value at December 31, 2016 are as follows (in thousands):

	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Marketable securities:				
Common stock ownership interests exceeding 20%:				
American National Insurance Company (a)	$ 762,372			$ 762,372
Gal-Tex Hotel Corporation			$ 31,110	31,110
Mutual funds:				
Domestic equity:				
Large-cap	163,251			163,251
Small-cap	41,322			41,322
Mid-cap	47,061			47,061
International equity	22,980			22,980
Money market	16,002			16,002
Bond	5,705			5,705
Corporate debt securities		$ 189,920		189,920
U. S. Government agency securities		119,216		119,216
U. S. Treasury securities	116,095			116,095
Common stock:				
Large-cap	44,888			44,888
Mid-cap	7,773			7,773
Small-cap	1,153			1,153
Municipal obligations		2,508		2,508
Total investments measured at fair value	1,228,602	311,644	31,110	1,571,356
Assets held in charitable remainder trust			1,190,212	1,190,212
Cash equivalents:				
Money market mutual funds	16,738			16,738
Total assets measured at fair value	$ 1,245,340	$ 311,644	$ 1,221,322	$ 2,778,306

(a) American National Insurance Company (ANICO) offers a broad spectrum of insurance products, including individual and group life insurance, health insurance, annuities, and property and casualty insurance throughout the United States and its affiliated territories. Through noninsurance subsidiaries, ANICO invests in stocks and real estate. At December 31, 2017 and 2016, the Foundation owned approximately 6.1 million shares of common stock of ANICO representing an ownership interest of approximately 23%.

Summarized combined financial information of ANICO is as follows (in thousands):

	2017	2016
Revenue	$3,411,000	$3,227,951
Net income	$493,651	$181,003
Total assets	$26,386,764	$24,533,222
Total liabilities	$21,130,993	$19,871,727
Stockholders' equity	$5,255,771	$4,661,495

Valuation methods used for assets measured at fair value are as follows:

- *Mutual funds* are valued at the reported net asset value.
- *Corporate debt securities, U. S. Government agency securities* and *municipal obligations* are valued using prices obtained from independent quotation bureaus that use computerized valuation formulas which may include market-corroborated inputs for credit risk factors, interest rate and yield curves, and broker quotes to calculate fair values.
- *Common stock* is valued at the closing price reported on the active market on which the individual securities are traded.
- *Common stock in Gal-Tex* is valued based on an independent appraisal of the ownership interest.
- *U. S. Treasury securities* are valued using prices obtained from active market makers and inter-dealer brokers on a daily basis.
- *Interest in charitable remainder trust* is valued using the net present value as described in Note 7.

These valuation methods may produce a fair value that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Foundation believes its valuation methods are appropriate, the use of different methods or assumptions could result in a different fair value measurement at the reporting date.

Investments are exposed to various risks including interest rate, market and credit risks. Because of these risks, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statement of financial position and statement of activities.

Changes in the value of Level 3 assets consist of the following (in thousands):

	GAL-TEX	CHARITABLE REMAINDER TRUST	TOTAL
Balance at December 31, 2015, as previously reported	$ 737	$ 927,067	$ 927,804
Change in accounting method *(Note 2)*	29,363		29,363
Balance at December 31, 2015, as adjusted	30,100	927,067	957,167
Unrealized gain	1,010	297,732	298,742
Distributions		(34,587)	(34,587)
Balance at December 31, 2016	31,110	1,190,212	1,221,322
Unrealized gain (loss)	2,790	(11,172)	(8,382)
Distributions		(33,978)	(33,978)
Balance at December 31, 2017	$ 33,900	$ 1,145,062	$ 1,178,962

NOTE 4 – INVESTMENT AND SPENDING POLICIES

The Foundation follows an investment and spending policy that attempts to provide a predictable stream of income to fund its charitable activities. Following this strategy, the Board of Trustees (the Board) invests all Foundation assets, restricted and unrestricted, in a manner that is intended to produce results that meet or exceed minimum distribution requirements plus inflation while assuming a moderate level of investment risk. Actual returns in any given year may vary from this amount. To satisfy its long-term rate-of-return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends).

The Foundation has a policy of appropriating for distribution each year an amount that at least meets the minimum distribution as required by tax laws pertaining to private foundations. These distribution payouts will be used to meet both grant making and administrative needs of the Foundation. To meet the payout level determined each year, the Foundation follows the investment policies described above, utilizing both income and capital appreciation. Where prudent, and not inconsistent with the Foundation's trust indenture or the Uniform Prudent Investor Act (the Act) of the Texas Trust Code, the Foundation may use a portion of the principal of certain funds to meet the established payout or to fund special projects as determined by the Board.

