

STATE OF NORTH CAROLINA

THE UNIVERSITY OF NORTH CAROLINA AT CHAPEL HILL

CHAPEL HILL, NORTH CAROLINA

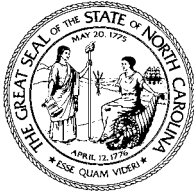
FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2014

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR



Beth A. Wood, CPA
State Auditor

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AUDITOR'S TRANSMITTAL

The Honorable Pat McCrory, Governor
The General Assembly of North Carolina
Board of Trustees, The University of North Carolina at Chapel Hill

We have completed a financial statement audit of The University of North Carolina at Chapel Hill 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.

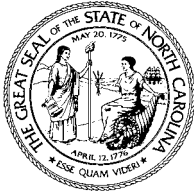
A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor

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Office of the State Auditor



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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
The University of North Carolina at Chapel Hill
Chapel Hill, North Carolina

Report on the Financial Statements

We have audited the accompanying financial statements of The University of North Carolina at Chapel Hill, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component units, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the University'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 opinions on these financial statements based on our audit. We did not audit the financial statements of the UNC Investment Fund, LLC, which represent 42 percent, 39 percent, and 10 percent, respectively, of the assets, net position, and revenues of the University; nor the financial statements of The Medical Foundation of North Carolina, Inc., The Educational Foundation Scholarship Endowment Trust, and the University of North Carolina at Chapel Hill Arts and Sciences Foundation, Inc., the University's discretely presented component units. Those statements were audited by other auditors, whose reports have been furnished to us, and our opinions, insofar as they relate to the amounts included for those entities, are based solely on the report of the other auditors.

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

INDEPENDENT AUDITOR'S REPORT (CONTINUED)

assurance about whether the financial statements are free from material misstatement. The financial statements of the UNC Investment Fund, LLC, The Medical Foundation of North Carolina, Inc., The Educational Foundation Scholarship Endowment Trust, and the University of North Carolina at Chapel Hill Arts and Sciences Foundation, Inc. were not audited in accordance with *Government Auditing Standards*.

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 University'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 University'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 opinions.

Opinions

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of The University of North Carolina at Chapel Hill, and its discretely presented component units, 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.

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, and other auditors, 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.

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 14, 2014 on our consideration of the University'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 compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University's internal control over financial reporting and compliance.



Beth A. Wood, CPA
State Auditor

Raleigh, North Carolina

November 14, 2014

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THE UNIVERSITY OF NORTH CAROLINA AT CHAPEL HILL MANAGEMENT'S DISCUSSION AND ANALYSIS

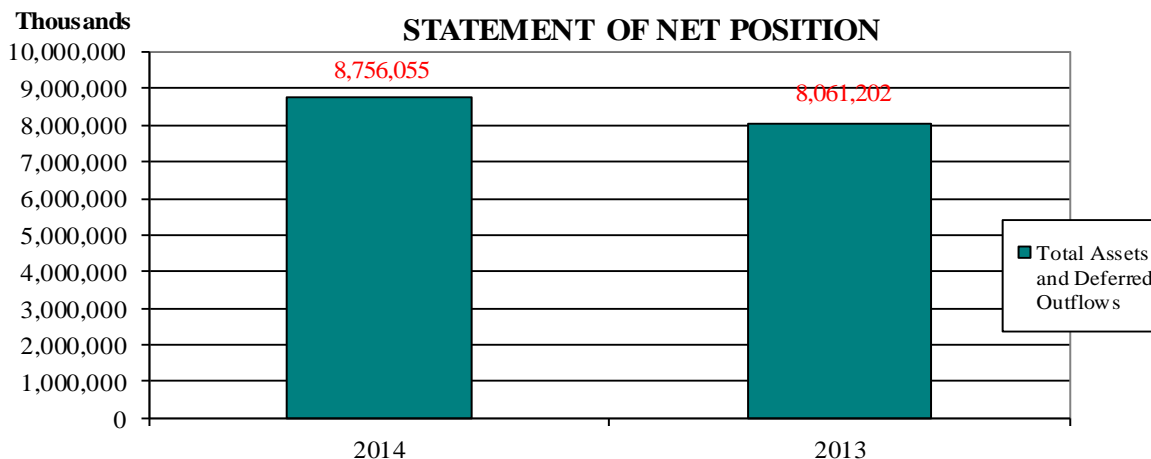
INTRODUCTION

Management's Discussion and Analysis provides an overview of the financial position and activities of The University of North Carolina at Chapel Hill (the University) for the fiscal year that ended June 30, 2014, with comparative information for the fiscal year ended June 30, 2013. Management has prepared the discussion and analysis to be read in conjunction with the financial statements and accompanying notes to the financial statements.

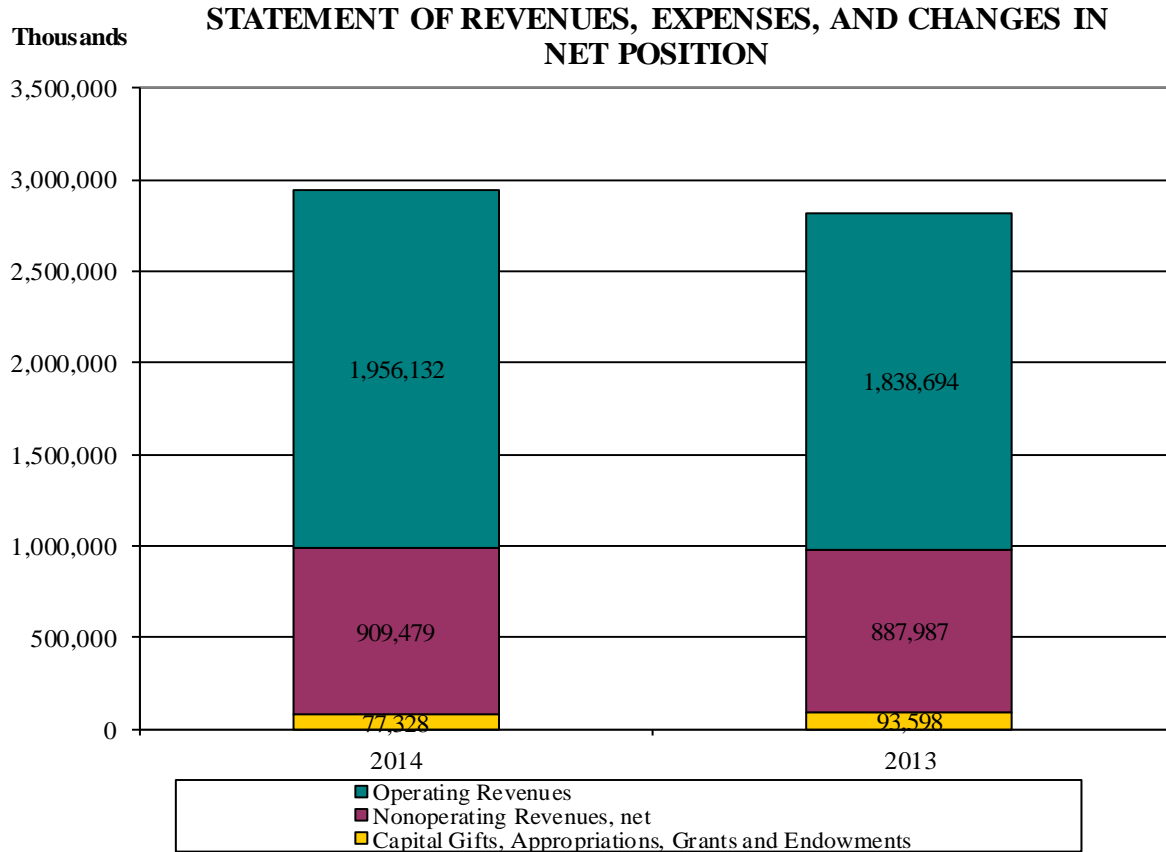
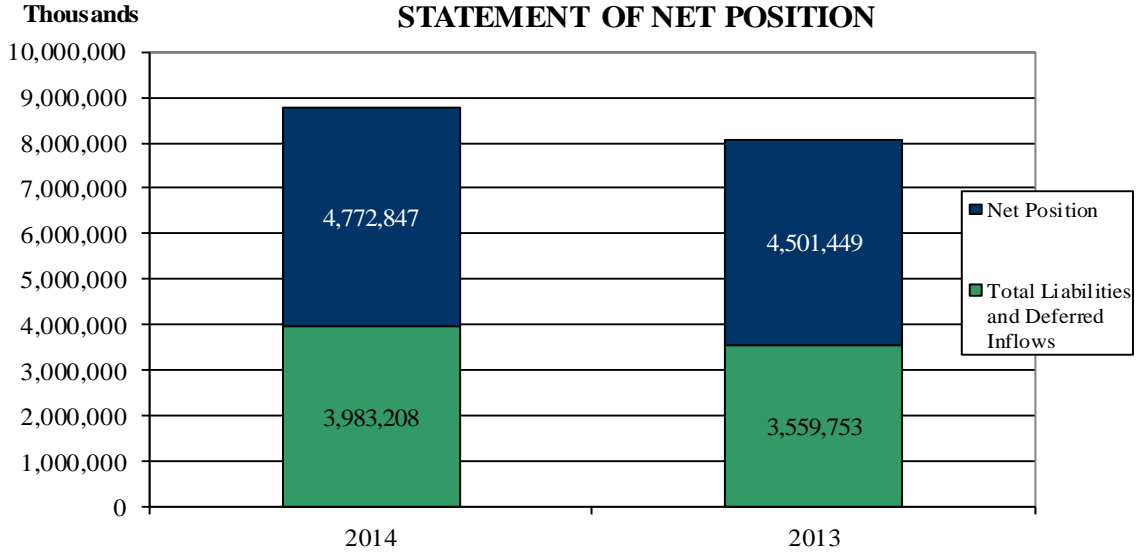
The University is a constituent institution of the multi-campus University of North Carolina System (UNC System), a component unit of the State of North Carolina, and an integral part of the State's *Comprehensive Annual Financial Report (CAFR)*. The financial reporting entity for the financial statements is comprised of the University and eleven component units. Eight component units are reported as if they were part of the University, and three are reported as discretely presented component units based on the nature and significance of their relationship to the University. Note 1A of the financial statements provides detailed information on the financial reporting entity.

FINANCIAL HIGHLIGHTS

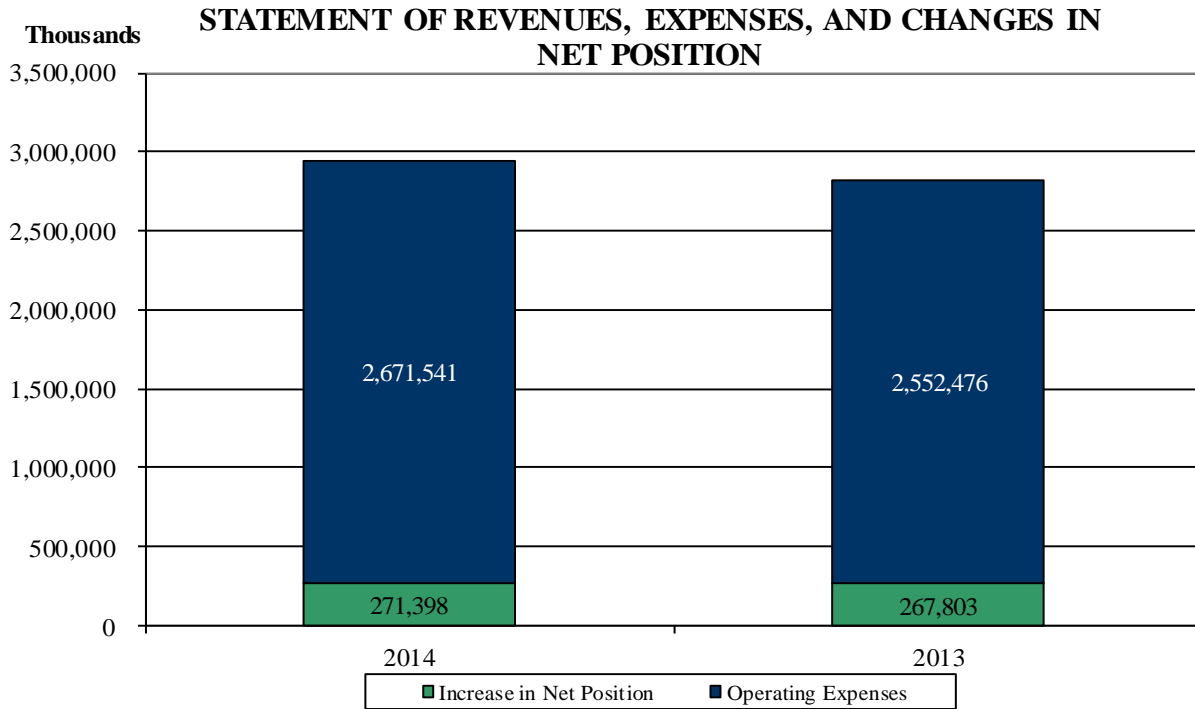
The University maintained its solid financial position at June 30, 2014 as the growth in operating revenues surpassed increases in operating expenses, and investment income grew substantially from the prior year. The University's total assets and deferred outflows were \$8.8 billion at June 30, 2014. Net position, which represents the residual interest in the University's assets and deferred outflows after deducting liabilities and deferred inflows, was \$4.8 billion at June 30, 2014. The University's net position increased by \$271 million in fiscal year 2013-2014 as a result of operating, nonoperating, and other changes in net position. A comparison of the total assets and deferred outflows, liabilities and deferred inflows, and net position at June 30, 2014 and June 30, 2013, along with the major components of the changes in net position for the two fiscal years are presented below:



MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)



MANAGEMENT’S DISCUSSION AND ANALYSIS (CONTINUED)



Net position improved 6.0% at June 30, 2014 over the prior year. Total assets increased 8.7% from the prior year and total liabilities rose 11.9% for the same period. The percentage increase of total operating revenues for fiscal year 2013-2014 over the prior year was greater than the corresponding increase in operating expenses: 6.4% and 4.7%, respectively. Net nonoperating revenues and expenses increased 2.4% in fiscal year 2013-2014 over the prior year, reflecting higher investment income mitigated by slightly lower state appropriations and noncapital gifts and grants. As a major research university, funding from contracts and grants continues to be of key importance to the University’s success in fulfilling its mission. In addition to the foregoing, fund raising for operational needs, sales and services, and tuition and fees likewise continued to provide important resources for the University.

USING THE FINANCIAL STATEMENTS

The financial statements have been prepared in accordance with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), which establishes standards for external financial reporting for public colleges and universities. The financial statements are presented on a consolidated basis to focus on the University as a whole. The full scope of the University’s activities is considered to be a single business type activity and accordingly, is reported within a single column in the basic financial statements.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The University's Financial Statements includes the following three financial statements.

- Statement of Net Position
- Statement of Revenues, Expenses, and Changes in Net Position
- Statement of Cash Flows

Management's Discussion and Analysis provides information regarding the Statement of Net Position and the Statement of Revenues, Expenses, and Changes in Net Position.

CONDENSED STATEMENT OF NET POSITION

The Statement of Net Position presents the financial position of the University at the end of the fiscal year, includes all assets and deferred outflows, all liabilities and deferred inflows, and segregates the assets and liabilities into current and noncurrent components. The following table summarizes the University's assets and deferred outflows, liabilities and deferred inflows, and net position on June 30, 2014 and June 30, 2013.

Assets, Liabilities, Deferred Resources, and Net Position (dollars in thousands)

	2014	2013	Percent Change
Assets:			
Current Assets	\$ 1,697,314	\$ 1,556,409	9.1
Noncurrent Assets:			
Endowment, Restricted, and Other Investments	3,574,709	3,129,647	14.2
Capital Assets, Net	3,117,129	3,112,151	0.2
Other Noncurrent Assets	282,037	182,568	54.5
Total Assets	8,671,189	7,980,775	8.7
Deferred Outflows of Resources	84,866	80,427	5.5
Liabilities:			
Current Liabilities	437,861	310,154	41.2
Noncurrent Liabilities:			
Funds Held in Trust for Pool Participants	1,973,240	1,661,608	18.8
Long-Term Liabilities	1,457,737	1,476,431	(1.3)
Other Noncurrent Liabilities	114,370	111,560	2.5
Total Liabilities	3,983,208	3,559,753	11.9
Deferred Inflows of Resources	0	0	
Net Position:			
Net Investment in Capital Assets	1,662,931	1,632,515	1.9
Restricted	2,189,082	1,896,046	15.5
Unrestricted	920,834	972,888	(5.4)
Total Net Position	\$ 4,772,847	\$ 4,501,449	6.0

Current Assets and Liabilities

The Statement of Net Position reflects that working capital, which is current assets less current liabilities, was \$1.2 billion at June 30, 2014 as well as the previous year. One of the factors contributing to a substantial working capital margin is that many operating funds are invested in the State Treasurer's Short-term Investment Fund in order to maintain a high

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

degree of liquidity while also earning interest. Such funds are reported as cash equivalents in the Statement of Net Position which details other current asset and current liability categories.

