STATE OF NORTH CAROLINA

NORTH CAROLINA STATE PORTS AUTHORITY

WILMINGTON, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2014

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

STATE OF NORTH CAROLINA

Office of the State Auditor

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AUDITOR'S TRANSMITTAL

The Honorable Pat McCrory, Governor
The General Assembly of North Carolina
Board of Directors, North Carolina State Ports Authority

We have completed a financial statement audit of the North Carolina State Ports Authority for the year ended June 30, 2014, and our audit results are included in this report. You will note from the independent auditor's report that we determined that the financial statements are presented fairly in all material respects.

The results of our tests disclosed no deficiencies in internal control over financial reporting that we consider to be material weaknesses in relation to our audit scope or any instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

Beth A. Wood

Beth A. Wood, CPA
State Auditor

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
North Carolina State Ports Authority
Wilmington, North Carolina

Report on the Financial Statements

We have audited the accompanying financial statements of the North Carolina State Ports Authority, a component unit of the State of North Carolina, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

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.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit 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 auditor's 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 Authority'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 Authority'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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the North Carolina State Ports Authority, as of June 30, 2014, and the changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 15 to the financial statements, during the year ended June 30, 2014, the North Carolina State Ports Authority adopted new accounting guidance, Governmental Accounting Standards Board Statement No. 65 – *Items Previously Reported as Assets and Liabilities*. Our opinion is not modified with respect to this matter.

Other Matters – Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 5, 2014 on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on

INDEPENDENT AUDITOR’S REPORT (CONCLUDED)

compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority’s internal control over financial reporting and compliance.

Beth A. Wood, CPA
State Auditor

Raleigh, North Carolina

November 5, 2014

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Overview of the Financial Statements and Financial Analysis

The annual financial statements of the North Carolina State Ports Authority (Authority) present the results of the Authority's financial activities for the fiscal year ended June 30, 2014. Management's Discussion and Analysis (MD&A) should be read in conjunction with the financial statements and provides a general overview of the Authority's financial activity during the fiscal year. The financial statements include, in addition to this MD&A, a Statement of Net Position, Statement of Revenues, Expenses, and Changes in Net Position, Statement of Cash Flows, and accompanying Notes to the Financial Statements. Management, in addition to this analysis, is responsible for the preparation of the accompanying basic financial statements.

The MD&A is intended to aid the reader in interpreting the Authority's relative financial position as of the above referenced date as well as gauging performance from one period to the next. Condensed key financial and nonfinancial information will be highlighted for the reader followed by a discussion of the Authority's current capital expansion program and economic outlook.

About the Authority

The North Carolina State Ports Authority was created by act of the North Carolina General Assembly (§ 136-260) in 1945 as a political subdivision of the State of North Carolina for the purpose of engaging in promoting, developing, constructing, equipping, maintaining and operating the harbors and seaports within the State, or within the jurisdiction of the State (§ 136-261). As a political subdivision of the State, the Authority has no stock or equity shareholders but rather is governed by an 11-member Board of Directors appointed by the Governor, Speaker of the House, and President Pro Tempore of the Senate of North Carolina. Specific Authority operations include the deep water ports of Morehead City and Wilmington, the inland terminal facilities located in Charlotte, NC and Greensboro, NC, as well as a private boat marina located in Southport, NC. These facilities, with the exception of the private boat marina, handle both import and export containerized, break bulk, and bulk cargos.

Financial Highlights and Analysis

The Governmental Accounting Standards Board (GASB) established as an independent nonprofit organization in 1984 is charged with establishing and maintaining accounting policy, procedure, and disclosure standards as they pertain to state and local governments. These standards are most commonly referred to as generally accepted accounting principles (GAAP). Governmental GAAP accounting requires the application of the GASB Statement No. 34 reporting model whose intent is to make financial statements more useful to and easier to understand by oversight bodies, investors, creditors, and citizens. This improvement in utility value is accomplished principally through the introduction of the MD&A and a reformatting and consolidation of the basic financial statements for the main type of governmental reporting fund types, general government and proprietary units. The Authority is classified as a discretely presented component unit and is reported as a non-major component unit in the State's *Comprehensive Annual Financial Report*.

The accompanying basic financial statements have been prepared on an accrual basis of accounting, meaning that revenues are recognized when earned and expenses when incurred. Please refer to Note 1 in the Notes to the Financial Statements for additional details relating to accounting policy. Taken as a whole, the Statement of Net Position, Statement of Revenues, Expenses, and Changes in Net Position, and Statement of Cash Flows are one measure of an organization's overall financial health and value. Individually, the Statement of Net Position is a static view of financial value while the other two depict the movement of key elements from one period to the next, with a specific focus on the organization's net position and cash and cash equivalents.

As summarized in the following table by major category, a comparison of net position as of June 30, 2014 to that of the prior year yields several significant changes.

Condensed Statement of Net Position

(in thousands)	June 30, 2014	June 30, 2013 (as restated)	Change	% Change
Current Assets	$ 17,157	$ 16,803	$ 354	2.1%
Capital Assets	276,164	290,275	(14,111)	-4.9%
Other Noncurrent Assets	13,277	14,392	(1,115)	-7.7%
Total Assets	306,598	321,470	(14,872)	-4.6%
Total Deferred Outflows of Resources	78	129	(51)	-39.5%
Current Liabilities	8,449	7,650	799	10.4%
Noncurrent Liabilities	92,432	94,921	(2,489)	-2.6%
Total Liabilities	100,881	102,571	(1,690)	-1.6%
Net Position	$ 205,795	$ 219,028	$ (13,233)	-6.0%

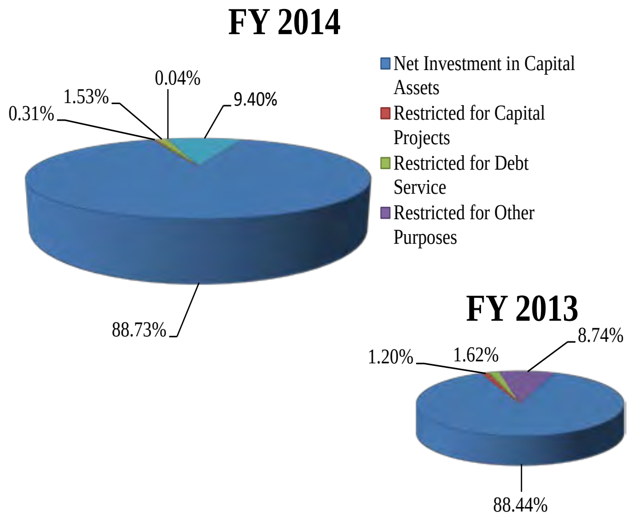
The change in capital assets, representing the single largest dollar value change in assets, is due to the impairment of construction projects that were placed on permanent stoppage during the fiscal year. The reduction in total liabilities represents the planned amortization of principal. The following table provides selected financial information pertaining to changes in assets and liabilities. Please refer to the accompanying Notes to the Financial Statements for further details with respect to these and other changes.

(in thousands)	June 30, 2014	June 30, 2013	Change	% Change
Current Assets:				
Cash and Cash Equivalents	$ 5,981	$ 4,261	$ 1,720	40.4%
Short-Term Investments	2,442	3,194	(752)	-23.5%
Receivable, Net	6,459	6,830	(371)	-5.4%
Capital Assets:				
Historical Cost	417,336	423,588	(6,252)	-1.5%
Accumulated Depreciation	(141,172)	(133,313)	7,859	5.9%
Noncurrent Assets:				
Investments	9,412	8,609	803	9.3%
Restricted Due from Primary Government	678	2,599	(1,921)	-73.9%
Noncurrent Liabilities:				
Long-Term Debt	92,354	94,792	(2,438)	-2.6%

The increase in unrestricted cash and cash equivalents relates principally to a reduction in cash outflows for the acquisition of capital assets as compared to the prior year, and reductions in certain operating expenses. The decrease in short-term investments is offset by an increase in noncurrent investments, and is the result of changes in the composition of the investment portfolio. The decrease in restricted due from primary government was a byproduct of the decrease in capital grant revenue described below.