NOTE 5 – PROGRAM NOTES RECEIVABLE

Program notes receivable consist of the following (in thousands):

	2017	2016
Unsecured 1.25% program note receivable from Moody Gardens	$ 12,096	$ 12,096
Other	237	292
Total program notes receivable	$ 12,333	$ 12,388

The unsecured 1.25% program note receivable from Moody Gardens is an advancing demand loan for a total amount of $12,096,000 that was advanced to the grant recipient in 2011. Interest only is due in annual payments on the anniversary date of the loan. Interest payments received were $151,000 in both 2017 and 2016. Payment of principal amounts outstanding are due upon demand of the Foundation or April 1, 2020, whichever should occur first.

NOTE 6 – FEDERAL EXCISE TAX

The Foundation qualifies as a tax-exempt organization, and accordingly, is not subject to federal income tax, except to the extent that it has unrelated business income. However, the Code imposes an excise tax on private foundations equal to 2% of net investment income (principally interest, dividends and net realized capital gains, less expenses incurred in the production of investment income). This tax is reduced to 1% for foundations that meet certain distribution requirements. The Foundation computed its provision for current federal excise tax at the rate of 1% in both 2017 and 2016. A deferred tax liability results from unrealized increases or decreases in fair value (appreciation) that are reported for financial statement purposes prior to recognition for tax purposes.

The Foundation's federal excise tax expense activity is as follows (in thousands):

	2017	2016
Current federal excise tax	$ 923	$ 474
Deferred federal excise tax expense (benefit)	589	(2,258)
Total federal excise tax expense (benefit)	$ 1,512	$ (1,784)
Current federal excise tax receivable	$ 361	$ 614
Deferred federal excise tax	$ 11,047	$ 10,458

Internal Revenue Code §4942 requires that the Foundation make qualifying charitable distributions approximately equal to 5% of the fair value of noncharitable assets reduced by acquisition indebtedness, if any, with respect to such assets. Such qualifying distributions must be made by the end of the succeeding taxable year in order to avoid the imposition of a 30% excise tax on any undistributed income. The Foundation is currently in compliance with these provisions and is not subject to this excise tax on undistributed income. The Foundation believes that it has appropriate support for the excise tax positions taken, and as such, does not have any uncertain tax positions that would result in a material impact on the Foundation's financial position or statement of activities.

NOTE 7 – INTEREST IN CHARITABLE REMAINDER TRUST

The Foundation has recorded its beneficial interest in the Trust based on the estimated fair value of the Foundation's percentage remainderman interest held by the Trust, less the present value of the payments expected to be made to other life estates. The present valuation 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 7.0%.

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

Approximately 82% of the assets of the Trust are 9,949,585 shares of ANICO common stock with a fair value of approximately $1.3 billion at December 31, 2017.

NOTE 8 – GRANTS PAYABLE

At December 31, 2017, grants approved and committed for future payments are expected to be funded as follows (in thousands):

2018	$ 32,696
2019	18,428
2020	7,471
2021	111
Thereafter	581
Total grants payable	$ 59,287

NOTE 9 – TEMPORARILY RESTRICTED AND PERMANENTLY RESTRICTED NET ASSETS

The Board, following the provisions of the Foundation's trust indenture and the Texas Trust Code, classify net assets, revenue, gains, and losses based on the existence or absence of donor-imposed restrictions, as applicable. Accordingly, net assets of the Foundation and changes therein are classified and reported as such.

Temporarily restricted net assets consist of estimated future distributions from the Trust. Assets are released from restriction when time restrictions are met.

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. Pursuant to donor restrictions, 338,522 shares of ANICO common stock held by the Foundation with a fair value of $43,415,000 at December 31, 2017 and $42,187,000 at December 31, 2016 are permanently restricted. Changes in permanently restricted net assets include the permanently restricted portion of the unrealized gain or loss on the ANICO common stock.

NOTE 10 – RELATED PARTY TRANSACTIONS

Certain employees of the Foundation are on the Board of Directors of Moody Gardens. At December 31, 2017, the Foundation had a note receivable from Moody Gardens in the amount of $12,096,000 (see Note 5).

Members of the Board benefit from a trust that has a majority ownership interest in the Moody National Bank of Galveston (the Bank). 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 $575,000 during the years ended December 31, 2017 and 2016, respectively. The Bank also serves as trustee for the Trust.

Members of the Board are on the Board of Directors of ANICO. At December 31, 2017, the Foundation beneficially owned 22.7% of the ANICO common stock. In addition, the Bank, in its capacity as trustee or agent of various accounts, had the power to vote approximately 49.1% of ANICO's common stock at December 31, 2017.

NOTE 11 – SUBSEQUENT EVENTS

Management has evaluated subsequent events through July 11, 2018, which is the date that the financial statements were available for issuance. As a result of this evaluation, no events were identified that are required to be disclosed or would have a material impact on reported net assets or changes in net assets.