ENDOWMENT, RESTRICTED AND OTHER INVESTMENTS

Endowment investments increased 13.9% during 2013-2014 and were \$1.7 billion at June 30, 2014 and \$1.49 billion at June 30, 2013, and include permanent endowments, funds internally designated as endowments and similar funds such as gift annuities and charitable trusts.

The endowment assets are invested with The University of North Carolina at Chapel Hill Foundation Investment Fund, Inc. (Chapel Hill Investment Fund, or CHIF), which is reported as a governmental external investment pool in the financial statements. The Chapel Hill Investment Fund is a 501(c)(3) nonprofit corporation established to support the University by operating an investment pool for charitable, nonprofit foundations, associations, trusts, endowments, and funds that are organized and operated primarily to support the University. It is expected that all or substantially all of the assets of the Chapel Hill Investment Fund will be invested in the UNC Investment Fund, LLC (UNC Investment Fund, or UNCIF), an investment pool organized by the Chapel Hill Investment Fund to allow the University, along with other constituent institutions of the UNC System and affiliated organizations, to pool investment resources.

The CHIF investment objective is to earn a long-term real rate of return exceeding 5.5%. This objective is intended to support the Chapel Hill Investment Fund's distribution policy of providing a stable source of spending support that is sustainable over the long-term while preserving the purchasing power of the invested funds. The distribution rate is determined annually by its Board of Directors and for the past 5 years has ranged between 5% and 6% based on the beginning market value of the Chapel Hill Investment Fund.

As reported by UNC Management Company, Inc. (Management Company), the manager of the UNC Investment Fund, the endowment assets invested in the UNC Investment Fund recorded a 15.7% return for fiscal year 2013-2014, exceeding both the Strategic Investment Policy Portfolio (SIPP) return of 15.0% and the primary objective of earning a real rate of return exceeding 5.5%. All seven major asset classes used in managing the portfolio produced positive returns for the fiscal year 2013-2014.

Over the long term, UNCIF's 10-year annualized performance of 9.2% has surpassed its primary objective of providing a real rate of return exceeding 5.5%. UNCIF's ten year return exceeds both the SIPP benchmark and the Global 70/30 Index (comprised of 70% invested in the MSCI All Country World Index and 30% in the Barclay's U.S. Aggregate Bond Index) which returned 8.7% and 7.0%, respectively.

Over the intermediate term, UNCIF's performance reflects recovery from the sharp decline in financial markets witnessed in 2007-2008 with a 5-year annualized return of 10.3%. During this period, the Global 70/30 Index and the SIPP benchmark had returns of 11.7% and 12.1%, respectively.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Recognizing that severe market declines periodically occur, a University Statutory Endowment policy (established pursuant to NC General Statute 116-36) addresses the provisions of the Uniform Prudent Management of Institutional Funds Act (UPMIFA). The policy indicates that campus departments shall examine the endowment-supported activity for the upcoming fiscal year for possible deferment of program expenses, and if appropriate, pursue alternative funding for essential activities, and consult with donors regarding other funding options for program support. Invasion of endowment principal is an option of last resort and will only be done consistent with approved limitations to preserve the endowment principal's value. The distribution of investment earnings for fiscal years 2013-2014 and 2012-2013 provided for a full distribution without reduction to principal value.

Restricted investments of \$1.8 billion at June 30, 2014 include funds of affiliated entities that are neither part of the University's reporting entity nor reported discretely but invested through UNCIF. Other investments include bond reserves and related funds aggregating \$27.7 million.

CAPITAL ASSETS AND DEBT MANAGEMENT

The University completed Marsico Hall, an imaging research building, the University's largest capital project to date, in March 2014. A significant portion of funding for this 343,000 square foot building came from state debt in the form of COPS, Certificate of Participation. Current projects in design include: a comprehensive renovation to Mary Ellen Jones research building; Student Housing Phase III – a 250 bed undergraduate suite style residence hall which will replace units in Odum Village scheduled for decommissioning in 2017; and an addition to the Manning Plant for generators and a chilled water plant to meet capacity needs. All these projects are funded by the University through cash and debt financing. Looking forward through 2019 in light of the fact that Capital renewal needs are ongoing, the University's six-year capital plan includes \$210 million worth of projects for possible state funding subject to the financial climate. The University's six-year capital plan for nonappropriated funding identifies \$475 million worth of projects funded from a variety of sources, including debt.

In 2015, the University will initiate a University Master Plan that reflects the campus' strategic plan for sustainability and will guide future development of University properties. The plan will develop land use principles to support the University's academic and research priorities and include examination of facility utilization and needs, infrastructure, environmental resources, and economic impact.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

A summary of changes in capital assets is disclosed in Note 5. Capital assets, net of accumulated depreciation and amortization, at June 30, 2014 and June 30, 2013, were as follows:

<u>Capital Assets (dollars in thousand)</u>	<u>2014</u>	<u>2013</u>	<u>Percent Change</u>
Capital Assets:			
Construction in Progress	\$ 44,257	\$ 231,972	(80.9)
Land and Other Nondepreciable Assets	216,892	189,931	14.2
Buildings	2,014,192	1,869,324	7.7
General Infrastructure	610,646	588,089	3.8
Machinery, Equipment, and Computer Software	231,142	232,835	(0.7)
Total	<u>\$ 3,117,129</u>	<u>\$ 3,112,151</u>	0.2

During fiscal year 2013-2014, the University funded capital improvement projects with proceeds from the Board of Governors of the University of North Carolina System General Revenue Series 2012AB bond issue. After those funds are exhausted, the University will continue to use its commercial paper program to provide low cost bridge financing for capital projects until gifts are received or in anticipation of an external bond issue. As such, outstanding commercial paper debt was \$18.0 million at both June 30, 2014 and at June 30, 2013.

On behalf of the University, the Board of Governors for the University of North Carolina System issued General Revenue Bonds Series 2014 in the amount of \$265.6 million during October 2014 to advance refund a portion of its General Revenue Bonds Series 2005A. (See Subsequent Events Note 20 for additional information.)

On February 14, 2014, a University unit that is blended for financial reporting purposes restructured a bank note, paying down \$4.25 million in principal and extending the duration of the remaining \$5.0 million with a final maturity date of February 14, 2024. In addition, on October 3, 2013, another University blended unit closed on a bank note that provides up to \$30.0 million in funding for the construction of a capital project. The note expires on October 2, 2016. At June 30, 2014, the total amount of draws against the note was \$4.7 million.

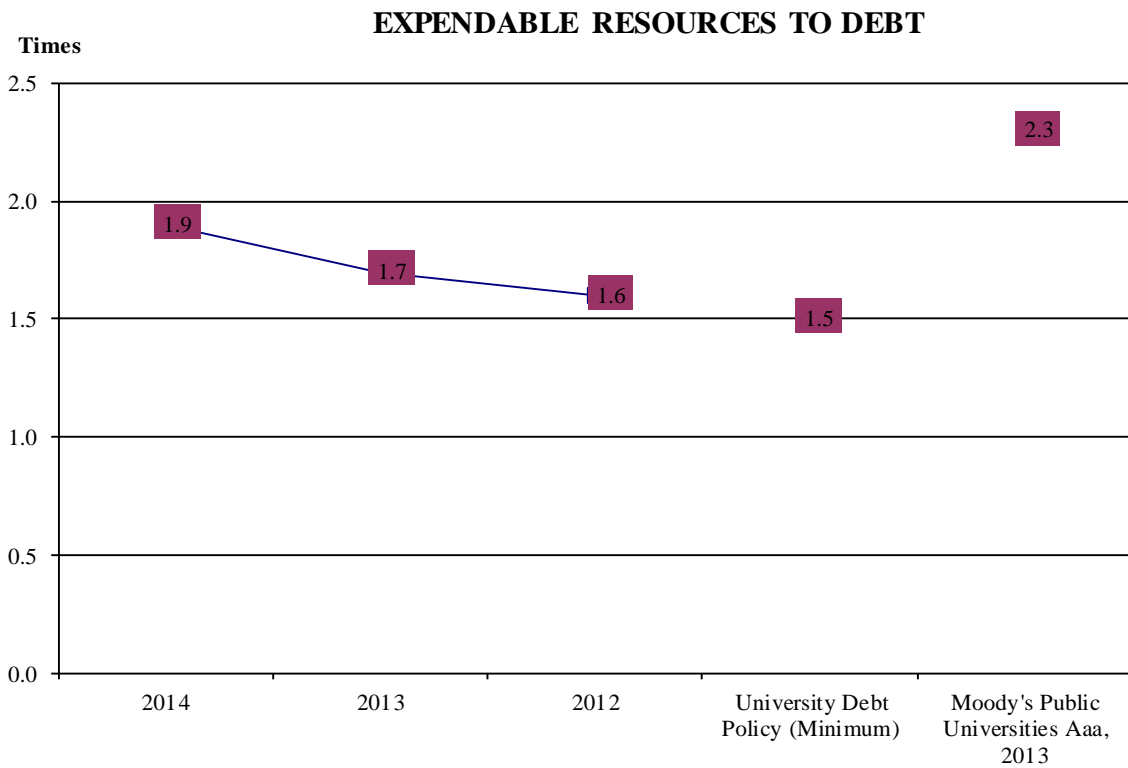
The University maintains a combination of variable and fixed rate debt, consistent with its debt management policy. The interest rate on the commercial paper program for fiscal year 2013-2014 ranged from 0.07 to 0.20% and for fiscal 2012-2013 ranged from 0.13 to 0.23%. Interest rates on the University's variable rate, long-term bonds ranged from 0.02 to 0.88% for fiscal year 2013-2014 and from 0.04 to 0.92% for fiscal year 2012-2013. Interest rates on fixed rate, long-term bonds are disclosed in Note 8B of the financial statements. These rates reflect direct interest rates and do not reflect any impact from the interest rate swaps as referenced in Note 9.

The University's debt policy uses two key ratios to measure debt capacity, financial health, and credit quality. The *expendable resources to debt ratio* measures unrestricted, expendable

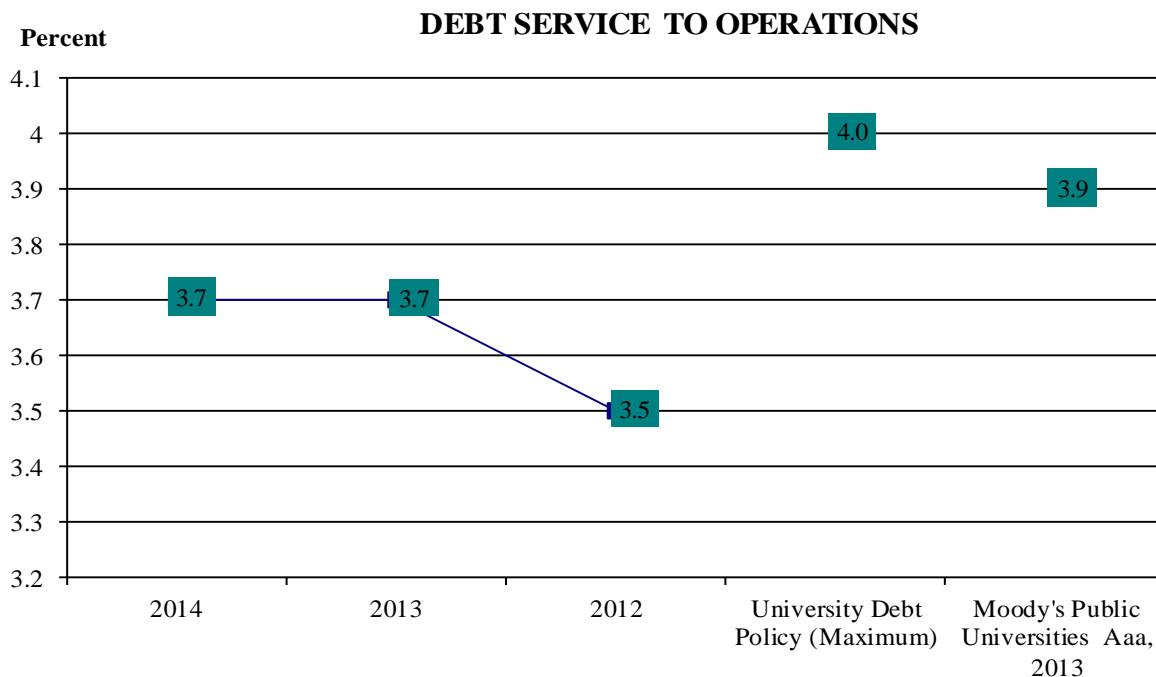
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

restricted, and temporarily restricted net position to funded debt and serves as a relative indicator of financial health or cushion. The *debt service to operations ratio* provides an indicator of the University's ability to repay annual principal and interest relative to its overall operating expenses. Each ratio is compared to the University's debt policy standard and the appropriate peer group comparison for fiscal year 2012-2013 (the latest available comparative statistics). At June 30, 2014, the *expendable resources to debt ratio* was 1.9 times, and the *debt service to operations ratio* was 3.7%.

The University continues to maintain its long-term bond ratings of Aaa/AA+/AAA from Moody's Investor Services, Standard & Poor's and Fitch Ratings, respectively.



MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)



OTHER NONCURRENT ASSETS AND LIABILITIES

Other noncurrent assets were \$282.0 million at June 30, 2014 and \$182.6 million at June 30, 2013, a 54.5% increase. Noncurrent restricted cash increased principally due to decrease in foundations' participation in the Temporary Investment Pool, shifting cash to other funds.

Noncurrent liabilities were \$3.5 billion at June 30, 2014 and \$3.2 billion at June 30, 2013, and include funds held in trust for the University's affiliated foundations and other campuses in the UNC System and their affiliates of \$2.0 billion and \$1.7 billion, respectively. These entities are not part of the University's financial reporting entity and are not discretely presented, but the entities do invest in the UNC Investment Fund. The increase in funds held in trust of 18.8% over the prior year resulted from additional participant contributions and net investment gains.

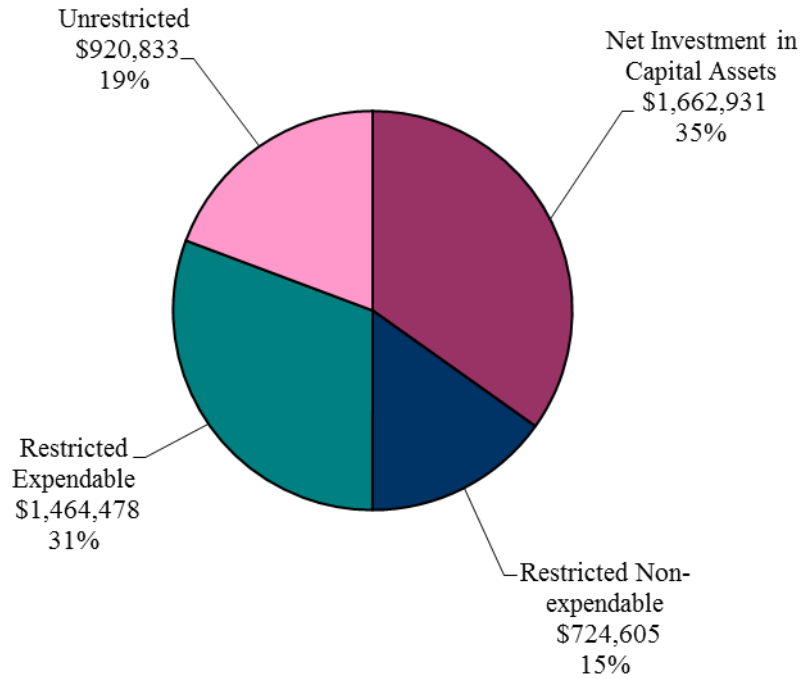
NET POSITION

Net position represents the value of the University's assets and deferred outflows after liabilities and deferred inflows are deducted. The University's net position was \$4.8 billion at June 30, 2014, an increase of \$271.4 million over the prior year. Net investment in capital assets represents the University'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. Nonexpendable restricted net position includes endowment and similar assets whose use is limited by donors or other

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

outside sources and as a condition of the gift, the principal is to be maintained in perpetuity. Expendable restricted net position includes resources in which the University is legally obligated to spend the resources in accordance with restrictions provided by external parties. Unrestricted net position is not subject to externally imposed stipulations; however, most of these resources have been designated for particular academic, research, or other programs, as well as capital projects.