The Authority's net position is divided into five major categories. The first, net investment in capital assets represents the Authority's equity position with regards to property, facilities, and equipment. The second category is restricted to expenditure for capital projects. The third category is restricted for debt service payments as required by bond indentures, for revolving debt payments used to finance equipment purchases, and other debt obligations. The fourth category is restricted for use by other third parties. The final category is that of unrestricted which is available for any lawful purpose of the Authority. The following exhibit analyzes the Authority's net position category mix for the periods ending June 30, 2014 and 2013, respectively. Significant changes, as noted above, are the result of the decrease in restricted due from primary government related to the receipt of capital grants receivable (Restricted for Capital Projects).

Net Position



(in thousands)	2014
Net Investment in Capital Assets	$ 182,604
Restricted for Capital Projects	634
Restricted for Debt Service	3,140
Restricted for Other Purposes	75
Unrestricted	19,342
Net Position	$ 205,795

	2013 (as restated)
Net Investment in Capital Assets	$ 193,699
Restricted for Capital Projects	2,639
Restricted for Debt Service	3,538
Unrestricted	19,152
Net Position	$ 219,028

The Statement of Revenues, Expenses, and Changes in Net Position reflects an overall decrease in net position for the current fiscal year ending June 30, 2014 of $13,232,647, or approximately 6%. This decrease is principally a product of decreased revenue generation from cargo movement, decreases in capital grant funding and the impairment of construction in progress assets that were placed on permanent stoppage. The following table identifies variances between major financial categories for the fiscal years ending June 30, 2014 and 2013, respectfully.

Condensed Statement of Revenues, Expenses, and Changes in Net Position

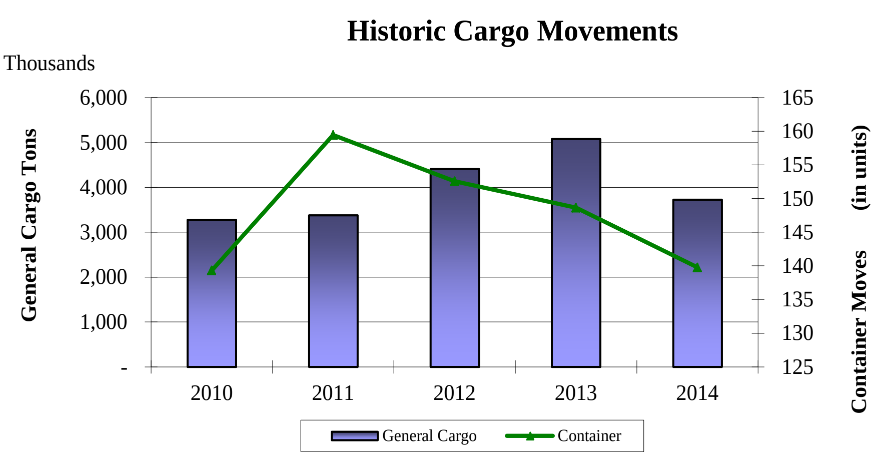
(in thousands)	June 30, 2014	June 30, 2013 (as restated)	Change	% Change
Operating Revenues	$ 39,200	$ 44,294	$ (5,094)	-11.5%
Operating Expenses	40,656	39,534	1,122	2.8%
Operating Income (Loss)	(1,456)	4,760	(6,216)	-130.6%
Nonoperating Revenues (Expenses):				
Investment Income, Net	55	16	39	243.8%
Interest and Fees on Debt	(3,923)	(3,962)	(39)	-1.0%
Other Nonoperating Revenues	73	46	27	58.7%
Net Nonoperating Expenses	(3,795)	(3,900)	(105)	-2.7%
Other Revenues and Losses:				
State Capital Aid		15	(15)	-100.0%
Capital Asset Impairment Loss	(8,644)	(4,295)	4,349	101.3%
Capital Grants	662	4,211	(3,549)	-84.3%
Total Revenues	39,990	48,582	(8,592)	-17.7%
Total Expenses	(53,223)	(47,791)	5,432	11.4%
Increase (Decrease) in Net Position	(13,233)	791	$ (14,024)	-1772.9%
Net Position, Beginning of Period	219,028	218,237		
Net Position, End of Period	$ 205,795	$ 219,028		

As reflected in the preceding table, the Authority posted an operating loss of $1,456,291 as the result of a decrease in overall revenue and an increase in total operating expenses. Total revenues declined significantly (17.7%) as a result of declined volumes in container movements as well as handled tonnage. The Authority also received significantly fewer capital grant funds during the current fiscal year. The following tables show the major sources of both operating and other revenues in detail, as well as revenues by major operating facility.

Operating and Other Revenues, by Major Source

(in thousands)	June 30, 2014	June 30, 2013	Change	% Change
Operating Revenues:				
Sales and Services, Net	$ 34,693	$ 39,734	$ (5,041)	-12.7%
Rental and Lease Earnings	4,507	4,560	(53)	-1.2%
Total Operating Revenues	39,200	44,294	(5,094)	-11.5%
Nonoperating Revenues:				
Investment Earnings, Net	55	16	39	243.8%
Other	73	46	27	58.7%
Other Nonoperating Revenues:				
State Capital Aid		15	(15)	-100.0%
Capital Grants	662	4,211	(3,549)	-84.3%
Total Other Nonoperating Revenues	662	4,226	(3,564)	-84.3%
Total Revenues	$ 39,990	$ 48,582	$ (8,592)	-17.7%

The decreased operating levels as compared to the prior year are viewed to be a product of both the global economy and commodities markets, and can be attributed to declines in North Carolina's agriculture and industrial sectors. The Authority, as previously indicated, has been experiencing a general recovery trend which is expected to resume in the following fiscal cycle. The following graph and table depict these current changes and general trends utilizing nonfinancial data and measurements.



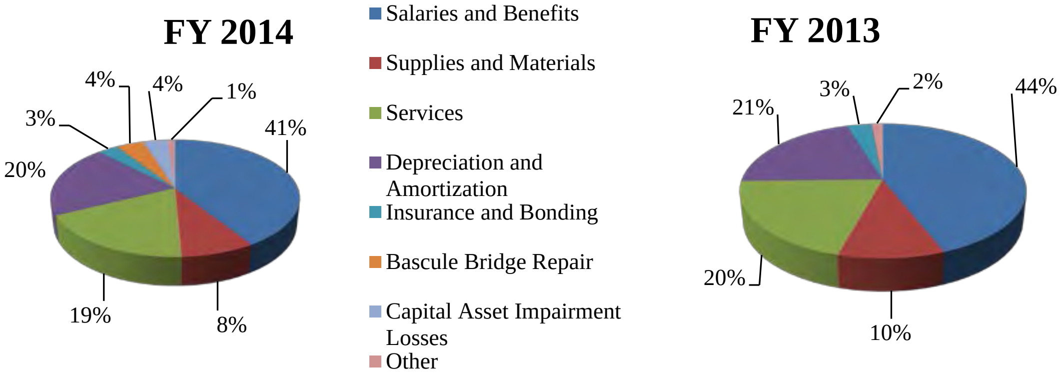
Summarized Cargo Movement (In Units)

	June 30, 2014	June 30, 2013	Change	% Change
Container Movement	139,755	148,637	(8,882)	-6.0%
General Cargo Movement (Short Tons)	3,932,634	5,169,225	(1,236,591)	-23.9%
Vessel Calls	1,029	1,027	2	0.2%
Rail Car Activity	9,280	13,246	(3,966)	-29.9%

Given the nature of declines in general cargo business volumes and the tentative nature of the global recovery, the Authority has continued to enforce cost containment measures where possible. However, these measures were offset by increases in other operating expenses categories. The notable increase in operating expenses related to two nonrecurring items, the first of which was related to repairs on an NCDOT bridge that enables rail access to Radio Island. The Authority's participation in funding the bridge repairs was advanced by the NCDOT and will be repaid over the next ten years. The second item represents the impairment of design plans for wood pellet export facilities due to construction stoppage. These projects were cancelled to allow the customer to build the facilities themselves. The majority of the cash spent on the design of these facilities occurred in the previous fiscal year. The following table and graphs analyze operating expense by major category as well as providing a relative mix year-over-year.