**2014 NET POSITION: \$4,772,847
(IN THOUSANDS)**



MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

CONDENSED STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

The Statements of Revenues, Expenses, and Changes in Net Position present the University's results of operations. The statements for the fiscal year ended June 30, 2014 and the prior year are summarized as follows:

University Operations (dollars in thousands)	2014	2013	Percent Change
Operating Revenues:			
Student Tuition and Fees, Net	\$ 361,771	\$ 348,049	3.9
Grants and Contracts	820,154	761,196	7.7
Sales and Services, Net	770,512	720,520	6.9
Other	3,695	8,929	(58.6)
Total Operating Revenues	1,956,132	1,838,694	6.4
Operating Expenses	2,671,541	2,552,476	4.7
Operating Loss	(715,409)	(713,782)	0.2
Nonoperating Revenues (Expenses):			
State Appropriations	482,728	515,121	(6.3)
Noncapital Gifts and Grants	238,649	250,442	(4.7)
Investment Income, Net	258,372	191,969	34.6
Interest and Fees on Debt	(66,218)	(70,119)	(5.6)
Federal Interest Subsidy on Debt	2,109	2,174	(3.0)
Other Net Nonoperating Expenses	(6,161)	(1,600)	285.1
Net Nonoperating	909,479	887,987	2.4
Income Before Other Revenues	194,070	174,205	11.4
Capital Appropriations	4,313	2,285	88.8
Capital Grants	41,507	44,177	(6.0)
Capital Gifts	5,899	23,182	(74.6)
Additions to Permanent Endowments	25,609	23,954	6.9
Increase in Net Position	271,398	267,803	1.3
Net Position – July 1	4,501,449	4,233,646	6.3
Net Position – June 30	\$ 4,772,847	\$ 4,501,449	6.0

Fiscal year 2013-2014 revenues and other changes total \$3,015,318 and expenses total \$2,743,920.

Fiscal year 2012-2013 revenues and other changes total \$2,891,998 and expenses total \$2,624,195.

OPERATING REVENUES

The operating revenues represent resources generated by the University in fulfilling its instruction, research, and public service missions. Net student tuition and fees for fiscal year 2013-2014 increased 3.9% over the prior year total. Student tuition and fees are reported net of scholarship discounts, which totaled \$96.03 million for fiscal year 2013-2014 and \$84.6 million for the prior year. Tuition rates increased for fiscal year 2013-2014 by 10.3% for undergraduate residents, 6.1% for undergraduate non-residents, 6.5% for graduate residents, and 6.8% for graduate non-residents.

Revenues from operating grants and contracts increased 7.7% over the prior year. Discussion of grants and contracts in terms of awards provides another useful perspective. Faculty secured \$792.7 million in research funding during fiscal year 2013-2014, as compared to \$777.8 million the previous year. The funding comes in contracts and grants awarded by federal and state agencies, foundations, nonprofit organizations, corporations and

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

associations, with the federal government providing the majority of the awards. Securing research funding has become an increasingly competitive endeavor, particularly as the portion of the federal government budget allocable to research is constrained. A key factor in dealing with such competitive pressures is diversifying funding sources and bringing in more awards from foundations and private industry and business.

The National Institutes of Health (NIH) remained the University's largest funding source, with awards exceeding \$428 million. NIH's strong and ongoing support reflects positively on the University's health-related professional schools (dentistry, medicine, nursing, pharmacy and public health), UNC Health Care and its teaching hospitals, and basic and social science units in the College of Arts and Sciences.

The University's other top funders were the National Science Foundation at \$37.4 million; the Department of Health and Human Services, \$22.2 million; and U.S. Agency for International Development, \$21.5 million. The University's multidisciplinary research centers and institutes continue to play a growing role in bringing research funding to North Carolina, accounting for approximately \$141.5 million of total awards in fiscal year 2013-2014, almost 18% of the total \$792.7 million. New, innovative research facilities and infrastructure have made possible groundbreaking interdisciplinary scientific research, which contributes to obtaining research awards.

Sales and services include the revenues of campus auxiliary operations such as student housing, student stores, student health services, the utilities system, and parking and transportation, as well as revenues from patient services provided by the professional health-care clinics. Other revenues represent operating resources not separately identified and include, for example, an assessment to the Chapel Hill Investment Fund to support University administrative services.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

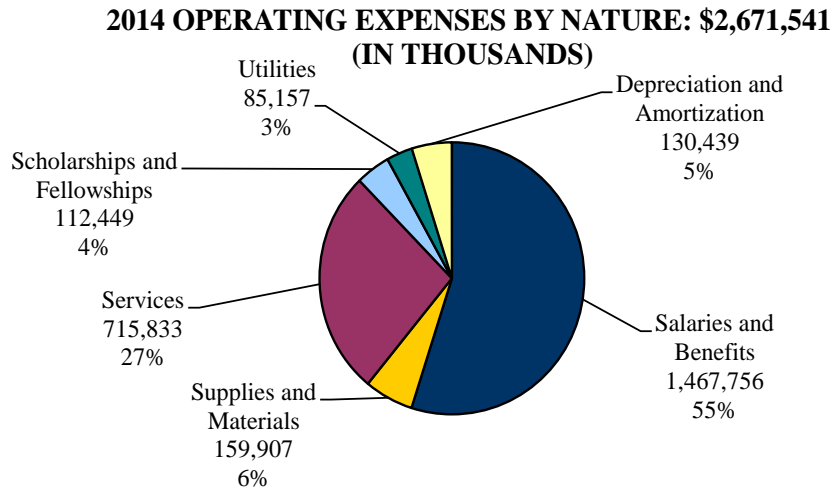
OPERATING EXPENSES

The University's operating expenses were \$2.7 billion for the fiscal year ended June 30, 2014, an increase of 4.7% over the prior year. The operating expenses are reported by natural classification in the financial statements and by functional classification in Note 12. The following tables illustrate the University's operating expenses by natural classification and by functional classification.

Operating Expenses by Nature (dollars in thousands)			
	2014	2013	Percent Change
Salaries and Benefits	\$ 1,467,756	\$ 1,435,472	2.2
Supplies and Materials	159,907	160,698	(0.5)
Services	715,833	650,516	10.0
Scholarships and Fellowships	112,449	104,557	7.5
Utilities	85,157	83,265	2.3
Depreciation and Amortization	130,439	117,968	10.6
Total Operating Expenses	\$ 2,671,541	\$ 2,552,476	4.7

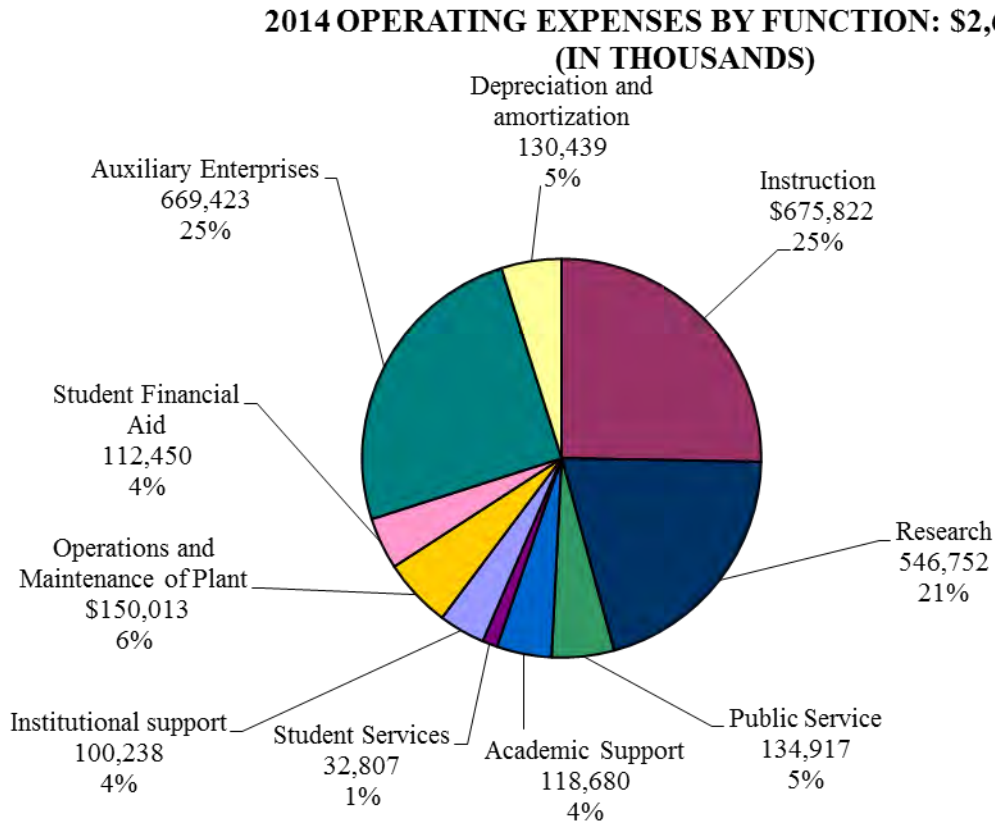
Operating Expenses by Function (dollars in thousands)			
	2014	2013	Percent Change
Instruction	\$ 675,822	\$ 694,692	(2.7)
Research	546,752	529,102	3.3
Public Service	134,917	133,059	1.4
Academic Support	118,680	114,371	3.8
Student Services	32,807	27,565	19.0
Institutional Support	100,238	93,852	6.8
Operations and Maintenance of Plant	150,013	135,314	10.9
Student Financial Aid	112,450	104,557	7.5
Auxiliary Enterprises	669,423	601,996	11.2
Depreciation and Amortization	130,439	117,968	10.6
Total Operating Expenses	\$ 2,671,541	\$ 2,552,476	4.7

The following graph illustrates the University's operating expenses by natural classification.



MANAGEMENT’S DISCUSSION AND ANALYSIS (CONTINUED)

The following graph illustrates the University’s operating expenses by function.



Operating expense categories changed at varying rates, although the overall rate of increase was 4.7%. Depreciation and amortization incurred the highest increase of 10.6%, followed by expenses for services and scholarships and fellowships at 10.0% and 7.5%, respectively. The other operating expense categories by natural classification incurred minimal changes. Operating expenses by functional classification recorded the same increases for depreciation and amortization and for student financial aid as the natural classification categories previously noted. For the other functional classifications, student services recorded the highest increase, 19.0% over the prior year.

NONOPERATING REVENUES AND EXPENSES

State appropriations, noncapital gifts and grants, and investment income are considered nonoperating because they were not generated by the University’s principal, ongoing operations. For example, state appropriations were not generated by the University but were provided to help fund operating expenses.

State appropriations totaled \$482.7 million for fiscal year 2013-2014, a net decrease of 6.3%, or \$32.4 million, from the state appropriations of \$515.1 million received during the prior year. The appropriations for fiscal 2013-2014 reflected a \$15 million reduction to the School

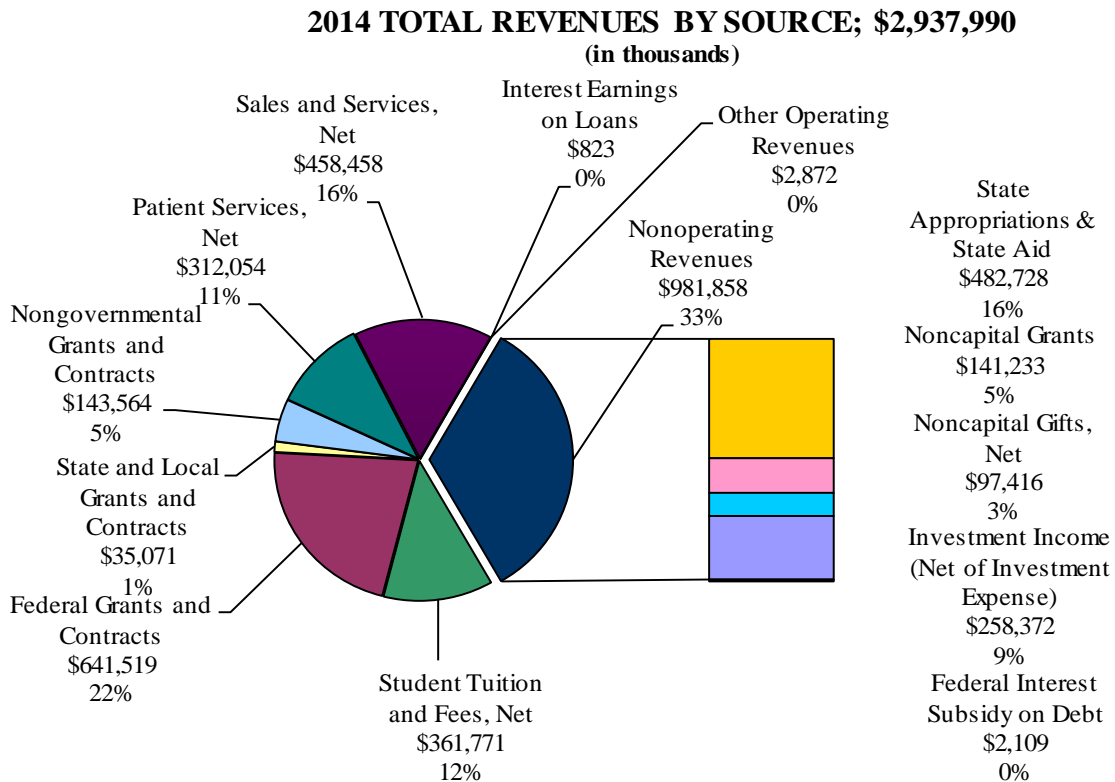
MANAGEMENT’S DISCUSSION AND ANALYSIS (CONTINUED)

of Medicine along with \$21 million campus-wide decline absorbed by postponed strategic and operational initiatives. Partially offsetting increases of \$6.5 million for operating new buildings and \$1.5 million for student enrollment growth along with various other less significant individual adjustments aggregated to the overall net decline for the year.

Noncapital gifts and grants decreased 4.7% to \$238.6 million and include expendable gifts and federal and other awards that are not considered to be operating revenues. Investment income for fiscal year 2013-2014 was \$258.4 million, an increase of 34.6% from the prior year. Investment income includes income and realized and unrealized gains, net of investment management fees.

TOTAL OPERATING AND NONOPERATING REVENUES

Operating and nonoperating revenues such as state appropriations, noncapital grants, noncapital gifts, and investment income are used to fund University operations. The following chart illustrates the University’s operating and nonoperating revenues, which total \$2.9 billion for fiscal year 2013-14.



OTHER CHANGES IN NET POSITION

Capital grants of \$41.5 million for fiscal year 2013-2014 and \$44.2 million for fiscal year 2012-2013 are for capital construction projects. Capital gifts of \$5.9 million for fiscal year 2013-2014 and \$23.2 million for the prior year include funding for construction projects

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)

and contributed improvements to facilities. Nonexpendable gifts and funds from the State's program to match gifts for distinguished professorship endowments resulted in additions to permanent endowments of \$25.6 million during fiscal year 2013-2014 and \$24.0 million during fiscal year 2012-2013.

ECONOMIC OUTLOOK

The University's state appropriations budget for fiscal year 2014-2015 is \$490.5 million, a net increase of \$7.8 million from the prior year, essentially stabilizing after recent significant reductions that have been challenging to ensure did not materially negatively impact the University's core mission.

Tuition rates for fiscal year 2014-2015 for undergraduate residents remained stable, and increased 11.7% for undergraduate non-residents, 4.2% for graduate residents, and 1.4% for graduate non-residents. The University continues to return a portion of tuition revenue to students in the form of need based aid and continues to provide 100% of documented need based aid to students.

Consistency and growth in sponsored awards is a proven and reliable source in support of the University's research mission. Philanthropic efforts continue to demonstrate success. Invested endowment funds provide an important distribution of earnings in support of the University's operating budget. The University's strong debt credit ratings of Aaa, AA+, and AAA allow it to obtain competitive financing for capital construction.

Fundraising has been a cornerstone resource for the University. Fiscal year 2013-2014 marked another strong fundraising year, the second best in University history, with a total of \$297.5 million in private gifts and grants, over a 9% increase compared to the prior fiscal year.

The University's investment management operation is separately organized as the UNC Management Company, Inc. (Management Company), the nonprofit corporation organized and operated as a 501(c)(3) entity, to provide investment management services and administrative services to the University and to the other campuses of the UNC System and their affiliated nonprofit foundations as appropriate. As of June 30, 2014, the Management Company managed invested assets of \$4.2 billion in the UNC Investment Fund.

The University of North Carolina at Chapel Hill
Statement of Net Position
June 30, 2014

Exhibit A-1
Page 1 of 2

ASSETS

Current Assets:	
Cash and Cash Equivalents	\$ 41,779,972
Restricted Cash and Cash Equivalents	427,804,306
Short-Term Investments	682,104,783
Restricted Short-Term Investments	201,630,037
Receivables, Net (Note 4)	293,749,498
Due from State of North Carolina Component Units	22,009,984
Inventories	23,783,217
Notes Receivable, Net (Note 4)	4,200,091
Other Assets	252,528
	<hr/>
Total Current Assets	1,697,314,416
	<hr/>
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	228,049,004
Receivables, Net (Note 4)	13,839,674
Restricted Due from Primary Government	327,656
Endowment Investments	1,701,042,103
Restricted Investments	1,846,015,944
Other Investments	27,650,514
Notes Receivable, Net (Note 4)	31,501,325
Investment In Joint Venture (Note 18)	8,318,917
Capital Assets - Nondepreciable (Note 5)	261,149,873
Capital Assets - Depreciable, Net (Note 5)	2,855,979,488
	<hr/>
Total Noncurrent Assets	6,973,874,498
	<hr/>
Total Assets	8,671,188,914
	<hr/>

DEFERRED OUTFLOWS OF RESOURCES

Deferred Loss on Refunding	1,676,332
Accumulated Decrease in Fair Value of Hedging Derivatives	83,190,081
	<hr/>
Total Deferred Outflows of Resources	84,866,413
	<hr/>

LIABILITIES

Current Liabilities:	
Accounts Payable and Accrued Liabilities (Note 6)	117,183,293
Due to Primary Government	4,409
Due to State of North Carolina Component Units	27,494,148
Deposits Payable	4,548,142
Funds Held for Others	91,505,631
Unearned Revenue	36,066,600
Interest Payable	12,675,557
Short-Term Debt (Note 7)	18,000,000
Long-Term Liabilities - Current Portion (Note 8)	130,383,639
	<hr/>
Total Current Liabilities	437,861,419
	<hr/>

The University of North Carolina at Chapel Hill
Statement of Net Position
June 30, 2014

Exhibit A-1
Page 2 of 2

Noncurrent Liabilities:	
U. S. Government Grants Refundable	31,180,116
Funds Held in Trust for Pool Participants	1,973,239,781
Hedging Derivative Liability (Note 9)	83,190,081
Long-Term Liabilities, Net (Note 8)	1,457,737,081
	<hr/>
Total Noncurrent Liabilities	3,545,347,059
	<hr/>
Total Liabilities	3,983,208,478
	<hr/>
DEFERRED INFLOWS OF RESOURCES	
Total Deferred Inflows of Resources	0
	<hr/>
NET POSITION	
Net Investment in Capital Assets	1,662,931,222
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	157,705,575
Research	19,708,735
Endowed Professorships	334,311,889
Departmental Uses	130,565,006
Loans	20,909,301
Library Acquisitions	31,361,277
Other	30,042,769
Expendable:	
Scholarships and Fellowships	238,069,838
Research	94,369,077
Endowed Professorships	431,223,609
Departmental Uses	409,311,578
Instruction and Educational Agreements	920,709
Plant Improvements	26,600,714
Capital Projects	127,289,735
Debt Service	76,933,465
Library Acquisitions	59,758,853
Unrestricted	920,833,497
	<hr/>
Total Net Position	<u>\$ 4,772,846,849</u>

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

***The University of North Carolina at Chapel Hill
Statement of Revenues, Expenses, and
Changes in Net Position
For the Fiscal Year Ended June 30, 2014***

Exhibit A-2

REVENUES

Operating Revenues:

Student Tuition and Fees, Net (Note 11)	\$ 361,770,560
Patient Services, Net (Note 11)	312,054,448
Federal Grants and Contracts	641,518,512
State and Local Grants and Contracts	35,071,213
Nongovernmental Grants and Contracts	143,564,204
Sales and Services, Net (Note 11)	458,458,394
Interest Earnings on Loans	822,910
Other Operating Revenues	2,871,956

Total Operating Revenues	1,956,132,197
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EXPENSES

Operating Expenses:

Salaries and Benefits	1,467,756,494
Supplies and Materials	159,906,582
Services	715,832,709
Scholarships and Fellowships	112,449,587
Utilities	85,156,899
Depreciation/Amortization	130,438,445

Total Operating Expenses	2,671,540,716
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Operating Loss	(715,408,519)
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NONOPERATING REVENUES (EXPENSES)

State Appropriations	482,727,867
Noncapital Grants - Student Financial Aid	18,621,786
Other Noncapital Grants	122,610,959
Noncapital Gifts, Net (Note 11)	97,416,148
Investment Income (Net of Investment Expense of \$4,894,702)	258,372,237
Interest and Fees on Debt	(66,217,726)
Federal Interest Subsidy on Debt	2,109,311
Other Nonoperating Expenses	(6,161,644)

Net Nonoperating Revenues	909,478,938
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Income Before Other Revenues	194,070,419
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Capital Appropriations	4,313,326
Capital Grants	41,506,762
Capital Gifts	5,898,596
Additions to Endowments	25,608,504

Increase in Net Position	271,397,607
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NET POSITION

Net Position - July 1, 2013	4,501,449,242
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Net Position - June 30, 2014	\$ 4,772,846,849
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The accompanying notes to the financial statements are an integral part of this statement.

The University of North Carolina at Chapel Hill
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2014

Exhibit A-3

Page 1 of 2

CASH FLOWS FROM OPERATING ACTIVITIES

Received from Customers	\$ 1,857,863,611
Payments to Employees and Fringe Benefits	(1,455,707,818)
Payments to Vendors and Suppliers	(952,271,422)
Payments for Scholarships and Fellowships	(112,449,587)
Loans Issued	(6,355,052)
Collection of Loans	5,869,711
Interest Earned on Loans	767,178
Other Receipts	7,992,826
	<hr/>
Net Cash Used by Operating Activities	(654,290,553)

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

State Appropriations	482,727,867
Noncapital Grants - Student Financial Aid	18,621,786
Other Noncapital Grants	122,610,959
Noncapital Gifts	99,249,901
Additions to Endowments	25,608,504
William D. Ford Direct Lending Receipts	174,258,609
William D. Ford Direct Lending Disbursements	(170,498,025)
Related Activity Agency Receipts	722,062,881
Related Activity Agency Disbursements	(451,015,627)
Receipts from UNC Health Care System for School of Medicine	15,400,040
	<hr/>
Net Cash Provided by Noncapital Financing Activities	1,039,026,895

CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES

Proceeds from Capital Debt	4,705,000
Capital Appropriations	4,313,326
Capital Grants	43,919,188
Capital Gifts	680,085
Acquisition and Construction of Capital Assets	(136,583,340)
Principal Paid on Capital Debt and Leases	(15,065,885)
Interest and Fees Paid on Capital Debt and Leases	(72,030,658)
Federal Interest Subsidy on Debt Received	2,109,311
	<hr/>
Net Cash Used by Capital Financing and Related Financing Activities	(167,952,973)

CASH FLOWS FROM INVESTING ACTIVITIES

Proceeds from Sales and Maturities of Investments	3,443,758,282
Investment Income	114,573,403
Purchase of Investments and Related Fees	(4,149,192,321)
	<hr/>
Net Cash Used by Investing Activities	(590,860,636)
	<hr/>
Net Decrease in Cash and Cash Equivalents	(374,077,267)
Cash and Cash Equivalents - July 1, 2013	1,071,710,549
	<hr/>
Cash and Cash Equivalents - June 30, 2014	\$ 697,633,282

***The University of North Carolina at Chapel Hill
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2014***

Exhibit A-3

Page 2 of 2

**RECONCILIATION OF NET OPERATING LOSS
TO NET CASH USED BY OPERATING ACTIVITIES**

Operating Loss	\$	(715,408,519)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:		
Depreciation/ Amortization Expense		130,438,445
Allowances, Write-Offs, and Amortizations		6,382,113
Changes in Assets and Liabilities:		
Receivables, Net		(89,097,394)
Inventories		278,080
Notes Receivable, Net		(478,352)
Accounts Payable and Accrued Liabilities		8,829,417
Due to Primary Government		(1,462)
U.S. Government Grants Refundable		46,728
Unearned Revenue		(464,905)
Compensated Absences		4,956,333
Other Assets		228,963
		<hr/>
Net Cash Used by Operating Activities	\$	<u>(654,290,553)</u>

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	\$	41,779,972
Restricted Cash and Cash Equivalents		427,804,306
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		228,049,004
		<hr/>
Total Cash and Cash Equivalents - June 30, 2014	\$	<u>697,633,282</u>

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Assets Acquired through a Gift	\$	5,218,511
Change in Fair Value of Investments		144,090,835
Loss on Disposal of Capital Assets		(6,385,046)
Amortization of Bond Premiums/Discounts		5,474,828

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

The University of North Carolina at Chapel Hill Foundations
Statement of Financial Position
June 30, 2014

Exhibit B-1

	UNC CH Arts and Sciences Foundation, Inc.	The Educational Foundation Scholarship Endowment Trust	The Medical Foundation of North Carolina, Inc.
ASSETS			
Current Assets:			
Cash and Cash Equivalents	\$ 17,753,531	\$ 10,559,908	\$ 58,332,857
Promises To Give, Net	6,559,330	2,407,577	3,047,221
Contributions Receivable From Split-Interest Agreements		3,890,245	
Accounts Receivable	387,043		
Funds Held In Trust	1,461,169		
Other Current Assets			314,128
Total Current Assets	<u>26,161,073</u>	<u>16,857,730</u>	<u>61,694,206</u>
Property and Equipment:			
Capital Assets			
Leasehold Interest - Building	3,750,483		987,600
Furniture and Equipment	594,558		
Vehicle			
Allowance For Depreciation	<u>(1,448,033)</u>		<u>(606,154)</u>
Total Property And Equipment	<u>2,897,008</u>		<u>381,446</u>
Other Assets:			
Investments	185,259,559	202,410,713	185,812,350
Real Estate	199,000		
Promises To Give, Net	5,959,477		4,877,242
Split-Interest Agreements	1,831,200		
Cash Surrender Value Of Life Insurance		1,943,600	
Other Assets			3,883,991
Total Other Assets	<u>193,249,236</u>	<u>204,354,313</u>	<u>194,573,583</u>
Total Assets	<u>222,307,317</u>	<u>221,212,043</u>	<u>256,649,235</u>
LIABILITIES			
Current Liabilities:			
Accounts Payable And Accrued Expenses	135,838		367,545
Annuities Payable		60,023	
Total Current Liabilities	<u>135,838</u>		<u>367,545</u>
Long-Term Liabilities:			
Deferred Revenue			1,703
Charitable Remainder Trusts			35,512
Total Long-Term Liabilities			<u>37,215</u>
Total Liabilities	<u>135,838</u>	<u>60,023</u>	<u>404,760</u>
NET ASSETS			
Unrestricted	36,887,551		9,813,649
Temporarily Restricted	89,482,787	109,618,963	163,592,811
Permanently Restricted	95,801,141	111,533,057	82,838,015
Total Net Assets	<u>\$ 222,171,479</u>	<u>\$ 221,152,020</u>	<u>\$ 256,244,475</u>

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

The University of North Carolina at Chapel Hill Foundations
Statement of Activities
For the Fiscal Year Ended June 30, 2014

Exhibit B-2

	UNC CH Arts and Sciences Foundation, Inc.	The Educational Foundation Scholarship Endowment Trust	The Medical Foundation of North Carolina, Inc.
REVENUES			
Support:			
Contributions	13,296,014	2,309,487	19,500,029
Development Assessment Fee	2,517,439		
Change In Value Of Split-Interest Agreements	58,700		567,915
Contributed Services And Facilities	82,675		1,969,153
Actuarial Adjustment Of Annuities Payable		2,065	
Endowment Investment Return Designated For Current Operations		9,568,515	
Total Support	15,954,828	11,880,067	22,037,097
Revenue:			
Interest and Dividends			2,421,005
Net Unrealized And Realized Gains On Investments	24,834,650	0	24,741,178
Investment Income	1,696,149		
Other Income	(5,616)		1,117,509
Total Revenue	26,525,183	0	28,279,692
Total Support And Revenue	42,480,011	11,880,067	50,316,789
EXPENSES			
Program Services			
Grants	10,069,874		16,773,381
Scholarship Expense Distribution		9,560,990	
Annuity Payments		7,525	
Total Program Services	10,069,874	9,568,515	16,773,381
Supporting Services			
Fundraising Expenses	3,138,585	0	3,474,221
Management, Administrative, and General	1,174,724		1,993,119
Total Supporting Services	4,313,309	0	5,467,340
Total Expenses	14,383,183	9,568,515	22,240,721
Bad Debt Expense	2,270,806		
Total Expenses and Bad Debt Expense	16,653,989	9,568,515	22,240,721
Changes in Nets Assets from Operations	25,826,022	2,311,552	28,076,068
OTHER CHANGES			
Endowment Investment Return in Excess of Amounts Designated for Current Operations		18,501,099	
CHANGES IN NET ASSETS			
Unrestricted	5,141,319		1,485,225
Temporarily Restricted	15,597,871	18,503,164	21,446,953
Permanently Restricted	5,086,832	2,309,487	5,143,890
Total Changes in Net Assets	25,826,022	20,812,651	28,076,068
Net Assets -- Beginning of Year	196,345,457	200,339,369	228,168,407
Net Assets -- End of Year	\$ 222,171,479	\$ 221,152,020	\$ 256,244,475

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

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THE UNIVERSITY OF NORTH CAROLINA AT CHAPEL HILL
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2014

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 University of North Carolina at Chapel Hill (University) is a constituent institution of the multi-campus University of North Carolina System (UNC System), which 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 belonging to the University and its component units. While the Board of Governors of the University of North Carolina System has ultimate responsibility, the Chancellor, the Board of Trustees, and the Board of Trustees of the Endowment Fund have delegated responsibilities for financial accountability of the University's funds. The University's component units are either blended or discretely presented in the University's financial statements. The blended component units, although legally separate, are, in substance, part of the University's operations and, therefore, are reported as if they were part of the University. Discretely presented component units' financial data are reported in separate financial statements because of their use of different GAAP reporting models and to emphasize their legal separateness.

Blended Component Units - Although legally separate, The University of North Carolina at Chapel Hill Foundation Investment Fund, Inc. (Chapel Hill Investment Fund), UNC Investment Fund, LLC (UNC Investment Fund), UNC Intermediate Pool, LLC (UNC Intermediate Fund), UNC Management Company, Inc. (Management Company), The University of North Carolina at Chapel Hill Foundation, Inc. (UNC-Chapel Hill Foundation), The Kenan-Flagler Business School Foundation (Business School Foundation), U.N.C. Law Foundation, Inc. (Law Foundation), and The University of North Carolina at Chapel Hill School of Education Foundation, Inc. (School of Education Foundation), component units of the University, are reported as if they were part of the University.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The Chapel Hill Investment Fund is governed by a board consisting of eight to eleven ex-officio directors and two to four elected directors. Ex-officio directors include all of the members of the Board of Trustees of the Endowment Fund of the University, which includes the Chair of the University Board of Trustees and the Chancellor, the Vice Chancellor for Finance and Administration, and the Vice Chancellor for University Advancement. The UNC-Chapel Hill Foundation Board may, in its discretion, elect one or two of its at-large members to the Chapel Hill Investment Fund Board. The ex-officio directors of the Chapel Hill Investment Fund may elect one or two directors by unanimous written consent. The Chapel Hill Investment Fund supports the University by operating an investment fund for certain eligible charitable, non-profit foundations, associations, trusts, endowments, and funds that are organized and operated primarily to support the University. Because members of the Board of Directors of the Chapel Hill Investment Fund are officials or appointed by officials of the University and the Chapel Hill Investment Fund's primary purpose is to benefit the University and other organizations operated primarily to support the University, its financial statements have been blended with those of the University.