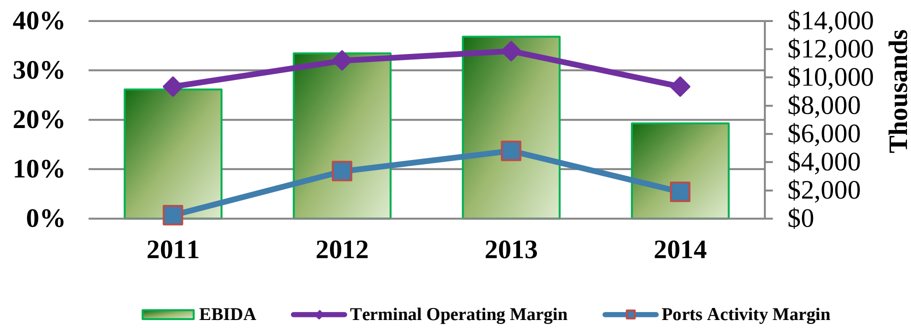
Operating Expense by Major Category

(in thousands)	June 30, 2014	June 30, 2013	Change	% Change
Salaries and Benefits	$ 16,765	$ 17,403	$ (638)	-3.7%
Supplies and Materials	3,359	4,062	(703)	-17.3%
Services	7,503	8,050	(547)	-6.8%
Bascule Bridge Repair	1,730		1,730	-
Capital Asset Impairment Losses	1,546		1,546	-
Depreciation and Amortization	8,210	8,129	81	1.0%
Insurance and Bonding	1,291	1,305	(14)	-1.1%
Other	252	585	(333)	-56.9%
Total Operating Expenses	$ 40,656	$ 39,534	$ 1,122	2.8%



The ultimate effect of declining volumes, stable pricing, and an increase in repair costs to support rail access to Radio Island is an overall decline in the Authority's marginal profitability and cash flow generation as derived from its operations. The following graph depicts this decline by analyzing operating margins and earnings before interest, depreciation, and amortization (EBIDA). This trend is anticipated to improve over the following fiscal cycle.

Historical Margin and EBIDA Analysis

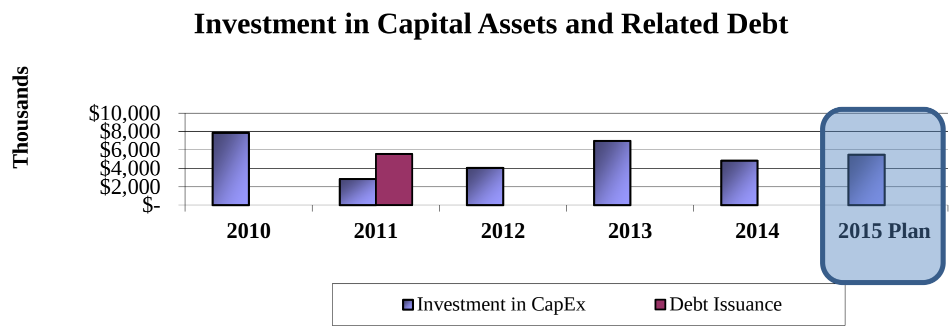


Given the continued global economic recovery over the next several years, the Authority's market share, market position, and long-term growth expectations are considered sustainable as they are driven in a large part, both in the case of container volumes as well as for general terminal activities, by the following domestic port operating conditions. The first being continued long-term growth outlook for US east coast cargo volumes associated with both general increases in world trade and the repositioning of certain cargo volumes from the West Coast relating to congestion, capacity, and operational limitations in those facilities. Second, increases in the North-South container trade and transshipment opportunities. Third, the growing allocation of resources to container operations in competing east coast ports to the north and south, and the resulting decline in capacity/facilities offerings for bulk and break bulk commodities.

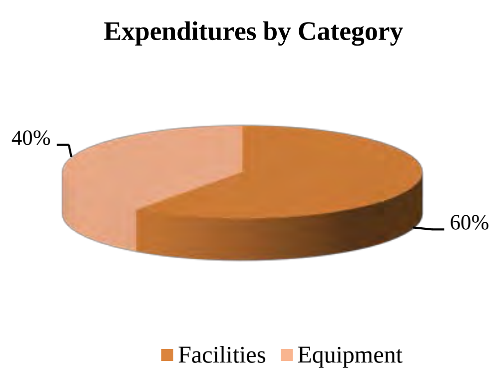
Capital Assets and Long-Term Debt

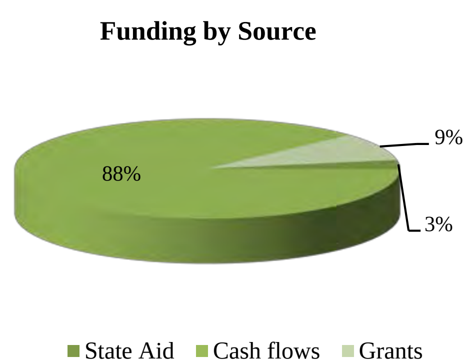
The origins of the Authority's current capital expansion program can be traced back to late fiscal year 1995 and early 1996, at which point, the Authority undertook a significant and comprehensive strategic planning effort which, among other outputs, produced a long-term market plan and corresponding capital infrastructure program. This program was based on a number of motivating factors including the need to address an aging infrastructure system, seek and secure new business development opportunities, and explore general economic growth opportunities. In keeping with the established planning process, the Authority continually updates its strategic business plan along with long-range market, financial, and corresponding capital infrastructure plans. Terminal improvements and equipment needs are identified and programmed to meet anticipated market growth requirements. Market growth expectations are adjusted for both long-term as well as short-term economic impacts associated with disruptions such as recessions. These expenditures are focused on the expansion or otherwise maintenance of the existing deep-water marine terminals in Wilmington and Morehead City and include acquisitions of equipment and the rehabilitation of existing facilities and infrastructure.

Since late fiscal year 2005 the Authority has assertively worked to rehabilitate or otherwise expand its facilities, investing approximately $196 million in equipment and infrastructure. Highlights of these expenditures include the acquisition of new container cranes and construction of a new warehouse facility. During the fiscal year $6 million was transferred out of construction in progress to depreciable capital assets, related mostly to enhancing our aging infrastructure system and updating operating systems. The following graph summarizes recent capital investment and related debt issuance.



Capital investment for the upcoming fiscal year is anticipated to continue and remain consistent with recent fiscal cycles, and is projected at approximately $6 million. Funding for these expenditures will be accomplished, as in recent years, by a combination of state capital aid, federal grants, reserves, and internal cash flows. A thorough review and update to the Authority's Capital Development Plan is underway. Further details on the capital improvement program can be found in the Authority's 2015 Capital Budget document. For a copy of this document call the finance office at (910) 343-6201. The following graphs provide a breakdown of planned fiscal year 2015 expenditures by category as well as anticipated funding by sources.





Economic Outlook

With recent global economic downturns, international trade has seen some of the deepest reductions ever posted. This, as indicated previously, has had notable effect on the Authority's cargo volumes. However the global recovery is clearly underway and coupled with improvements in key sectors of North Carolina's economy, trade volume is widely anticipated to return to and ultimately exceed traditional levels in the coming years. The Authority has experienced this recovery over the past several years through expansion and stabilization of container market share, recoveries of bulk volumes in 2010 and 2013, a resurgence of break bulk volumes in 2013, and projected stability in cargo trends for the upcoming fiscal cycle 2015.

Growth in cargo movement activity as reported in the Authority's fiscal year 2015 operating budget assumes an 8% increase in container activity as well as new bulk business and growth in breakbulk activities at both the Wilmington and Morehead City locations. As a result of these growth projections, the Authority is anticipating that utilization at its existing facilities will improve, thus raising operating profitability. Further, based on current as well as anticipated financial performance, the Authority will have adequate cash flows from operations to meet all current obligations as well as debt service requirements. The Authority's all-in debt service coverage for budgeted fiscal year 2015 is $1.95 to $1.00, which is well within the stipulated debt covenant requirements and sufficient to maintain its current credit ratings.

The Authority is currently engaged in a strategic planning initiative. The purpose of this initiative is to update the Authority's strategic direction and realign priorities to reflect the current organizational direction.

Contacting the Authority's Financial Management

If you have questions about these financial statements or need additional financial information, contact the Authority's Finance Department, 2202 Burnett Blvd., Wilmington, NC 28412 at (910) 343-6201.

North Carolina State Ports Authority
Statement of Net Position *Exhibit A-1*
June 30, 2014

ASSETS		
Current Assets:		
Cash and Cash Equivalents	$	5,980,869.94
Restricted Cash and Cash Equivalents		253,375.38
Short-Term Investments		2,441,742.76
Receivables, Net (Note 4)		6,459,430.14
Inventories		758,491.30
Prepaid Items		1,263,258.27
Total Current Assets		17,157,167.79
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		2,961,930.94
Investments		9,411,940.12
Restricted Due from Primary Government		678,423.33
Unamortized Charges		224,583.35
Capital Assets - Nondepreciable (Note 5)		61,120,925.17
Capital Assets - Depreciable, Net (Note 5)		215,043,537.07
Total Noncurrent Assets		289,441,339.98
Total Assets		306,598,507.77
DEFERRED OUTFLOWS OF RESOURCES		
Accumulated Decrease in Fair Value of Hedging Derivatives		77,857.16
Total Deferred Outflows of Resources		77,857.16
LIABILITIES		
Current Liabilities:		
Accounts Payable and Accrued Liabilities (Note 6)		1,847,156.75
Due to Primary Government		669,412.81
Unearned Revenue		432,710.29
Interest Payable		1,417,962.58
Advance from Primary Government - Current Portion (Note 9)		444,453.41
Long-Term Liabilities - Current Portion (Note 7)		3,637,634.95
Total Current Liabilities		8,449,330.79
Noncurrent Liabilities:		
Hedging Derivative Liability		77,857.16
Advance from Primary Government (Note 9)		1,285,813.50
Long-Term Liabilities (Note 7)		91,068,115.38
Total Noncurrent Liabilities		92,431,786.04
Total Liabilities		100,881,116.83
DEFERRED INFLOWS OF RESOURCES		
Deferred Inflows of Resources		0.00

NET POSITION

Net Investment in Capital Assets		182,604,177.38
Restricted for:		
Expendable:		
Capital Projects		633,449.18
Debt Service		3,140,306.32
Other		75,000.00
Unrestricted		19,342,315.22
Total Net Position	$	205,795,248.10

The accompanying notes to the financial statements are an integral part of this statement.

North Carolina State Ports Authority
Statement of Revenues, Expenses, and Changes in Net Position
For the Fiscal Year Ended June 30, 2014 ***Exhibit A-2***

REVENUES	
Operating Revenues:	
Sales and Services (Net of $188,262.96 in Allowance for Doubtful Accounts)	$ 34,693,729.66
Rental and Lease Earnings	4,506,764.73
Total Operating Revenues	39,200,494.39
EXPENSES	
Operating Expenses:	
Salaries and Benefits	16,765,444.69
Supplies and Materials	3,358,863.04
Services	7,503,986.87
Insurance and Bonding	1,291,096.36
Bascule Bridge Repair	1,730,266.91
Capital Asset Impairment Losses (Note 5)	1,545,586.49
Other Operating Expenses	251,729.12
Depreciation/Amortization	8,209,811.70
Total Operating Expenses	40,656,785.18
Operating Loss	(1,456,290.79)
NONOPERATING REVENUES (EXPENSES)	
Investment Income (Net of Investment Expense of $41,505.39)	55,180.93
Interest and Fees on Debt	(3,922,588.27)
Other Nonoperating Revenues	72,764.20
Net Nonoperating Expenses	(3,794,643.14)
Loss Before Other Revenues or Losses	(5,250,933.93)
Capital Asset Impairment Losses (Note 5)	(8,643,900.81)
Capital Grants	662,187.86
Decrease in Net Position	(13,232,646.88)
NET POSITION	
Net Position - July 1, 2013, as Restated (Note 15)	219,027,894.98
Net Position - June 30, 2014	$ 205,795,248.10

The accompanying notes to the financial statements are an integral part of this statement.

North Carolina State Ports Authority
Statement of Cash Flows — *Exhibit A-3*
For the Fiscal Year Ended June 30, 2014 — *Page 1 of 2*

CASH FLOWS FROM OPERATING ACTIVITIES		
Received from Customers	$	39,804,500.58
Payments to Employees and Fringe Benefits		(16,674,969.80)
Payments to Vendors and Suppliers		(12,698,078.59)
Net Cash Provided by Operating Activities		10,431,452.19
CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES		
Proceeds from Capital Debt		19,750,000.00
Capital Grants		2,583,148.96
Acquisition and Construction of Capital Assets		(5,164,770.13)
Proceeds from Sale of Capital Assets		72,764.20
Principal Paid on Capital Debt and Leases		(22,765,716.58)
Interest and Fees Paid on Capital Debt and Leases		(3,713,260.78)
Net Cash Used by Capital Financing and Related Financing Activities		(9,237,834.33)
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment Income		163,884.54
Net Cash Provided by Investing Activities		163,884.54
Net Increase in Cash and Cash Equivalents		1,357,502.40
Cash and Cash Equivalents - July 1, 2013		7,838,673.86
Cash and Cash Equivalents - June 30, 2014	$	9,196,176.26
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating Loss	$	(1,456,290.79)
Adjustments to Reconcile Loss to Net Cash Provided by Operating Activities:		
Depreciation/Amortization Expense		8,209,811.70
Capital Asset Impairment Losses		1,545,586.49
Changes in Assets and Liabilities:		
Receivables (Net)		374,273.31
Inventories		(88,851.05)
Prepaid Items		9,405.69
Accounts Payable and Accrued Liabilities		(181,538.10)
Due to Primary Government		38,720.52
Advance from Primary Government		1,730,266.91
Unearned Revenue		229,732.88
Compensated Absences		20,334.63
Net Cash Provided by Operating Activities	$	10,431,452.19

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	$	5,980,869.94
Restricted Cash and Cash Equivalents		253,375.38
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		2,961,930.94
Total Cash and Cash Equivalents - June 30, 2014	$	9,196,176.26

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Change in Fair Value of Investments	$	(108,703.61)
Amortization of Bond Premiums/Discounts		8,006.88
Loss on Impairment of Capital Assets		9,538,671.53

The accompanying notes to the financial statements are an integral part of this statement.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

A. Financial Reporting Entity - The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America (GAAP), the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government serves as a nucleus for a reporting entity when it issues separate financial statements. The North Carolina State Ports Authority is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*.

The accompanying financial statements present all funds for which the Authority's Board of Directors is financially accountable. Related foundations for which the Authority is not financially accountable or for which the nature of their relationship is not considered significant to the Authority are not part of the accompanying financial statements.

B. Basis of Presentation - The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis - for State and Local Governments*, the full scope of the Authority's activities is considered to be a single business-type activity and accordingly, is reported within a single column in the basic financial statements.

C. Basis of Accounting - The financial statements of the Authority have been prepared using the economic resource measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred, regardless of the timing of the cash flows.

Nonexchange transactions, in which the Authority receives (or gives) value without directly giving (or receiving) equal value in exchange includes certain grants and investment income. Revenues are recognized, net of estimated uncollectible amounts, as soon as all eligibility requirements imposed by the provider have been met, if probable of collection.

D. Cash and Cash Equivalents - This classification includes undeposited receipts, petty cash, cash on deposit with private bank accounts, cash on deposit with fiscal agents, and deposits held by the State Treasurer in the Short-Term Investment Fund (STIF). The STIF maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.

E. Investments - Investments generally are reported at fair value, as determined by quoted market prices or estimated amounts determined by management if quoted market prices are not available. Because of the inherent uncertainty in the use of estimates, values that are based on estimates may differ from the values that would have been used had a ready market existed for the investments. The net increase (decrease) in the fair value of investments is recognized as a component of investment income.