The UNC Investment Fund was organized by the Chapel Hill Investment Fund to allow the University, the UNC System, other constituent institutions of the UNC System, and certain eligible affiliated foundations, associations, trusts, and endowments that support the University and the UNC System, to pool their resources and invest collectively in investment opportunities identified, structured and managed by the Management Company. The membership interests are offered only to eligible government entities or tax-exempt organizations that are controlled by or support the University, the UNC System, or other constituent institutions of the UNC System. The Chapel Hill Investment Fund contributed and assigned all of its assets to the UNC Investment Fund effective January 1, 2003, in exchange for its membership interest in the UNC Investment Fund. Upon such contribution and assignment, and in consideration thereof, the UNC Investment Fund has assumed all liabilities and obligations of the Chapel Hill Investment Fund in respect of such contributed assets. At June 30, 2014, the Chapel Hill Investment Fund membership interest was approximately 64% of the UNC Investment Fund total membership interests. Because the Chapel Hill Investment Fund is the organizer and controlling member of the UNC Investment Fund, the financial statements of the UNC Investment Fund have been blended with those of the University.

The UNC Intermediate Fund was organized by the University to make available an intermediate-term investment fund for eligible participants. The University is the controlling member. Eligible participants in the fund include not only the University but also the UNC System, its

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

constituent institutions, and/or affiliates and supporting organizations of the UNC System or such constituent institutions. The University has retained the Management Company to serve as the investment manager of the fund. Because the University is the organizer and controlling member of the UNC Intermediate Fund, the financial statements of the UNC Intermediate Fund have been blended with those of the University.

The Management Company is a North Carolina nonprofit corporation organized and operated exclusively to support the educational mission of the University. The Management Company provides investment management and administrative services to the University, UNC System, and institutions and affiliated tax exempt organizations, and performs other functions for and generally carries out the purposes of the University. The Management Company is governed by five ex-officio directors and one to three additional directors as fixed or changed from time to time by the board, elected by the ex-officio directors. The ex-officio directors consist of the Chancellor, the Vice Chancellor for Finance and Administration, the Chair of the University Board of Trustees, the Chair of the Board of Directors of the Chapel Hill Investment Fund, and the President of the Management Company. Because members of the Board of Directors of the Management Company are officials or appointed by officials of the University and the Management Company's primary purpose is to benefit the University and other organizations operated primarily to support the University, its financial statements have been blended with those of the University.

The UNC-Chapel Hill Foundation is governed by a 17-member board consisting of nine ex-officio directors and eight elected directors. Ex-officio directors include the Chair of the University Board of Trustees, the Chancellor, the Vice Chancellor for Finance and Administration, and the Vice Chancellor for University Advancement (non-voting). In addition, the Board of Trustees elects two ex-officio directors from among its own members as well as three ex-officio directors from the Board of Trustees of the Endowment Fund who have not otherwise been selected. The eight remaining directors are elected as members of the UNC-Chapel Hill Foundation Board of Directors by action of the ex-officio directors. The UNC-Chapel Hill Foundation aids, supports, and promotes teaching, research, and service in the various educational, scientific, scholarly, professional, artistic, and creative endeavors of the University. Because members of the Board of Directors of the UNC-Chapel Hill Foundation are officials or appointed by officials of the University and the UNC-Chapel Hill Foundation's sole purpose is to benefit the University, its financial statements have been blended with those of the University.

The Business School Foundation is governed by a board consisting of four ex-officio directors and four or more elected directors. Ex-officio

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

directors include the Dean of the Kenan-Flagler Business School (Business School), as well as the school's Chief Financial Officer, Associate Dean of Academic Affairs, and Associate Dean for MBA Programs. The remaining directors are elected to the Business School Foundation Board of Directors by action of the ex-officio directors. The Business School Foundation aids, promotes, and supports the Kenan-Flagler Business School at the University. Because members of the Board of Directors of the Business School Foundation are officials or appointed by officials of the University, the financial statements of the Business School Foundation have been blended with those of the University.

The Law Foundation is governed by a board consisting of one ex-officio director, six appointed directors, and six elected directors. The ex-officio director is the Dean of the School of Law of the University. The ex-officio director appoints six directors and the Board of Directors of the Law Alumni Association of UNC, Inc. elects the other six directors. The Law Foundation provides support, fosters, and encourages the study and teaching of law at the University's Law School. Because a majority of the members of the Board of Directors of the Law Foundation are officials or appointed by officials of the University, the financial statements of the Law Foundation have been blended with those of the University.

The School of Education Foundation is governed by a board consisting of seven ex-officio directors and up to 15 elected directors. Ex-officio directors include the Dean of the School of Education, as well as the school's Associate Dean for Academic Programs, Assistant Dean for External Relations, Assistant Dean for Administration and Finance, Director of Alumni Relations, President of the Alumni Council, and President-Elect of the Alumni Council. The remaining directors are elected to the School of Education Foundation Board of Directors by action of the ex-officio directors. The School of Education Foundation aids, supports and promotes teaching, research, and service at the School of Education. Because members of the Board of Directors of the School of Education Foundation are officials or appointed by officials of the University, the financial statements of the School of Education Foundation have been blended with those of the University.

Separate financial statements for the Chapel Hill Investment Fund, UNC Investment Fund, UNC Intermediate Fund, the Management Company, and blended foundations may be obtained from the University Controller's Office, Campus Box 1270, Chapel Hill, NC 27599-1270, or by calling (919) 962-1370.

Condensed combining information regarding blended component units is provided in Note 19.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Discretely Presented Component Units – The Medical Foundation of North Carolina, Inc. (Medical Foundation), The University of North Carolina at Chapel Hill Arts and Sciences Foundation, Inc. (Arts and Sciences Foundation), and The Educational Foundation Scholarship Endowment Trust (Educational Foundation Trust) are legally separate, nonprofit, tax exempt organizations and are reported as discretely presented component units based on the nature and significance of their relationship to the University.

The Medical Foundation is governed by a board consisting of one ex-officio director, the Dean of the UNC School of Medicine, and up to 33 elected directors, which serve staggered terms. Two other ex-officio directors, the President of UNC Health Care and the President of the Medical Foundation, have no voting rights on any matters. Its purpose is to support educational, scientific, and public service efforts of the University's School of Medicine and UNC Health Care System. Historically, the University's School of Medicine has been the major recipient of financial support from the Medical Foundation rather than UNC Health Care System. Although the University does not control the timing or amount of receipts from the Medical Foundation, the majority of resources or income that the Medical Foundation holds and invests is restricted to the University by the donors. Because these restricted resources held by the Medical Foundation can only be used by, or for the benefit of the University, the Medical Foundation is considered a component unit of the University.

The Arts and Sciences Foundation is governed by a board consisting of five ex-officio directors, 30 elected directors and such number of emeritus directors determined from time to time by the Board of Directors. The 30 elected directors are elected for staggered terms by the Board of Directors in office at the time of election. The purpose of the Arts and Sciences Foundation is to promote and support the University's College of Arts and Sciences. Although the University does not control the timing or amount of receipts from the Arts and Sciences Foundation, the majority of resources or income that the Arts and Sciences Foundation holds and invests is restricted to the activities of the University by the donors. Because these restricted resources held by the Arts and Sciences Foundation can only be used by, or for the benefit of the University, the Arts and Sciences Foundation is considered a component unit of the University.

The Educational Foundation Trust is governed by The Educational Foundation Scholarship Endowment Trust Agreement which designates the voting members of the Investment Committee of The Educational Foundation, Inc. as trustees. The Investment Committee consists of five members elected from the membership of The Educational

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Foundation, Inc. The Educational Foundation Trust operates solely to assist the University in providing financial assistance to students at the University. On an annual basis, the Board of Trustees of the Educational Foundation Trust appropriates a portion of the net appreciation on its assets to The Educational Foundation, Inc. in its capacity as agent for the Educational Foundation Trust. The distribution from the Educational Foundation Trust to The Educational Foundation, Inc. is then forwarded by The Educational Foundation, Inc. to the University to provide financial assistance to students at the University. Although the University does not control the timing or amount of receipts from the Educational Foundation Trust, the majority of resources or income that the Educational Foundation Trust holds and invests is restricted to the students of the University by the donors. Because these restricted resources held by the Educational Foundation Trust can only be used for the benefit of the students of the University, the Educational Foundation Trust is considered a component unit of the University.

The Medical Foundation, the Arts and Sciences Foundation, and the Educational Foundation Trust are private, nonprofit organizations that report their financial results under Financial Accounting Standards Board (FASB) Statements. As such, certain revenue recognition criteria and presentation features are different from Governmental Accounting Standards Board (GASB) revenue recognition criteria and presentation features. No modifications have been made to the financial information in the University's financial reporting entity for these differences.

During the year ended June 30, 2014, the Medical Foundation, the Arts and Sciences Foundation, and the Educational Foundation Trust distributed in total \$36,404,245 to the University for both restricted and unrestricted purposes. Complete financial statements for the Medical Foundation, Arts and Sciences Foundation, and Educational Foundation Trust can be obtained from the University Controller's Office, Campus Box 1270, Chapel Hill, NC 27599-1270, or by calling (919) 962-1370.

Other related foundations and similar nonprofit corporations for which the University is not financially accountable 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 GASB.

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Public Colleges and Universities, the full scope of the University'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 University 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 University receives (or gives) value without directly giving (or receiving) equal value in exchange includes state appropriations, certain grants, and donations. 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 are generally reported at fair value. The fair values of all debt and equity securities with readily determinable fair market values are based on quoted market prices. Investments for which a readily determinable fair value does not exist include investments in certain commingled funds and limited partnerships. These investments are carried at estimated fair values as provided by the respective fund managers of these investments or third party administrators. The Management Company reviews and evaluates the values provided by the fund managers as well as the valuation methods and assumptions used in determining the fair value of such investments. Those estimated fair values may differ significantly from the values that would have been used had a ready market for these investments existed. The net increase or decrease in the fair value of investments is recognized as a component of investment income. The majority of private equity limited partnerships and real assets limited partnerships are subject to fair value estimation, which includes discounted cash flow and transaction comparison. The estimated fair value of these investments is \$1.42 billion.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Money market funds, real estate not held by a governmental external investment pool, and other asset holdings are reported at cost, if purchased, or at fair value or appraised value at date of gift, if donated.

Short-term investments include marketable securities representing the investment of cash that is available for current operations. A majority of this available cash is invested in the University's Temporary Pool, a governmental external investment pool.

Endowment investments include the principal amount of gifts and bequests that, according to donor restrictions, must be held in perpetuity, along with any accumulated investment earnings on such amounts. Further, endowment investments also include amounts internally designated by the University for investment in an endowment capacity (i.e., quasi-endowments), along with accumulated investment earnings on such amounts. Land and other real estate held as investments by endowments are reported at fair value, consistent with how investments are generally reported.

- F. Receivables** – Receivables consist of tuition and fees charged to students and charges to patients for services provided by the UNC Faculty Physicians and the Dental Faculty Practices. Receivables also include amounts due from the federal government, state and local governments, private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants, pledges that are verifiable, measurable, and expected to be collected and available for expenditures for which the resource provider's conditions have been satisfied, and notes receivable from loans to students. Student, patient, pledges, and notes receivable are recorded net of the allowance for doubtful accounts. The accounts and other receivables are shown at book value with no provision for doubtful accounts considered necessary.
- G. Inventories** – Inventories held by the University are priced at cost or average cost except for the Student Stores inventory, which is valued at the lower of cost or market. Inventories consist of expendable supplies, postage, fuel held for consumption, textbooks, and other merchandise for resale.
- H. 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 University capitalizes assets that have a value or cost in excess of \$5,000 at the date of acquisition and an expected useful life of more than one year except for intangible assets which are capitalized when the value

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

or cost is \$100,000 or greater and internally generated software which is capitalized when the value or cost is \$1,000,000 or greater.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 10 to 75 years for general infrastructure, 12 to 75 years for buildings, and 3 to 30 years for equipment. Amortization is computed using the straight-line method over the estimated useful lives of the assets, from 3 to 20 years for computer software.

The University's historic property, artworks, and literary collections are capitalized at cost or fair value at the date of donation. These properties and collections are considered inexhaustible and are therefore not depreciated.

- I. 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 and resources legally segregated for the payment of principal and interest as required by debt covenants, unspent debt proceeds, and endowment and other restricted investments.
- J. Funds Held in Trust for Pool Participants** – Funds held in trust for pool participants represent the external portion of the University's governmental external investment pools more fully described in Note 2. The assets associated with this liability are included in restricted investments, cash, and other similar asset accounts.
- K. Funds Held in Trust by Others** – Funds held in trust by others are resources neither in the possession nor the control of the University, but held and administered by an outside organization, with the University deriving income from such funds. Such funds established under irrevocable trusts where the University has legally enforceable rights or claims have not been recorded on the accompanying financial statements. The value of these assets at June 30, 2014 is \$33,846,331.
- L. Noncurrent Long-Term Liabilities** – Noncurrent long-term liabilities include principal amounts of revenue bonds payable, notes payable, capital lease obligations, annuity and life income payable, and compensated absences that are not scheduled to be paid within the next fiscal year.

Revenue bonds payable are reported net of unamortized premiums or discounts. The University amortizes bond premiums/discounts over the life of the bonds using the straight-line method. The deferred charges on

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

refundings are amortized over the life of the old debt or new debt (whichever is shorter) using the straight-line method, and are included as Deferred Outflows or Deferred Inflows of Resources on the Statement of Net Position. Issuance costs are expensed.

- M. Compensated Absences** - The University'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. 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.

In addition to the vacation leave described above, compensated absences include the accumulated unused portion of the special annual leave bonuses awarded by the North Carolina General Assembly. The bonus leave balance on December 31 is retained by employees and transferred into the next calendar year. It is not subject to the limitation on annual leave carried forward described above and is not subject to conversion to sick leave.

When classifying compensated absences into current and noncurrent, leave is considered taken using a last-in, first-out (LIFO) method.

There is no liability for unpaid accumulated sick leave because the University 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 University's net position is classified as follows:

Net Investment in Capital Assets – This represents the University'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 or related debt are also included in this component of net position.

Restricted Net Position – Nonexpendable – Nonexpendable restricted net position includes endowments and similar type assets whose use is limited by donors or other outside sources, and, as a condition of the gift, the principal is to be maintained in perpetuity.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Restricted Net Position – Expendable – Expendable restricted net position includes resources for which the University 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 student tuition and fees, sales and services, unrestricted gifts, royalties, and interest income.

Restricted and unrestricted resources are tracked using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. When both restricted and unrestricted funds are available for expenditure, the decision for funding is transactional based within the departmental management system in place at the University. For projects funded by tax exempt debt proceeds and other sources, the debt proceeds are always used first. Both restricted and unrestricted net position includes consideration of deferred inflows and outflows of resources.

- O. Scholarship Discounts** – Student tuition and fees revenues and certain other revenues from University charges are reported net of scholarship discounts in the accompanying Statement of Revenues, Expenses, and Changes in Net Position. The scholarship discount is the difference between the actual charge for goods and services provided by the University and the amount that is paid by students or by third parties on the students' behalf. Student financial assistance grants, such as Pell grants, and other federal, state, or nongovernmental programs, are recorded as nonoperating revenues in the accompanying Statement of Revenues, Expenses, and Changes in Net Position. To the extent that revenues from these programs are used to satisfy tuition, fees, and other charges, the University has recorded a scholarship discount.
- P. Revenue and Expense Recognition** – The University 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 University's principal ongoing operations. Operating revenues include activities that have characteristics of exchange transactions, such as (1) student tuition and fees, (2) sales and services of auxiliary enterprises, (3) certain federal, state and local grants and contracts that are essentially contracts for services, and (4) interest earned on loans. Operating expenses are all expense transactions incurred other than those related to capital and noncapital financing or investing activities as defined by GASB Statement

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 appropriations that represent subsidies or gifts to the University, 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.

- Q. Internal Sales Activities** – Certain institutional auxiliary operations provide goods and services to University departments, as well as to its customers. These institutional auxiliary operations include activities such as utility services, telecommunications, central stores, printing and copy centers, postal services, and repairs and maintenance services. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

NOTE 2 - DEPOSITS AND INVESTMENTS

- A. Deposits** - Unless specifically exempt, the University 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. However, the University of North Carolina Board of Governors, pursuant to G.S. 116-36.1, may authorize the University to deposit its institutional trust funds in interest-bearing accounts and other investments authorized by the Board of Governors, without regard to any statute or rule of law relating to the investment of funds by fiduciaries. Although specifically exempted, the University may voluntarily deposit institutional trust funds, endowment funds, special funds, revenue bond proceeds, debt service funds, and funds received for services rendered by health care professionals with the State Treasurer. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

At June 30, 2014, the amount shown on the Statement of Net Position as cash and cash equivalents includes \$579,344,554 which represents the University's equity position in the State Treasurer's STIF. The STIF

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(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 \$133,907. The carrying amount of the University's deposits not with the State Treasurer was \$118,154,821 and the bank balance was \$94,877,881. Custodial credit risk is the risk that in the event of a bank failure, the University's deposits may not be returned to it. The University does not have a deposit policy for custodial credit risk. As of June 30, 2014, \$92,524,541 of the University's bank balance was exposed to custodial credit risk as uninsured and uncollateralized.

- B. Investments** - The University is authorized by The University of North Carolina Board of Governors pursuant to G.S. 116-36.2 and Section 600.2.4 of the Policy Manual of the University of North Carolina, to invest its special funds and funds received for services rendered by health care professionals 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 obligations of or fully guaranteed by the United States; obligations of certain federal agencies; repurchase agreements; obligations of the State of North Carolina; time deposits of specified institutions; prime quality commercial paper; and asset-backed securities with specified ratings. Also, G.S. 147-69.1(c) authorizes specified bills of exchange or time drafts and corporate bonds and notes with specified ratings. G.S. 147-69.2 authorizes 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

G.S. 116-36(e) provides that the trustees of the Endowment Fund shall be responsible for the prudent investment of the Fund in the exercise of their sound discretion, without regard to any statute or rule of law relating to the investment of funds by fiduciaries but in compliance with any lawful condition placed by the donor upon that part of the Endowment Fund to be invested.

Investments of the University's component units, UNC-Chapel Hill Foundation, Management Company, Chapel Hill Investment Fund, UNC Intermediate Fund, UNC Investment Fund, Business School Foundation, Law Foundation, School of Education Foundation, Medical Foundation, Arts and Sciences Foundation, and Educational Foundation Trust, are subject to and restricted by G.S. 36E "Uniform Prudent Management of Institutional Funds Act" (UPMIFA) and any requirements placed on them by contract or donor agreements. The UNC Management Company does not hold endowment funds.

Investments of various funds may be pooled unless prohibited by statute or by terms of the gift or contract. The University utilizes investment pools to manage investments and distribute investment income.

Investments are subject to the following risks.

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

Foreign Currency Risk: Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The University does not have a formal policy for foreign currency risk.

Temporary Investment Pool (Temporary Pool) – The Temporary Pool is a fixed income portfolio managed by the Management Company and Novant Asset Management, LLC. It operates in conjunction with the University's Bank of America disbursing account for all special funds, funds received for services rendered by health care professionals, and endowment revenue funds (internal portion) and funds of affiliated foundations (external portion). Because of the participation in the Temporary Pool by affiliated foundations, it is considered a governmental external investment pool. The external portion of the Temporary Pool is presented in the accompanying financial statements as Funds Held in Trust for Pool Participants. Fund ownership of the University's Temporary Pool is measured using the unit value method. Under this

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

method, participant activity is recorded on a cost basis in the UNC-Chapel Hill Money Market System. This is the official means of recording activity in the Temporary Pool. The Temporary Pool is not registered with the SEC and is not subject to any formal oversight other than that provided by the University Board of Trustees. The University has not provided legally binding guarantees during the period to support the value of the pool's investments. There are no involuntary participants in the Temporary Pool.

The Bank of New York Mellon is the custodian for the Temporary Pool and provides the University with monthly statements defining income and market value information. Investments of the Temporary Pool are generally highly liquid and include U.S. government securities, collateralized mortgage obligations, asset-backed securities, corporate bonds, and mutual funds. The University has elected to invest a portion of the Temporary Pool assets in the Chapel Hill Investment Fund.

Participants may purchase and sell shares in the Temporary Pool at a fixed value of \$1 per share. Generally, the purchase and sale of participation shares occur only at the beginning of the month. Income distribution is determined each quarter by multiplying the distribution rate by the average of the invested fund balance. Statements are provided via internet website to each participating account or group of accounts on a quarterly basis reflecting the participants' balance and income distribution. The rate earned by an account is dependent upon its account classification and investable fund balance. The rates are set by policy and approved by the Vice Chancellor for Finance and Administration.

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

Temporary Pool Investments

Investment Type	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1 to 5	6 to 10	More than 10
<i>Debt Securities</i>					
U.S. Treasuries	\$ 125,152,800	\$ 40,073,850	\$ 85,078,950	\$ 0	\$ 0
U.S. Agencies	124,280,330	12,717,032	19,512,216	2,670,022	89,381,060
Mortgage Pass Throughs	29,233	29,233			
Collateralized Mortgage Obligations	9,337,973	2,960,574	77,314		6,300,085
Asset-backed Securities	1,007,785	1,007,785			
Money Market Mutual Funds	48,726,939	48,726,939			
Domestic Corporate Bonds	31,189,902	9,718,301	17,376,892	493,505	3,601,204
Total Debt Securities	339,724,962	\$ 115,233,714	\$ 122,045,372	\$ 3,163,527	\$ 99,282,349
<i>Other Securities</i>					
Domestic Stocks	30,000				
Total Temporary Pool Investments	\$ 339,754,962				

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The University has elected to invest \$47,719,183 of the Temporary Pool assets in the UNC Chapel Hill Investment Fund. The disclosures for these investments are not included in the preceding table. Rather, the disclosures for this portion of the Temporary Investment Pool are included in those for UNC Chapel Hill Investment Fund, Inc.

At June 30, 2014, investments in the Temporary Pool had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa	AA Aa	A	BBB Baa	BB, Ba and below	Unrated
U.S. Agencies	\$ 124,280,330	\$ 15,683	\$ 124,264,647	\$ 0	\$ 0	\$ 0	\$ 0
Collateralized Mortgage Obligations	9,337,973					5,175,522	4,162,451
Asset-backed Securities	1,007,786					1,007,786	
Mortgage Pass Throughs	29,233				29,233		
Money Market Mutual Funds	48,726,939	48,726,939					
Domestic Corporate Bonds	31,189,900	4,951,839	10,158,388	15,222,338	493,505	363,830	
Total	\$ 214,572,161	\$ 53,694,461	\$ 134,423,035	\$ 15,222,338	\$ 522,738	\$ 6,547,138	\$ 4,162,451

Rating Agency: Moody's/Standard & Poor's/Fitch (lowest rating reported above)

Since a separate annual financial report of the Temporary Investment Pool is not issued, the following additional disclosures are being provided in the University's financial statements.

The Temporary Investment Pool's Statement of Net Position and Statement of Operations and Changes in Net Position as of and for the period ended June 30, 2014, are as follows:

Statement of Net Position

June 30, 2014

	Amount
Assets:	
State Treasurer Investment Fund	\$ 80,000,000
Accounts Receivable	24
Accrued Investment Income	754,148
Deferred Loss	61,227
Chapel Hill Investment Fund Investments	47,719,183
	<u>339,754,962</u>
Total Assets	\$ 468,289,544
Liabilities:	
Accounts Payable	\$ 2,090,806
Total Liabilities	<u>2,090,806</u>
Net Position As Held in Trust for All Pool Participants:	
Internal Portion	275,675,323
External Portion	190,523,415
Total Net Position	<u>466,198,738</u>
Total Liabilities and Net Position	\$ 468,289,544

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Statement of Operations and Changes in Net Position For the Fiscal Year Ended June 30, 2014

	Amount
<i>Increase in Net Position from Operations:</i>	
Revenues:	
Investment Income	\$ 3,086,064
Expenses:	
Investment Management	(504,058)
Net Increase in Net Position Resulting from Operations	2,582,006
<i>Distributions to Participants:</i>	
Distributions Paid and Payable	(2,582,006)
<i>Share Transactions:</i>	
Net Share Liquidations	(13,931,610)
Total Decrease in Net Position	(13,931,610)
<i>Net Position:</i>	
Beginning of Year	480,130,348
End of Year	<u>\$ 466,198,738</u>

Intermediate Investment Pool (Intermediate Pool) - Established in October 2007, the Intermediate Pool is a portfolio managed by the Management Company, comprised of fixed income investments and investments with the UNC-Chapel Hill Foundation Investment Fund, Inc. (Chapel Hill Investment Fund). Participation in the Intermediate Pool is open to all participants that are eligible for the UNC Chapel Hill Temporary Investment Pool; currently, the University is the only member. Fund ownership of the University's Intermediate Pool is measured using the unit value method. Under this method, each participant's investment balance is determined on a market value basis. The Intermediate Pool is not registered with the SEC and is not subject to any formal oversight other than that provided by the University Board of Trustees. The University has not provided legally binding guarantees during the period to support the value of the pool's investments. There are no involuntary participants in the Intermediate Pool.

The Bank of New York Mellon is the custodian for the Intermediate Pool and provides the University with monthly statements defining income and market value information. Generally a minimum of 45% and a maximum of 65% of the market value of the Intermediate Pool will be invested in the Chapel Hill Investment Fund. The remaining assets of the Intermediate Pool will be invested primarily (at least 80%) in cash, money market instruments, high quality bonds, and other high quality fixed income instruments in accordance with investment guidelines.

Purchase and sale of participation shares occur at the beginning of the month. As calculated by the Management Company, returns net of fees and expenses will be allocated 85% to the Intermediate Pool participants and 15% to the University. Statements are provided by the Management

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Company to each participant on a monthly basis reflecting the participants' balance and investment activity.

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

Intermediate Pool Investments

Investment Type	Fair Value	Investment Maturities (in Years)	
		Less Than 1	1 to 5
<i>Debt Securities</i>			
Debt Mutual Funds	\$ 7,468,132	\$ 0	\$ 7,468,132
Money Market Mutual Funds	6,642,984	6,642,984	
Total Intermediate Pool Investments	\$ 14,111,116	\$ 6,642,984	\$ 7,468,132

At June 30, 2014, investments in the Intermediate Pool had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa	A
Debt Mutual Funds	\$ 7,468,132	\$ 2,393,891	\$ 5,074,241
Money Market Mutual Funds	6,642,984	6,642,984	
Total	\$ 14,111,116	\$ 9,036,875	\$ 5,074,241

Rating Agency: Moody's/Standard & Poor's/Fitch (lowest rating reported above)

At June 30, 2014, the Intermediate Investment Pool had investments of \$19,204,795 in the Chapel Hill Investment Fund. The disclosures for these investments are not included here. The disclosures for this portion of the Intermediate Investment Pool can be found under the heading UNC Chapel Hill Investment Fund, Inc.

UNC Intermediate Pool, LLC (UNC Intermediate Fund) - The UNC Intermediate Fund was organized in May 2013 by the University to make available an intermediate-term investment fund for eligible participants with the University being the controlling member. The Intermediate Pool is classified as a governmental external investment pool. Eligible participants in the fund include not only the University but also the University of North Carolina System (UNC System), its constituent institutions, and/or affiliates and supporting organizations of the UNC System or such constituent institutions. The University has retained the Management Company to serve as the investment manager of the fund.

Fund ownership of the UNC Intermediate Fund is measured using the unit value method. Under this method, each participant's investment balance is

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

determined on a market value basis. The UNC Intermediate Fund is not registered with the SEC and is not subject to any formal oversight beyond that provided by the Management Company as well as an Oversight Committee of University employees appointed by the Chancellor of the University. The University has not provided legally binding guarantees during the period to support the value of the pool's investments. There are no involuntary participants in the Intermediate Fund.

The audited financial statements for the UNC Intermediate Fund may be obtained from the University Controller's Office, Campus Box 1270, Chapel Hill, NC 27599-1270, or by calling (919) 962-1370.

The Bank of New York Mellon is the custodian for the UNC Intermediate Fund and provides the University with monthly statements providing income and market value information. UNC Intermediate Fund investments are comprised of shares in mutual funds, money market accounts, and the UNC Investment Fund.

As of June 30, 2014, the University's membership interest was approximately 98% of the UNC Intermediate Fund's total membership interests. An affiliated organization, not included in the University's reporting entity, held the remaining 2% membership interest. This external portion of the UNC Intermediate Fund is presented in the accompanying financial statements as Funds Held in Trust for Pool Participants.

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

UNC Intermediate Fund Investments

Investment Type	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1 to 5	6 to 10	More than 10
<i>Debt Securities</i>					
U.S. Treasuries	\$ 3,353,101	\$ 0	\$ 3,353,101	\$ 0	\$ 0
U.S. Agencies	1,263,846				1,263,846
Mortgage Pass Throughs	8,679,274	6,575,988			2,103,286
Collateralized Mortgage Obligations	17,994,184	3,902,443		672,593	13,419,148
Asset-backed Securities	16,127,207	16,127,207			
Debt Mutual Funds	200,169,658		11,535,468	188,634,190	
Money Market Mutual Funds	27,494,134	27,494,134			
Domestic Corporate Bonds	11,259,874		5,401,766	5,507,848	350,260
Foreign Corporate Bonds	23,011,852	1,739,920	10,210,625	9,178,600	1,882,707
Foreign Government Bonds	419,000		202,000	217,000	
Total Debt Securities	309,772,130	\$ 55,839,692	\$ 30,702,960	\$ 204,210,231	\$ 19,019,247
<i>Other Securities</i>					
Real Estate Investment Trusts	172,571				
Total UNC Intermediate Fund Investments	\$ 309,944,701				

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

At June 30, 2014, investments in UNC Intermediate Fund had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa	AA Aa	A	BBB Baa	BB, Ba and below	Unrated
U.S. Agencies	\$ 1,263,846	\$ 0	\$ 1,263,846	\$ 0	\$ 0	\$ 0	\$ 0
Collateralized Mortgage Obligations	17,994,183	463,867	863,331	500,606		15,125,637	1,040,742
Asset-backed Securities	16,127,208	4,811,958	1,367,414	3,001,765	3,937,853	1,745,100	1,263,118
Debt Mutual Funds	200,169,657	71,233,165	117,401,024			11,535,468	
Mortgage Pass Throughs	8,679,274	289,892			1,681,709	6,707,673	
Money Market Mutual Funds	27,494,134	27,494,134					
Domestic Corporate Bonds	11,259,875		498,325	1,527,835	3,154,802	6,078,913	
Foreign Corporate Bonds	23,011,851		400,093	1,385,369	8,053,081	13,173,308	
Foreign Government Bonds	419,000				202,000	217,000	
Total	\$ 306,419,028	\$ 104,293,016	\$ 121,794,033	\$ 6,415,575	\$ 17,029,445	\$ 54,583,099	\$ 2,303,860

Rating Agency: Moody's/Standard & Poor's/Fitch (lowest rating reported above)

The University has elected to invest \$72,012,710 of assets of the UNC Intermediate Fund in the UNC Investment Fund. The disclosures for these investments are not included in the preceding table. Rather, the disclosures for this portion of UNC Intermediate Fund investments are included in those for UNC Investment Fund.

UNC Chapel Hill Foundation Investment Fund, Inc. (Chapel Hill Investment Fund) – Chapel Hill Investment Fund is a North Carolina nonprofit corporation exempt from income tax pursuant to Section 501(c)(3). It was established in January 1997 and is classified as a governmental external investment pool. The pool is utilized to manage the investments for charitable, nonprofit foundations, associations, trusts, endowments, and funds that are organized and operated primarily to support the University. The University's Endowment, UNC-Chapel Hill Foundation, Business School Foundation, School of Education Foundation, Law Foundation, Medical Foundation, Arts and Sciences Foundation, and Educational Foundation Trust are participants in the Chapel Hill Investment Fund and are included in the University's reporting entity (internal portion). Other affiliated organizations (external portion) in the Chapel Hill Investment Fund are not included in the University's reporting entity. Fund ownership of the Chapel Hill Investment Fund is measured using the unit value method. Under this method, each participant's investment balance is determined on a market value basis. The external portion of the Chapel Hill Investment Fund is presented in the accompanying financial statements as Funds Held in Trust for Pool Participants.

The Chapel Hill Investment Fund is not registered with the SEC and is not subject to any formal oversight other than that provided by the Chapel Hill Investment Fund Board of Directors (See Note 1A).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The Chapel Hill Investment Fund is the primary participant of UNC Investment Fund, LLC (UNC Investment Fund) and on a monthly basis receives a unitization report from the Management Company defining change in book and market value, applicable realized gains and losses and expenses. The Chapel Hill Investment Fund uses a unit basis to determine each participant's market value and to distribute the fund's earnings according to the fund's spending policy. There are no involuntary participants in the Chapel Hill Investment Fund. The University has not provided or obtained any legally binding guarantees during the period to support the value for the Chapel Hill Investment Fund. The audited financial statements for the Chapel Hill Investment Fund may be obtained from the University Controller's Office, Campus Box 1270, Chapel Hill, NC 27599-1270, or by calling (919) 962-1370.