F. Receivables - Receivables consist of charges to customers for services, contract guarantees, and use of facilities. Receivables have been recorded for interest income and for amounts due from employees for salary advances. Receivables are recorded net of estimated uncollectible amounts.

G. Inventories - Inventories, consisting of expendable supplies, are valued at the lower of cost or market on a moving weighted average cost basis, which approximates cost on a first-in, first-out (FIFO) basis.

H. Prepaid Items - Prepaid items consist of prepayments for insurance, subscriptions, and maintenance contracts.

I. Unamortized Charges - Unamortized charges are comprised of prepayments of maintenance contracts for dredging that will be incurred in future periods.

J. Capital Assets - Capital assets are stated at cost at date of acquisition or fair value at date of donation in the case of gifts. The value of assets constructed includes all material direct and indirect construction costs. Interest costs incurred are capitalized during the period of construction.

The Authority capitalizes assets that have a value or cost of $5,000 or greater at the date of acquisition and an estimated useful life of more than one year. The Authority capitalizes intangible assets and internally generated software under these same provisions.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 10 to 60 years for general infrastructure, 8 to 75 years for buildings, 3 to 40 years for equipment, and 3 to 5 years for computer software.

K. **Restricted Assets** - Certain resources are reported as restricted assets because restrictions on asset use change the nature or normal understanding of the availability of the asset. Resources that are not available for current operations and are reported as restricted include resources restricted for the acquisition or construction of capital assets, resources legally segregated for the payment of principal and interest as required by debt covenants, and resources restricted for use by other external parties.

L. **Noncurrent Long-Term Liabilities** - Noncurrent long-term liabilities include principal amounts of revenue bonds payable, notes payable, capital lease obligations, and compensated absences that will not be paid within the next fiscal year.

Revenue bonds payable are reported net of unamortized premiums or discounts. The Authority amortizes bond premiums/discounts over the life of the bonds using the straight-line method. Issuance costs are expensed.

M. **Compensated Absences** - The Authority's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 or for which an employee can be paid upon termination of employment. When classifying compensated absences into current and noncurrent, leave is considered taken using a last-in, first-out (LIFO) method. Also, any accumulated vacation leave in excess of 30 days at year-end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

There is no liability for unpaid accumulated sick leave because the Authority has no obligation to pay sick leave upon termination or retirement. However, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

N. **Net Position** - The Authority's net position is classified as follows:

Net Investment in Capital Assets - This represents the Authority's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of Net Investment in Capital Assets. Additionally, deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of capital assets are also included in this component of net position.

Restricted Net Position - Expendable - Expendable restricted net position includes resources for which the Authority is legally or contractually obligated to spend in accordance with restrictions imposed by external parties.

Unrestricted Net Position - Unrestricted net position includes resources derived from sales and services, rental and lease earnings, sale of surplus property, and interest income.

Restricted and unrestricted resources are tracked separately. When both restricted and unrestricted funds are available for expenditure, the decision for funding is determined by management on a case-by-case basis.

O. Revenue and Expense Recognition - The Authority classifies its revenues and expenses as operating or nonoperating in the accompanying Statement of Revenues, Expenses, and Changes in Net Position. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Authority's principal ongoing operations. Operating revenues include activities that have characteristics of exchange transactions, such as sales and services and rental and lease earnings. Operating expenses are all expense transactions incurred other than those related to capital and noncapital financing or investing activities as defined by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*.

Nonoperating revenues include activities that have the characteristics of nonexchange transactions. Revenues from nonexchange transactions and state capital appropriations that represent subsidies or gifts to the Authority, as well as investment income, are considered nonoperating since these are either investing, capital, or noncapital financing activities. Capital contributions are presented separately after nonoperating revenues and expenses.

NOTE 2 - DEPOSITS AND INVESTMENTS

A. Deposits - Unless specifically exempt, the Authority is required by *North Carolina General Statute* 147-77 to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer.

At June 30, 2014, the amount shown on the Statement of Net Position as cash and cash equivalents includes $21,931.27 which represents the Authority's equity position in the State Treasurer's STIF. The STIF (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.3 years as of June 30, 2014. Assets and shares of the STIF are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's STIF) are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page http://www.osc.nc.gov/ and clicking on "Reports," or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

Cash on hand at June 30, 2014 was $1,260. The carrying amount of the Authority's deposits not with the State Treasurer was $9,172,984.99 and the bank balance was $9,337,187.51. Custodial credit risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned to it. The Authority does not have a deposit policy for custodial credit risk. As of June 30, 2014, the Authority's bank balance was exposed to custodial credit risk as follows:

Uninsured and Uncollateralized	$ 8,337,187.51

B. Investments - The Authority invests its excess funds in the same manner as the State Treasurer is required to invest, as discussed below.

G.S. 147-69.1(c), applicable to the State's General Fund, and G.S. 147-69.2, applicable to institutional trust funds, authorize the State Treasurer to invest in the following: obligations of or fully guaranteed by the United States; obligations of certain federal agencies; repurchase agreements; obligations of the State of North Carolina; certificates of deposit and other deposit accounts of specified financial institutions; prime quality commercial paper; asset-backed securities with specified ratings, specified bills of exchange or time drafts, and corporate bonds/notes with specified ratings; general obligations of other states; general obligations of North Carolina local governments; and obligations of certain entities with specified ratings.

In accordance with the bond resolutions, bond proceeds and debt service funds are invested in obligations that will by their terms mature on or before the date funds are expected to be required for expenditure or withdrawal. These bond proceeds and debt service funds are subject to the same investment risks noted below.

Investments are subject to the following risks.

Interest Rate Risk: Interest rate risk is the risk the Authority may face should interest rate variances affect the fair value of investments. The Authority does not have a formal policy that addresses interest rate risk.

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Authority has a formal policy that addresses credit risk. The policy limits investments to: obligations of the United States, or obligations backed by the full faith and credit by the U.S. government; government agencies; repurchase agreements with regard to securities guaranteed by the U.S. government; obligations of the State of North Carolina; time deposits of banks with a physical presence in North Carolina for the purpose of receiving commercial or retail deposits, not to exceed $100,000 per deposit (must be FDIC insured); prime quality commercial paper with a credit rating of no less than AAA by a nationally recognized rating agency; and corporate bonds and notes that bear a rating of no less than AAA by a nationally recognized rating agency.

Custodial Credit Risk: Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Authority does not have a formal policy for custodial credit risk.

The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2014.

		Investment Maturities (in Years)			
	Fair Value	Less Than 1	1 to 5	6 to 10	More than 10
Investment Type					
Debt Securities					
U.S. Agencies	$ 11,237,289.91	$ 1,825,349.79	$ 5,487,142.46	$ 866,139.79	$ 3,058,657.87
Money Market Funds	616,392.97	616,392.97			
Total Investments	$ 11,853,682.88	$ 2,441,742.76	$ 5,487,142.46	$ 866,139.79	$ 3,058,657.87

At June 30, 2014, the Authority's investments had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa
U.S. Agencies	$ 11,237,289.91	$ 11,237,289.91
Money Market Funds	616,392.97	616,392.97
Totals	$ 11,853,682.88	$ 11,853,682.88

Rating Agency: Moody's/Standard & Poors

At June 30, 2014, the Authority's investments were exposed to custodial credit risk as follows:

Investment Type	Held by Couterparty's Trust Dept or Agent not in Authority's Name
U.S. Agencies	$ 11,237,289.91

NOTE 3 - DERIVATIVE INSTRUMENTS

Derivative instruments held at June 30, 2014 are as follows:

		Change in Fair Value		Fair Value at June 30, 2014	
Type	Notional Amount	Classification	Increase (Decrease)	Classification	Asset (Liability)
Hedging Derivative Instruments					
Cash Flow Hedges					
Pay-Fixed Interest Rate Swap - Crane 11 Acquistion	$ 1,020,000	Deferred Inflow of Resources	$ 24,162.89	Hedging Derivative Liability	$ (61,341.36)
Pay-Fixed Interest Rate Swap - Toplift Acquisition	569,025	Deferred Inflow of Resources	26,905.88	Hedging Derivative Liability	(16,515.80)
			$ 51,068.77		$ (77,857.16)

Hedging derivative instruments held at June 30, 2014 are as follows:

Type	Objective	Notional Amount	Effective Date	Maturity Date	Terms
Pay-Fixed Interest Rate Swap	Hedge changes in cash flows	$ 1,020,000	02/07/05	02/07/20	Pay 4.35%, Receive 55% of USD Prime
Pay-Fixed Interest Rate Swap	Hedge changes in cash flows	569,025	11/17/05	12/16/15	Pay 3.76%, Receive 72% of USD 30 day LIBOR

The fair value of the pay-fixed interest rate swaps were estimated by the Authority's financial advisors through a calculation of Mark-To-Market (MTM) estimates utilizing the construction of mid-market forward curves that once constructed generate a nominal amount for each of a transaction's expected future payments. Those payments are then discounted at the respective zero rate, with the sum of all discounted payments equaling the MTM estimate.

Hedging Derivative Risks

Interest Rate Risk: The Authority is exposed to interest rate risk on its pay-fixed interest rate swaps. The fair values of these instruments are highly sensitive to interest rate changes. Additionally, as the underlying variable rate index decreases, the Authority's net payment on the swap agreement increases.

Termination Risk: The Authority is exposed to termination risk as it or the counterparty may terminate the swap if the other fails to perform under the terms of the contract. If terminated, the underlying variable-rate debt's interest rate risk would no longer be effectively hedged. In addition, if at the time of termination the swap has a negative fair value, the Authority would be liable to the counterparty for a payment equal to the counterparty's fair value in the swap.

Rollover Risk: The Authority is exposed to rollover risk as the maturity dates for the hedged variable-rate Crane 11 debt and the interest rate swap agreement are not the same with the underlying debt maturing on April 7, 2015 and the swap agreement maturing on February 7, 2020. Provisions have been made to review and renew the credit extension of the underlying debt through the maturity date of the swap agreement. However, this review will not occur until the current maturity date is reached and will be subject to a credit assessment at that point in time.

NOTE 4 - RECEIVABLES

Receivables at June 30, 2014, were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Due from Customers	$ 6,259,181.54	$ 188,262.96	$ 6,070,918.58
Investment Earnings	51,583.98		51,583.98
Due from Employees	236,085.59	15,916.31	220,169.28
Other	116,758.30		116,758.30
Total Current Receivables	$ 6,663,609.41	$ 204,179.27	$ 6,459,430.14

NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2014, is presented as follows:

	Balance July 1, 2013	Increases	Decreases	Balance June 30, 2014
Capital Assets, Nondepreciable:				
Land and Permanent Easements	$ 58,703,691.93	$ 0.00	$ 0.00	$ 58,703,691.93
Construction in Progress	13,935,601.29	3,813,272.91	16,253,768.94	1,495,105.26
Computer Software in Development	502,452.34	419,675.64		922,127.98
Total Capital Assets, Nondepreciable	73,141,745.56	4,232,948.55	16,253,768.94	61,120,925.17
Capital Assets, Depreciable:				
Buildings	84,331,002.41	1,330,596.50	627,868.79	85,033,730.12
Machinery and Equipment	76,053,007.25	2,217,182.52	6,950.00	78,263,239.77
General Infrastructure	186,251,345.42	2,869,814.07	13,146.55	189,108,012.94
Computer Software	3,810,356.22			3,810,356.22
Total Capital Assets, Depreciable	350,445,711.30	6,417,593.09	647,965.34	356,215,339.05
Less Accumulated Depreciation for:				
Buildings	26,479,961.10	1,585,262.50		28,065,223.60
Machinery and Equipment	32,510,636.07	2,374,400.27	6,950.00	34,878,086.34
General Infrastructure	71,792,374.17	3,552,910.51		75,345,284.68
Computer Software	2,529,538.48	353,668.88		2,883,207.36
Total Accumulated Depreciation	133,312,509.82	7,866,242.16	6,950.00	141,171,801.98
Total Capital Assets, Depreciable, Net	217,133,201.48	(1,448,649.07)	641,015.34	215,043,537.07
Capital Assets, Net	$ 290,274,947.04	$ 2,784,299.48	$ 16,894,784.28	$ 276,164,462.24

During the year ended June 30, 2014, the Authority incurred $3,922,588.27 in interest costs related to the acquisition and construction of capital assets that was charged to interest and fees on debt.

The Authority has pledged machinery and equipment with a carrying value of \$2,358,643.75 as security for notes payable. Additional information regarding notes payable can be found in Note 7.

The Authority has pledged land with a carrying value of \$30,738,105.56 as security for the Port Facilities Subordinated Revenue Refunding Bond, Series 2014. Additional information regarding the Series 2014 bond can be found in Note 7.

The Statement of Revenues, Expenses, and Changes in Net Position contains a nonoperating capital asset impairment loss of \$8,643,900.81. This amount is included in the decreases to construction in progress shown above. During the fiscal year ended June 30, 2013, the Authority reported a capital asset impairment loss that represented management's estimate of the total amount of construction in progress that was permanently impaired due to obsolescence. During the current period Authority management determined that the prior period estimate required adjustment, and that the NC International Terminal, Radio Island Terminal, and other related construction projects were impaired in their entirety due to obsolescence. GASB accounting standards require this change in estimate to be reported during the current period in the same manner as the original transaction.

The Statement of Revenues, Expenses, and Changes in Net Position also contains \$1,545,586.49 in capital asset impairment losses that are classified as operating expenses. This amount is included in the decreases to construction in progress shown above. This impairment was caused by the permanent construction stoppage of plans for development of wood forest export facilities at the Port of Wilmington & Morehead City. Instead, the customers have contracted to design and build the facilities themselves. This loss was caused by events that are separate and apart from those described above.

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2014, were as follows:

	Amount
Accounts Payable	\$ 1,428,660.91
Accrued Payroll	418,495.84
Total Accounts Payable and Accrued Liabilities	**\$ 1,847,156.75**

NOTE 7 - LONG-TERM LIABILITIES

A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities for the year ended June 30, 2014, is presented as follows:

	Balance July 1, 2013	Additions	Reductions	Balance June 30, 2014	Current Portion
Revenue Bonds Payable	$ 65,105,000.00	$ 19,750,000.00	$ 21,575,000.00	$ 63,280,000.00	$ 1,540,000.00
Add Premium	212,848.95		8,006.88	204,842.07	
Total Revenue Bonds Payable	65,317,848.95	19,750,000.00	21,583,006.88	63,484,842.07	1,540,000.00
Notes Payable	2,148,375.00		559,350.00	1,589,025.00	1,399,350.00
Capital Leases Payable	29,109,777.49		623,359.70	28,486,417.79	654,150.79
Compensated Absences	1,125,130.84	928,715.12	908,380.49	1,145,465.47	44,134.16
Total Long-Term Liabilities	$ 97,701,132.28	$ 20,678,715.12	$ 23,674,097.07	$ 94,705,750.33	$ 3,637,634.95

Additional information regarding capital lease obligations is included in Note 8.

B. Revenue Bonds Payable - The Authority was indebted for revenue bonds payable for the purposes shown in the following table:

Purpose	Series	Rate/ Ranges	Maturity Date	Amount of Issue	Paid Through June 30, 2014	Outstanding June 30, 2014
Construct Bulk Grain Facility	2001	.25%-15%	09/2022	$ 11,000,000.00	$ 8,345,000.00	$ 2,655,000.00
Port Facilities Revenue Bond, Jr. Lien	2008	.25%-15%	06/2036	20,500,000.00	20,500,000.00	
Port Facilities Revenue Bond, Sr. Lien	2010-A	5.25%	02/2040	23,690,000.00		23,690,000.00
Port Facilities Revenue Bond, Sr. Lien	2010-B	3.0%-5.0%	02/2029	20,245,000.00	3,060,000.00	17,185,000.00
Port Facilities Senior Lien Revenue Refunding Bond	2013	Variable[1]	02/2036	10,000,000.00		10,000,000.00
Port Facilities Subordinated Revenue Refunding Bond	2014	Variable[2]	02/2029	9,750,000.00		9,750,000.00
Total Revenue Bonds Payable (principal only)				$ 95,185,000.00	$ 31,905,000.00	
Plus Unamortized Premium						204,842.07
Total Revenue Bonds Payable, Net						$ 63,484,842.07

[1] Variable rate calculated monthly as .72% per annum + 68%(1-month LIBOR)
[2] Variable rate calculated monthly as .70% per annum + 68%(1-month LIBOR)

C. Demand Bonds - Included in bonds payable are two variable rate demand bond issues. Demand bonds are securities that contain a "put" feature that allows bondholders to demand payment before the maturity of the debt upon proper notice to the Authority's remarketing or paying agents.