The Chapel Hill Investment Fund consists of an approximate 64% membership in the UNC Investment Fund categorized below.

UNC Investment Fund, LLC (UNC Investment Fund) – The UNC Investment Fund is a nonprofit limited liability company exempt from income tax pursuant to Section 501(c)(3) organized under the laws of the State of North Carolina. It was established in December 2002 by the Chapel Hill Investment Fund and is classified as a governmental external investment pool. The pool is utilized to manage the investments for The University of North Carolina, its constituent institutions, and affiliates of the constituent institutions. This includes charitable, nonprofit foundations, associations, trusts, endowments, and funds that are organized and operated primarily to support these institutions. As previously noted, the Chapel Hill Investment Fund, with an approximate 64% membership interest as of June 30, 2014, is the predominant member of the UNC Investment Fund.

The University's reporting entity portion of the Chapel Hill Investment Fund and the Management Company's portion of the UNC Investment Fund are characterized as the internal portion. Other affiliated organizations in the Chapel Hill Investment Fund, in addition to other members of the UNC Investment Fund not included in the University's reporting entity, are characterized as the external portion. The external portion of the UNC Investment Fund is presented in the accompanying financial statements as Funds Held in Trust for Pool Participants. Membership interests of the UNC Investment Fund are measured using the unit value method. Under this method, each member's investment balance is determined on a market value basis.

The UNC Investment Fund is not registered with the SEC and is not subject to any formal oversight other than that provided by the Chapel Hill Investment Fund as the controlling member (See Note 1A).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Effective January 1, 2003, the Management Company entered into an investment management services agreement with the UNC Investment Fund and provides investment management and administrative services.

The Bank of New York Mellon is the custodian for the UNC Investment Fund and provides the University with monthly statements defining income and market value information. The UNC Investment Fund uses a unit basis to determine each member's market value and to distribute the fund's earnings. The University has not provided or obtained any legally binding guarantees during the period to support the value for the UNC Investment Fund investments. The audited financial statements for the UNC Investment Fund may be obtained from UNC Management Company, Inc., 1400 Environ Way, Chapel Hill, NC 27517.

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

UNC Investment Fund Pool Investments

	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1 to 5	6 to 10	More than 10
Investment Type					
<i>Debt Securities</i>					
U.S. Treasuries	\$ 14,729,425	\$ 0	\$ 7,102,180	\$ 7,627,245	\$ 0
U.S. Agencies	7,315,268	873,600	1,859,963	1,449,224	3,132,481
Mortgage Pass Throughs	1,687,259	1,687,259			
Collateralized Mortgage Obligations	32,567,235	32,536,664			30,571
Asset-backed Securities	13,550,772	13,550,772			
Debt Mutual Funds	78,788,815	1,519,372		77,269,443	
Money Market Mutual Funds	170,575,707	170,575,707			
Domestic Corporate Bonds	4,522,773	1,265,273	2,109,685	505,540	642,275
Total Debt Securities	323,737,254	\$ 222,008,647	\$ 11,071,828	\$ 86,851,452	\$ 3,805,327
<i>Other Securities</i>					
International Equity Index Funds	39,542,380				
Equity Index Funds	11,583,114				
Real Estate Investment Trust	33,734,977				
Long/Short Hedge Funds	789,695,974				
Diversifying Hedge Funds	376,319,235				
Hedge Funds in Liquidation	18,083,494				
Long Only Equity Funds	1,034,289,312				
Private Equity Limited Partnerships	895,050,209				
Real Assets Limited Partnerships	523,267,641				
Domestic Stocks	168,695,095				
Total UNC Investment Fund Pool	\$ \$4,213,998,685				

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

At June 30, 2014, investments in the UNC Investment Fund Pool had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa	AA Aa	A	BBB Baa	BB, Ba & Below
U.S. Agencies	\$ 7,315,269	\$ 0	\$ 7,315,269	\$ 0	\$ 0	\$ 0
Mortgage Pass Throughs	1,687,258					1,687,258
Collateralized Mortgage Obligations	32,567,234	11,881				32,555,353
Asset-backed Securities	13,550,772				1,888,930	11,661,842
Debt Mutual Funds	78,788,815				78,788,815	
Money Market Mutual Funds	170,575,708	170,575,708				
Domestic Corporate Bonds	4,522,773		500,990	3,761,805		259,978
Total	\$ 309,007,829	\$ 170,587,589	\$ 7,816,259	\$ 3,761,805	\$ 80,677,745	\$ 46,164,431

Rating Agency: Moody's/Standard and Poor's/Fitch (lowest rating reported above)

Foreign Currency Risk: At June 30, 2014, the UNC Investment Fund Pool's exposure to foreign currency risk is as follows:

Investment	Currency	Fair value (U.S. dollars)
Private Equity Limited Partnerships	Euro	\$ 97,027,892
Real Assets Limited Partnerships	Euro	21,915,101
Other Hedge Funds	Euro	30,847,091
Total Euro		149,790,084
Private Equity Limited Partnerships	British Pound Sterling	11,464,104
Real Assets Limited Partnerships	British Pound Sterling	8,607,988
Total British Pound Sterling		20,072,092
Real Assets Limited Partnerships	Canadian Dollar	9,850,080
Private Equity Limited Partnerships	Australian Dollar	5,790,081
Total		\$ 185,502,337

Investment Derivatives: At June 30, 2014, the UNC Investment Fund is invested in futures contracts with a fair value of \$80,521,014. Additional information is provided in Note 9 Derivative Instruments.

Non-Pooled Investments - The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2014, for the University's non-pooled investments.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Non-Pooled Investments

Investment Type	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1 to 5	6 to 10	More than 10
Debt Securities					
U.S. Treasuries	\$ 125,231	\$ 125,231	\$ 0	\$ 0	\$ 0
U.S. Agencies	426	426			
Mortgage Pass Throughs	204	204			
Collateralized Mortgage Obligations	48,630	48,630			
State and Local Government	7,693,565	504,669	3,315,380	3,485,291	388,225
Money Market Mutual Funds	52,443,331	52,443,331			
Domestic Corporate Bonds	577,830	484,325		93,505	
Foreign Corporate Bonds	1,479,385	90,279		1,389,106	
Foreign Government Bonds	33,220	33,220			
Total Debt Securities	62,401,822	\$ 53,730,315	\$ 3,315,380	\$ 4,967,902	\$ 388,225
Other Securities					
International Mutual Funds	670,890				
Equity Mutual Funds	713,174				
Investments in Real Estate	418,223				
Real Estate Investment Trust	2,720,635				
Private Equity Limited Partnerships	2,769,766				
Real Assets Limited Partnerships	3,237,911				
Domestic Stocks	15,577,796				
Foreign Stocks	4,229,812				
Other	13,455,140				
Total Non-Pooled Investments	\$ 106,195,169				

At June 30, 2014, the University's Non-Pooled investments had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa	AA Aa	A	BBB Baa	BB, Ba and below	Unrated
U.S. Agencies	\$ 426	\$ 0	\$ 426	\$ 0	\$ 0	\$ 0	\$ 0
Mortgage Pass Throughs	204						204
Collateralized Mortgage Obligations	48,630						48,630
Debt Mutual Funds	7,693,564	388,225	3,268,142	1,074,818	2,183,863	273,847	504,669
Money Market Mutual Funds	52,443,330	52,381,428		61,902			
Domestic Corporate Bonds	577,830				93,505	484,325	
Foreign Corporate Bonds	1,479,386	1,356,398	32,709	22,046			68,233
Foreign Government Bonds	33,220						33,220
Total	\$ 62,276,590	\$ 54,126,051	\$ 3,301,277	\$ 1,158,766	\$ 2,277,368	\$ 758,172	\$ 654,956

Rating Agency: Moody's/Standard & Poor's/Fitch (lowest rating reported above)

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Total Investments – The following table presents the fair value of the total investments at June 30, 2014.

Investment Type	Fair Value
<i>Debt Securities</i>	
U.S. Treasuries	\$ 143,360,557
U.S. Agencies	132,859,871
Mortgage Pass Throughs	10,395,970
Collateralized Mortgage Obligations	59,948,022
Asset-backed Securities	30,685,765
Debt Mutual Funds	294,120,169
Money Market Mutual Funds	305,883,096
Domestic Corporate Bonds	47,550,379
Foreign Corporate Bonds	24,491,237
Foreign Government Bonds	452,219
Total Debt Securities	1,049,747,285
<i>Other Securities</i>	
International Equity Index Funds	39,542,380
International Equity Mutual Funds	670,890
Equity Index Funds	11,583,114
Equity Mutual Funds	713,174
Investments in Real Estate	418,223
Real Estate Investment Trust	36,628,183
Long/Short Hedge Funds	737,513,922
Diversifying Hedge Funds	376,319,235
Hedge Funds in Liquidation	94,258,889
Long Only Hedge Funds	1,010,295,969
Private Equity Limited Partnerships	897,819,975
Real Assets Limited Partnerships	526,505,551
Domestic Stocks	184,302,891
Foreign Stocks	4,229,812
Other	13,455,140
Total Investments	\$ 4,984,004,633

Total investments are reported in the University's financial statements:

University Statement of Net Position	<u>Amount</u>
Short-Term Investments	\$ 682,104,783
Restricted Short-Term Investments	201,630,037
Endowment Investments	1,701,042,103
Restricted Investments	1,846,015,944
Other Investments	<u>27,650,514</u>
Subtotal	<u>4,458,443,381</u>
Investments of UNC Investment Fund Held for Component Units that are Discretely Presented in Accompanying Financial Statements	<u>525,561,252</u>
Total Investments	<u><u>\$ 4,984,004,633</u></u>

The University's reporting entity, including the three discretely presented component units, comprises approximately 66% of the UNC Investment Fund.

Component Units - Investments of the University's discretely presented component unit, the Medical Foundation of North Carolina, Inc., are subject to

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

and restricted by G.S. 36E “Uniform Prudent Management of Institutional Funds Act” (UPMIFA) and any requirements placed on them by contract or donor agreements. Because the Medical Foundation reports under the FASB reporting model, disclosures of the various investment risks are not required. A summary of investments not held by the University as of June 30, 2014:

<u>Investment Type</u>	<u>Carrying Value</u>
Money Market Funds	\$ 1,645,976
Common Stock	73,043
Mutual Funds - Equity Oriented	29,569,173
Mutual Funds - Credit Oriented	7,831,966
International Equity Fund	7,991,606
Certificate of Deposit	256,747
Total Investments	\$ 47,368,511

NOTE 3 - ENDOWMENT INVESTMENTS

Substantially all of the investments of the University’s endowment funds are pooled in the Chapel Hill Investment Fund. Under the “Uniform Prudent Management of Institutional Funds Act” (UPMIFA), authorized by the North Carolina General Assembly on March 19, 2009, the Board may appropriate expenditures from eligible nonexpendable balances if deemed prudent and necessary to meet program outcomes and for which such spending is not specifically prohibited by the donor agreements. During the year, the Board did not appropriate expenditures from eligible nonexpendable endowment funds. Investment return of the University’s pooled endowment funds is predicated on the total return concept (yield plus appreciation). Annual distributions from the Chapel Hill Investment Fund to the University’s pooled endowment funds are generally based on an adopted distribution policy. Under this policy, the prior year distribution is increased by the rate of inflation as measured by the Consumer Price Index (CPI) unless the Board determines otherwise. Each year’s distribution, however, is subject to a minimum of 4% and a maximum of 7% of the pooled endowment fund’s average market value for the previous year.

To the extent that the total return for the current year exceeds the distribution, the excess is added to principal. If current year earnings do not meet the distribution requirements, the University uses accumulated income and appreciation to make up the difference. At June 30, 2014, accumulated income and appreciation of \$687,081,349 was available in the University’s pooled endowment funds of which \$625,663,203 was restricted to specific purposes including scholarships and fellowships, research, library acquisitions, professorships, departmental and other uses. The remaining portion of net appreciation available to be spent is classified as unrestricted net position.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 4 - RECEIVABLES

Receivables at June 30, 2014, were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
Current Receivables			
Students	\$ 5,229,681	\$ 2,522,512	\$ 2,707,169
Student Sponsors	219,954		219,954
Patients	187,960,113	135,417,693	52,542,420
Accounts	39,806,417		39,806,417
Auxiliary	16,422,269		16,422,269
Intergovernmental	169,732,754		169,732,754
Pledges	10,613,589	241,542	10,372,047
Investment Earnings	831,161		831,161
Interest on Loans	1,060,483		1,060,483
Other	54,824		54,824
	Total Current Receivables	\$ 138,181,747	\$ 293,749,498
Noncurrent Receivables			
Pledges	\$ 14,194,538	\$ 354,864	\$ 13,839,674
Notes Receivable			
Notes Receivable - Current:			
Institutional Student Loan Programs	\$ 4,563,185	\$ 363,094	\$ 4,200,091
Notes Receivable - Noncurrent:			
Federal Loan Programs	26,109,881	1,982,262	24,127,619
Institutional Student Loan Programs	7,867,503	493,797	7,373,706
	Total Notes Receivable - Noncurrent	\$ 2,476,059	\$ 31,501,325

Pledges are receivable over varying time periods ranging from one to ten years, and have been discounted based on a projected interest rate of 0.036% for the outstanding periods, and allowances are provided for the amounts estimated to be uncollectible.

Scheduled receipts, the discounted amount under these pledge commitments, and allowances for uncollectible pledges are as follows:

Fiscal Year	Amount
2015	\$ 10,613,589
2016	4,967,946
2017	1,545,134
2018	1,195,024
2019	863,607
2020-2024	5,648,453
	Total Pledge Receipts Expected
	24,833,753
Less Discount Amount Representing Interest (0.036% Rate of Interest)	25,626
	Present Value of Pledge Receipts Expected
	24,808,127
Less Allowance for Doubtful Accounts	596,406
	Pledges Receivable
	\$ 24,211,721

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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	\$ 63,488,953	\$ 0	\$ 0	\$ 63,488,953
Art, Literature, and Artifacts	86,277,115	2,270,044	1,396	88,545,763
Construction in Progress	231,972,475	29,590,050	217,305,218	44,257,307
Computer Software in Development	39,164,977	27,530,575	2,837,702	63,857,850
Other Intangible Assets	1,000,000			1,000,000
Total Capital Assets, Nondepreciable	<u>421,903,520</u>	<u>59,390,669</u>	<u>220,144,316</u>	<u>261,149,873</u>
Capital Assets, Depreciable				
Buildings	2,694,714,426	220,414,929		2,915,129,355
Machinery and Equipment	394,295,353	29,759,602	19,300,852	404,754,103
General Infrastructure	904,706,404	49,483,266		954,189,670
Computer Software	49,196,387	2,897,702		52,094,089
Total Capital Assets, Depreciable	<u>4,042,912,570</u>	<u>302,555,499</u>	<u>19,300,852</u>	<u>4,326,167,217</u>
Less Accumulated Depreciation/Amortization for				
Buildings	825,390,668	75,547,082		900,937,750
Machinery and Equipment	202,363,056	24,910,635	12,915,806	214,357,885
General Infrastructure	316,617,251	26,926,252		343,543,503
Computer Software	8,294,115	3,054,476		11,348,591
Total Accumulated Depreciation/Amortization	<u>1,352,665,090</u>	<u>130,438,445</u>	<u>12,915,806</u>	<u>1,470,187,729</u>
Total Capital Assets, Depreciable, Net	<u>2,690,247,480</u>	<u>172,117,054</u>	<u>6,385,046</u>	<u>2,855,979,488</u>
Capital Assets, Net	<u>\$ 3,112,151,000</u>	<u>\$ 231,507,723</u>	<u>\$ 226,529,362</u>	<u>\$ 3,117,129,361</u>

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

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

	Amount
Accounts Payable	\$ 52,454,443
Accrued Payroll	41,136,623
Contract Retainage	11,912,488
Intergovernmental Payables	7,851,260
Investment Derivatives Liability	3,828,479
Total Accounts Payable and Accrued Liabilities	<u>\$ 117,183,293</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 7 - SHORT-TERM DEBT

Short-term debt activity for the year ended June 30, 2014, was as follows:

	Balance July 1, 2013	Draws	Repayments	Balance June 30, 2014
Commercial Paper Program	\$ 18,000,000	\$ 0	\$ 0	\$ 18,000,000

The University manages a commercial paper (“CP”) program under the issuer name of the Board of Governors of the University of North Carolina that provides up to \$500,000,000 in short-term financing for the University’s and North Carolina State University’s (“NCSU”) capital improvement programs. Under this CP program, the University is authorized to issue up to \$400,000,000 and NCSU is authorized to issue up to \$100,000,000. Contingent liquidity needs for the entire CP program are provided by the University of North Carolina at Chapel Hill and supported by a pledge of the University’s available funds.