With regards to the following demand bonds, the Authority has not entered into legal agreements, which would convert the demand bonds not successfully remarketed into another form of long-term debt. The bonds are subject to purchase on demand with 180 days prior written notice on any date specified in such notice occurring on or after 7 years of the date of issuance.

North Carolina State Ports Authority - Port Facilities Senior Lien Revenue Refunding Bond, Series 2013 (Series 2013): On December 20, 2013, the Authority issued a tax-exempt variable rate Series 2013 demand bond in the amount of $10,000,000 that has a final maturity date of February 1, 2036. The bond was initially issued as one fully registered bond without coupons in the aggregate principal amount of $10,000,000 and may not be exchanged for any denomination other than the outstanding principal amount thereof. This bond is a special obligation of the Authority secured by a senior lien upon and pledge of the Net Receipts of the Authority and on parity with all other parity indebtedness. The proceeds of this bond issue were used to refund the outstanding Port Facilities Subordinate Revenue Bonds Series 2008 and pay the costs of expenses incurred in connection with the sale and issuance of the Series 2013 Bond. The bond is not subject to a parity or special reserve account requirement. The bond is subject to purchase on demand with 180 days prior written notice on any date specified in such notice occurring on or after 7 years of the date of issuance beginning December 20, 2020.

North Carolina State Ports Authority - Port Facilities Subordinated Revenue Refunding Bond, Series 2014 (Series 2014): On January 23, 2014, the Authority issued a tax-exempt variable rate Series 2014 demand bond in the amount of $9,750,000 that has a final maturity date of February 1, 2029. The bond was initially issued as one fully registered bond without coupons in the aggregate principal amount of $9,750,000 and may not be exchanged for any denomination other than the outstanding principal amount thereof. The bond issue is not subject to a parity or special reserve account requirement. This bond is a special obligation of the Authority secured by a junior lien upon and pledge of the Net Receipts of the Authority. As additional security for these bonds, the Authority executed and delivered a deed of trust on the site of the NCIT Project to secure the Authority's obligations. The proceeds of this bond issue were used to refund the outstanding Port Facilities Subordinate Revenue Bonds Series 2008 and pay the costs of expenses incurred in connection with the sale and issuance of the Series 2014 Bond. The bond is subject to purchase on demand with 180 days prior written notice on any date specified in such notice occurring on or after 7 years of the date of issuance beginning January 23, 2021.

D. Bond Defeasance – The Authority has extinguished long-term debt obligations by the issuance of new long-term debt instruments and other available funds of the Authority. On December 20, 2013, the Authority issued a $10,000,000 Series 2013 refunding bond with a variable interest rate of .72% per annum plus 68% (1-month LIBOR), and on January 23, 2014, the Authority issued a $9,750,000 Series 2014 refunding bond with a variable interest rate of .70% per annum plus 68% (1-month LIBOR). These bonds were issued for the current refunding of $20,460,000 of outstanding Series 2008 Port Facilities Revenue Bonds with an average interest rate of .25%-15% and the payment of costs of expenses incurred in connection with the sale and issuance of the bonds. The refunding was undertaken to replace an irrevocable direct pay letter of credit issued by a bank dated November 1, 2008 and due to expire on February 12, 2014. There was no measurable economic gain or loss resulting from the issuance of the new long-term debt instruments due to their variable interest rates.

E. **Notes Payable** - The Authority was indebted for notes payable for the purposes shown in the following table:

Purpose	Financial Institution	Interest Rate	Final Maturity Date	Original Amount of Issue	Principal Paid Through June 30, 2014	Principal Outstanding June 30, 2014
Crane 11 Acquisition	SunTrust	4.35%	04/07/2015	$ 2,700,000.00	$ 1,680,000.00	$ 1,020,000.00
Container Handlers	BB&T	3.76%	12/16/2015	3,793,500.00	3,224,475.00	569,025.00
Total Notes Payable				$ 6,493,500.00	$ 4,904,475.00	$ 1,589,025.00

The above commercial debt is secured by the assets acquired. The Authority plans to refinance the note maturing on April 7, 2015, by extending the repayment term another five years.

F. **Annual Requirements** - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2014, are as follows:

	Annual Requirements			
	Revenue Bonds Payable		Notes Payable	
Fiscal Year	Principal	Interest	Principal	Interest
2015	$ 1,540,000.00	$ 2,285,187.25	$ 1,399,350.00	$ 148,958.00
2016	1,755,000.00	2,242,884.77	189,675.00	7,132.00
2017	1,810,000.00	2,196,986.58		
2018	1,865,000.00	2,146,048.59		
2019	1,935,000.00	2,090,372.86		
2020-2024	10,530,000.00	9,455,978.69		
2025-2029	11,785,000.00	7,600,964.54		
2030-2034	14,875,000.00	5,325,977.83		
2035-2039	14,445,000.00	2,427,489.23		
2040-2041	2,740,000.00	246,600.00		
Total Requirements	$ 63,280,000.00	$ 36,018,490.34	$ 1,589,025.00	$ 156,090.00

NOTE 8 - CAPITAL LEASE OBLIGATIONS

Capital lease obligations relating to container cranes are recorded at the present value of the minimum lease payments. Future minimum lease payments under capital lease obligations consist of the following at June 30, 2014:

2015	$ 2,036,403.52
2016	2,036,403.52
2017	2,036,403.52
2018	2,036,403.52
2019	2,036,403.52
2020-2023	29,436,932.25
Total Minimum Lease Payments	39,618,949.85
Amount Representing Interest (4.88% Rate of Interest)	11,132,532.06
Present Value of Future Lease Payments	$ 28,486,417.79

Machinery and equipment acquired under capital leases amounted to $33,892,318.27 at June 30, 2014. Depreciation for the capital assets associated with capital leases is included in depreciation expense, and accumulated depreciation for assets acquired under capital lease totaled $5,294,111.15 at June 30, 2014.

NOTE 9 - ADVANCE FROM PRIMARY GOVERNMENT

The Authority entered into an inter-agency agreement with the NC Department of Transportation in May 2011 to repair and strengthen the bascule span of NCDOT Railroad Bridge R-110, which crosses the Newport River and enables rail access to Radio Island. The agreement committed the Authority to fund 35% cost sharing repayable over ten years at 4% interest. The payments are unsecured and uncollateralized. Future minimum payments under the agreement consist of the following:

	Annual Requirements Advance from Primary Government	
Fiscal Year	Principal	Interest
2015	$ 444,453.41	$ 187,137.27
2016	156,913.15	51,496.17
2017	164,843.99	45,156.01
2018	171,437.75	38,562.25
2019	178,295.26	31,704.74
2020-2022	614,323.35	51,170.87
Total Requirements	$ 1,730,266.91	$ 405,227.31

NOTE 10 - FUTURE RENTAL REVENUES

The Authority leases certain land and facilities to others. These leases are accounted for as operating leases; revenues are recorded when earned on leased facilities. Future minimum revenues under noncancelable agreements treated as operating leases consist of the following at June 30, 2014:

Fiscal Year	Amount
2015	$ 3,354,322.48
2016	926,508.46
2017	822,362.90
2018	817,265.37
2019	824,009.37
2020 and thereafter	1,508,980.01
Total Future Rental Revenues	$ 8,253,448.59

NOTE 11 - PENSION PLANS

Retirement Plans - Each permanent full-time employee, as a condition of employment, is a member of the Teachers' and State Employees' Retirement System.

The Teachers' and State Employees' Retirement System (TSERS) is a cost-sharing multiple-employer defined benefit pension plan established by the State to provide pension benefits for employees of the State, its component units, and local boards of education. TSERS is administered by a 14-member Board of Trustees, with the State Treasurer serving as Chairman of the Board.

Benefit and contribution provisions for the TSERS are established by *North Carolina General Statutes* 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2014, these rates were set at 8.69% of covered payroll for employers and 6% of covered payroll for members.

For the current fiscal year, the Authority had a total payroll of $11,852,378.56, of which $11,773,267.03 was covered under the TSERS. Total employer and employee contributions for pension benefits for the year were $1,023,096.90 and $706,396.02, respectively.

Required employer contribution rates for the years ended June 30, 2013, and 2012, were 8.33% and 7.44%, respectively, while employee contributions were 6% each year. The Authority made 100% of its annual required contributions for the years ended June 30, 2014, 2013, and 2012, which were \$1,023,096.90, \$1,016,719.61, and \$952,502.43, respectively.

The Teachers' and State Employees' Retirement System's financial information is included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page http://www.osc.nc.gov/ and clicking on "Reports" or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

NOTE 12 - OTHER POSTEMPLOYMENT BENEFITS

A. Health Benefits - The Authority participates in the Comprehensive Major Medical Plan (the Plan), a cost-sharing, multiple-employer defined benefit health care plan that provides postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System. Coverage eligibility varies depending on years of contributory membership service in their retirement system prior to disability or retirement.

The Plan's benefit and contribution provisions are established by Chapter 135, Article 3B, of the General Statutes, and may be amended only by the North Carolina General Assembly. The Plan does not provide for automatic post-retirement benefit increases.

By General Statute, a Retiree Health Benefit Fund (the Fund) has been established as a fund in which accumulated contributions from employers and any earnings on those contributions shall be used to provide health benefits to retired and disabled employees and applicable beneficiaries. By statute, the Fund is administered by the Board of Trustees of the Teachers' and State Employees' Retirement System and contributions to the Fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and applicable beneficiaries and are not subject to the claims of creditors of the employers making contributions to the Fund. Contribution rates to the Fund, which are intended to finance benefits and administrative expenses on a pay-as-you-go basis, are established by the General Assembly.

For the current fiscal year the Authority contributed 5.4% of the covered payroll under the Teachers' and State Employees' Retirement System to the Fund. Required contribution rates for the years ended June 30, 2013, and 2012, were 5.3% and 5.0%, respectively. The Authority made 100% of its annual required contributions to the Plan for the years ended June 30, 2014, 2013, and 2012, which were \$635,756.42, \$646,892.43, and $640,122.60, respectively. The Authority assumes no liability for retiree health care benefits provided by the programs other than its required contribution.

Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page http://www.osc.nc.gov/ and clicking on "Reports," or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

B. Disability Income - The Authority participates in the Disability Income Plan of North Carolina (DIPNC), a cost-sharing, multiple-employer defined benefit plan, to provide short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System. Benefit and contribution provisions are established by Chapter 135, Article 6, of the General Statutes, and may be amended only by the North Carolina General Assembly. The plan does not provide for automatic post-retirement benefit increases.

Disability income benefits are funded by actuarially determined employer contributions that are established by the General Assembly. For the fiscal year ended June 30, 2014, the Authority made a statutory contribution of .44% of covered payroll under the Teachers' and State Employees' Retirement System to the DIPNC. Required contribution rates for the years ended June 30, 2013, and 2012, were .44% and .52%, respectively. The Authority made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2014, 2013, and 2012, which were $51,802.37, $53,704.28, and $66,572.75, respectively. The Authority assumes no liability for long-term disability benefits under the Plan other than its contribution.

Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

NOTE 13 - RISK MANAGEMENT

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These exposures to loss are handled via a combination of methods, including participation in State-administered insurance programs, purchase of commercial insurance, and self-retention of certain risks. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

The risk of tort claims of up to $1,000,000 per claimant is retained under the authority of the State Tort Claims Act. In addition, the State provides excess public officers' and employees' liability insurance up to $10,000,000 via contract with a private insurance company. The Authority pays the premium, based on a composite rate, directly to the private insurer.

The Authority is required to maintain fire and lightning coverage on all State-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the State. Such coverage is provided at no cost to the Authority for operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a $5,000 per occurrence deductible. However, in order to reduce its premiums the Authority has established higher deductibles for losses associated with buildings and supporting infrastructure of $100,000 and $250,000 on equipment.

All State-owned vehicles are covered by liability insurance through a private insurance company and handled by the North Carolina Department of Insurance. The liability limits for losses are $1,000,000 per claim and $10,000,000 per occurrence. The Authority pays premiums to the North Carolina Department of Insurance for the coverage.

The Authority is protected for losses from employee dishonesty and computer fraud. This coverage is with a private insurance company and is handled by the North Carolina Department of Insurance. The Authority is charged a premium by the private insurance company. Coverage limit is $5,000,000 per occurrence. The private insurance company pays 90% of each loss less a $75,000 deductible.

The Authority purchased other authorized coverage from private insurance companies through the North Carolina Department of Insurance. The Authority carries terminal operator's legal liability coverage from a private insurer at a premium of .265% for every dollar of operating revenue, not including rental and lease earnings. The Authority has also elected to pay an additional 5% of the total premium for terrorism coverage. The Authority has also purchased a clause to reduce the deductible related to airplane fuselage lifts at a cost of $1,100 per lift if using Authority equipment, or $850 per lift if using the ship's equipment.

Authority employees and retirees are provided comprehensive major medical care benefits. Coverage is funded by contributions to the State Health Plan (Plan), a discretely presented component unit of the State of North Carolina. The Plan has contracted with third parties to process claims.

The North Carolina Workers' Compensation Program provides benefits to workers injured on the job. All employees of the State and its component units are included in the program. When an employee is injured, the Authority's primary responsibility is to arrange for and provide the necessary treatment for work related injury. The Authority is responsible for paying medical benefits and compensation in accordance with the North Carolina Workers' Compensation Act. The Authority retains the risk for workers' compensation.

Term life insurance (death benefits) of $25,000 to $50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State Treasurer and funded via employer contributions. The employer contribution rate was .16% for the current fiscal year. Additional term life insurance (accidental death and disability benefits) is provided through a private insurance company. The benefit is equal to one and one-half times the employee's annual salary and is effective for all full-time employees. Employees may purchase additional coverage through payroll deduction and have the option to convert the terms offered by the provider to maintain the policy at their own cost upon termination of employment. Total employer contributions on behalf of Authority employees for the year ended June 30, 2014, were $51,519.95. The voluntary contributions by employees amounted to $25,414.27 for the year ended June 30, 2014.

Additional details on the state-administered risk management programs are disclosed in the State's *Comprehensive Annual Financial Report*, issued by the Office of the State Controller.

NOTE 14 - COMMITMENTS AND CONTINGENCIES

A. Commitments - The Authority has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were $2,944,361 at June 30, 2014.

B. Pending Litigation and Claims - The Authority is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. Authority management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the Authority.

NOTE 15 - NET POSITION RESTATEMENT

As of July 1, 2013, net position as previously reported was restated as follows:

		Amount
July 1, 2013 Net Position as Previously Reported	$	219,566,677.29
Restatements:		
Expense previously amortized bond issuance costs pursuant to GASB 65 requirements		(538,782.31)
July 1, 2013 Net Position as Restated	$	219,027,894.98

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Directors
North Carolina State Ports Authority
Wilmington, North Carolina

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the North Carolina State Ports Authority, a component unit of the State of North Carolina, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated November 5, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Authority's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

**INDEPENDENT AUDITOR'S REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS (CONCLUDED)**

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Authority's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Beth A. Wood

Beth A. Wood, CPA
State Auditor

Raleigh, North Carolina

November 5, 2014

ORDERING INFORMATION

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For additional information contact:
Bill Holmes
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This audit required 440 audit hours at an approximate cost of $41,360.