The University will typically utilize the commercial paper program for construction financing and will periodically issue long-term bonds to refund the outstanding balances under this program in order to provide permanent financing for these capital improvement projects.

At its June 2012 meeting, the Board of Governors for the University of North Carolina issued a resolution to limit the cumulative amount of outstanding commercial paper for the University of North Carolina at Chapel Hill under this program to \$250,000,000. This resolution does not impact NCSU.

NOTE 8 - 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, are presented as follows:

	Balance July 1, 2013 (As Restated)	Additions	Reductions	Balance June 30, 2014	Current Portion
Revenue Bonds Payable	\$ 1,403,975,000	\$ 0	\$ 30,205,000	\$ 1,373,770,000	\$ 119,984,746
Plus: Unamortized Premium	30,061,279		1,297,738	28,763,541	
Less: Unamortized Discount	(15,187,901)		(3,538,675)	(11,649,226)	
Total Revenue Bonds, Net	1,418,848,378		27,964,063	1,390,884,315	119,984,746
Notes Payable	45,256,992	4,705,000	5,133,031	44,828,961	986,219
Capital Leases Payable	764,902		280,038	484,864	293,191
Compensated Absences	134,740,072	75,080,233	70,123,901	139,696,404	7,683,222
Annuity and Life Income Payable	13,882,106	1,169,311	2,825,241	12,226,176	1,436,261
Total Long-Term Liabilities	\$ 1,613,492,450	\$ 80,954,544	\$ 106,326,274	\$ 1,588,120,720	\$ 130,383,639

Additional information regarding capital lease obligations is included in Note 9.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

Purpose	Series	Interest Rate/Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through June 30, 2014	Accretion on Capital Appreciation Bonds	Principal Outstanding June 30, 2014	See Table Below
General Revenue Bonds Payable								
	2001B	4.538%*	12/01/2025	\$ 54,970,000	\$ 28,015,000	\$ 0	\$ 26,955,000	
	2001C	3.270%*	12/01/2025	54,970,000	28,015,000		26,955,000	
	2003	5.000%	12/01/2013	107,960,000	107,960,000		0	
	2005A	4.250 - 5.000%	12/01/2034	404,960,000	16,555,000		388,405,000	
	2007	4.450 - 5.000%	12/01/2036	298,475,000	0		298,475,000	
	2009A	3.000 - 5.000%	12/01/2028	97,735,000	15,150,000		82,585,000	
	2009B	5.757%**	12/01/2039	112,805,000	0		112,805,000	
	2012A	4.295%*	12/01/2018	100,000,000	0		100,000,000	
	2012B	5.125%*	12/01/2020	100,000,000	0		100,000,000	
	2012C	0.617 - 3.596%	12/01/2033	127,095,000	2,020,000		125,075,000	
	2012D	1.400%*	08/18/2016	41,000,000	0		41,000,000	
Total General Revenue Bonds				<u>1,499,970,000</u>	<u>197,715,000</u>		<u>1,302,255,000</u>	
Utilities System	1997	5.400 - 5.500%	08/01/2021	30,379,142	16,830,000	42,337,382	55,886,524	(1)
U.S. EPA Project	1991	9.050%	02/15/2015	36,678,921	53,915,000	21,215,329	3,979,250	
Total Revenue Bonds Payable (Principal Only)				<u>\$ 1,567,028,063</u>	<u>\$ 268,460,000</u>	<u>\$ 63,552,711</u>	<u>1,362,120,774</u>	
Less: Unamortized Discount							(92,299)	
Plus: Unamortized Premium							28,855,840	
Total Revenue Bonds Payable, Net							<u>\$ 1,390,884,315</u>	

* For variable rate debt, interest rates in effect at June 30, 2014 are included. For variable rate debt with interest rate swaps, the synthetic fixed rates are included.

** The University has elected to treat these bonds as federally taxable "Build America Bonds" for the purposes of the American Recovery and Reinvestment Act and to receive a cash subsidy from the U.S. Treasury equal to 32% of the interest payable on these bonds. For these bonds, the interest rate included is the taxable rate, which does not factor in the cash subsidy from the U.S. Treasury.

The University has pledged future revenues, net of specific operating expenses, to repay revenue bonds as shown in the table below:

Ref	Revenue Source	Total Future Revenues Pledged	Current Year			Estimate of % of Revenues Pledged
			Revenues Net of Expenses	Principal	Interest	
(1)	Utilities Revenue	\$ 67,305,000	\$ 43,886,801	\$ 8,415,000	\$ 0	6%

C. Demand Bonds - Included in bonds payable are several 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 University's remarketing or paying agents.

With regards to the following demand bonds, the University has not entered into legal agreements, which would convert the demand bonds not successfully remarketed into another form of long-term debt.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

General Revenue, Series 2001B and 2001C

In 2001 the University issued two series of variable rate demand bonds in the amount of \$54.97 million (2001B) and \$54.97 million (2001C) that each has a final maturity date of December 1, 2025. The bonds are subject to mandatory sinking fund redemption on the interest payment date on or immediately preceding each December throughout the term of the bonds. The proceeds of these issuances were used to provide funds to refund in advance of their maturity the following issues: Ambulatory Care Clinic, Series 1990; Athletic Facilities, Series 1998; Carolina Inn, Series 1994; School of Dentistry, Series 1995; Kenan Stadium, Series 1996; Housing System, Series 2000; and Parking System, Series 1997C. While bearing interest at a weekly rate, the bonds are subject to purchase on demand with seven days' notice and delivery to the University's Remarketing Agents; J.P. Morgan Securities, Inc. (2001B) and Banc of America Securities, LLC (2001C). Effective September 23, 2008, J.P. Morgan Securities, Inc. replaced Lehman Brothers, Inc.

The University entered into line of credit agreements in the amount of \$200 million with Wells Fargo Bank, N.A. ("the Bank") and \$200 million with J.P. Morgan Chase, N.A. ("the Bank") on September 21, 2011. Under each line of credit agreement, the University is entitled to draw amounts sufficient to pay the principal and accrued interest on Variable Rate Demand Bonds (or Commercial Paper Bonds) delivered for purchase. Under each line of credit agreement, the University may, at any time and for any reason, reduce the commitment by any amount upon 30 days prior written notice to the Bank.

The University is required to pay a quarterly facility fee for each line of credit in the amount of 0.38% per annum based on the size of the commitment. If a long-term debt rating assigned by Standard & Poor's (S&P), Fitch Ratings (Fitch) or Moody's Investors Service (Moody's) is lowered, the facility fee assigned to the rating in the below table shall apply. In the event of a split rating (i.e., one or more of the rating agency's ratings is at a different level than the rating of either of the other rating agencies), the facility fee rate shall be determined as follows: (i) if two of the three ratings appear in the same level, the facility fee rate shall be based on that level; (ii) if no two ratings appear in the same level, the facility fee rate shall be based on the level which includes the middle of the three ratings.

S&P	Fitch	Moody's	Facility Fee
AA	AA	Aa2	0.48%
AA-	AA-	Aa3	0.58%
A+	A+	A1	0.68%
A	A	A2	0.78%
A- or lower	A- or lower	A3 or lower	1.78%

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The University will pay an accrued interest fee equal to the amount of accrued interest, at the time of purchase of the bonds, multiplied by the bank rate multiplied by the ratio of the number of days from the date of purchase of the bonds until the date of payment of the accrued interest to 365 days.

Under each line of credit agreement, draws to purchase bonds will accrue interest at the bank rate payable on the same interest date as provided in the Series Indenture for the original bonds. The University is required to begin making a series of six fully amortizing semiannual principal payments on bonds held by the Bank six months after the date of funding. Commercial Paper Bonds held by the Bank may be rolled over for a period of 180 days and must be reduced by 1/6th of the original amount of the Commercial Paper Bonds for a period of up to five rollovers. All outstanding principal and accrued but unpaid interest is due in full at the maturity of the line of credit.

Each line of credit agreement expires on September 21, 2014 and is subject to covenants customary to this type of transaction, including a default provision in the event that the University's long-term bond ratings were lowered to below a BBB- for S&P, BBB- for Fitch, and Baa3 for Moody's. At June 30, 2014, no purchase drawings had been made under the line of credit. On September 19, 2014, the University entered into new line of credit agreements, maintaining an aggregate coverage amount of \$400 million, with \$200 million from Wells Fargo Bank, N.A., \$100 million from Royal Bank of Canada, and \$100 million from U.S. Bank, N.A.

General Revenue, Series 2012D

On December 14, 2012, the University issued a bond to be designated "The University of North Carolina at Chapel Hill General Revenue Bond (Kenan Stadium Improvements Phase II), Series 2012D" to The Educational Foundation, Inc. (the "Owner") in exchange for certain improvements to Kenan Stadium on the University's campus known as "Kenan Stadium Improvements, Phase 2 - Carolina Student Athlete Center for Excellence". The 2012D Bond was issued in the amount of \$41 million and matures on August 18, 2016 ("maturity date").

Interest will be payable on the 2012D Bond on the maturity date or, if sooner, the prepayment date of the bond as permitted under the tender option or the prepayment options as referenced below. The unpaid principal balance of the 2012D Bond, together with all accrued and unpaid interest thereon will be due and payable in full on the maturity date in the event that the tender option or prepayment option is not exercised in advance of the maturity date.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The University shall be responsible for calculating the interest due on the 2012D Bond and reporting such amount to the Owner and The Bank of New York Mellon Trust Company, N.A. (the "Trustee"). Payments of principal and interest on the bond shall be made directly by the University to the Owner under the terms of the bond documents and the Trustee shall have no responsibility for making such payments. The University shall promptly notify the Trustee in writing of any such payments. Any payments of principal of and interest on the 2012D Bond made directly by the University to the Owner will be credited against The Board of Governors of the University of North Carolina's (the "Board") obligation to cause payments to be made with respect to the 2012D Bond to the Debt Service Fund under the General Indenture.

The 2012D Bond may be tendered by the Owner for payment by the University, on behalf of the Board, in whole or in part without premium or penalty on any business day on or after 90 days prior written notice to the University and the Trustee.

The 2012D Bond may be prepaid by the University, on behalf of the Board, in whole or in part without premium or penalty on any business day on or after 90 days prior written notice to the Owner and the Trustee.

When payment is due at maturity or upon exercise of the tender or prepayment options, the University may use proceeds from a long-term bond issue or proceeds from the issuance of Commercial Paper at the time of the payment to fund the obligation under the bond.

The unpaid principal balance of the 2012D Bond outstanding from time to time will bear interest at the Adjusted LIBOR Rate. "Adjusted LIBOR Rate" means a rate of interest per annum equal to the sum obtained (rounded upwards, if necessary, to the next higher 1/16 of 1.0%) by adding (1) the One Month LIBOR plus (2) 1.0% per annum, which shall be adjusted monthly on the first day of each LIBOR Interest Period; provided, however, for any particular LIBOR Interest Period, the Adjusted LIBOR Rate will not be less than 1.4% per annum.

With respect to other terms and conditions, this bond is not supported by any other letters of credit or standby liquidity agreements and does not contain any take-out agreements.

- D. Capital Appreciation Bonds** - The University's Series 1997 Utility System and the Series 1991 U.S. Environmental Protection Agency Project bond issues include capital appreciation bonds with an original issue amount of \$30,379,142 and \$3,828,921, respectively. These bonds are recorded in the amounts of \$55,886,524 (\$84,135,000 ultimate maturity less \$11,418,476 discount less \$16,830,000 principal paid) and \$3,979,250 (\$25,275,000 ultimate maturity less \$230,750 accreted

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

principal less \$21,065,000 principal paid), respectively, which is the accreted value at June 30, 2014. These bonds mature in the years from 2014 to 2021.

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

Fiscal Year	Annual Requirements				
	Revenue Bonds Payable			Notes Payable	
	Principal	Interest	Interest Rate Swaps, Net*	Principal	Interest
2015	\$ 30,840,000	\$ 48,950,669	\$ 9,981,083	\$ 986,219	\$ 1,803,849
2016	43,881,667	48,470,078	9,498,740	1,244,534	1,901,464
2017	102,293,333	47,325,838	8,385,135	5,836,345	1,831,328
2018	77,645,000	46,484,462	6,488,101	1,182,524	1,764,850
2019	78,360,000	45,694,488	4,381,373	1,236,076	1,711,298
2020-2024	193,295,000	216,354,723	5,473,588	34,343,263	4,206,639
2025-2029	171,205,000	189,821,533	321,951		
2030-2034	378,550,000	136,575,920			
2035-2039	285,850,000	25,478,755			
2040-2044	11,850,000	341,102			
Total Requirements	\$ 1,373,770,000	\$ 805,497,568	\$ 44,529,971	\$ 44,828,961	\$ 13,219,428

Interest on the variable rate General Revenue Bonds 2001B is calculated at 0.03% at June 30, 2014.

Interest on the variable rate General Revenue Bonds 2001C is calculated at 0.06% at June 30, 2014.

Interest on the variable rate General Revenue Bonds 2012A is calculated at 0.55% at June 30, 2014.

Interest on the variable rate General Revenue Bonds 2012B is calculated at 0.85% at June 30, 2014.

Interest rates on General Revenue Bonds 2001 Series B and Series C are reset each week by the remarketing agent based upon a combination of the University's credit rating and market conditions.

Interest rates on General Revenue Bonds 2012 Series A and Series B are based on the 1-month LIBOR index rate plus an interest rate spread of 45 and 75 basis points for 2012 Series A and Series B, respectively.

This schedule also includes the debt service requirements for debt associated with interest rate swaps.

More detailed information about interest rate swaps is presented in Note 9 Derivative Instruments.

*Computed using $(5.240\% - 0.060\%) \times (\$22,000,000 - \text{annual swap reduction})$; $(3.314\% - 0.1040\%) \times \$86,145,000$ notional amount; and, $(4.375\% - 0.1040\%) \times \$150,000,000$ notional amount.

The fiscal year 2015 principal requirements include demand bonds principal payments due for 2015 only. This differs from the amount disclosed as current in Note 8A Changes in Long-term Liabilities as the current portion of bonds payable includes all outstanding principal for the demand bonds. See Note 8C Demand Bonds.

The 2012AB Bonds have a maturity date of December 1, 2041. However, the bonds are issued initially in the Index Mode extending to the initial index tender dates of December 1, 2015 for Series 2012A and December 1, 2017 for Series 2012B. While in this mode, the bonds will bear interest at the index rate, which will be the rate per annum determined monthly equal to 67.0% of One Month LIBOR plus an applicable spread of 0.45% (45 basis points) for the 2012A Bonds and 0.75% (75 basis points) for the 2012B Bonds.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The 2012AB Bonds of each series in an Index Mode are subject to redemption, at the option of the University, in whole or in part, on any business day during the period beginning six months prior to the index tender date for such 2012AB Bonds, to and including such index tender date, at a redemption price equal to 100% of the principal amount of 2012AB Bonds called for redemption, plus accrued interest, if any, to the date of redemption. In addition, and also at the discretion of the University during the period beginning six months prior to the index tender date for such 2012AB Bonds, the interest rate can be reset which would trigger a redemption requirement and a remarketing.

If the funds available to purchase 2012AB Bonds of a series tendered on an index tender date are not sufficient to pay the purchase price of all such 2012AB Bonds, a Delayed Remarketing Period will commence on such index tender date and the failure to purchase such tendered 2012AB Bonds will not constitute an event of default under the Indentures. The Delayed Remarketing Period will continue to (but not include) the earlier of (a) the date on which all such 2012AB Bonds are successfully remarketed or (b) the date on which all of such 2012AB Bonds have been deemed to have been paid and are no longer outstanding.

During a Delayed Remarketing Period for a Series of 2012AB Bonds, unless the 2012AB Bonds of such Series have been remarketed, the 2012AB Bonds of such Series shall be subject to special mandatory redemption. Beginning with the first such June 1 or December 1 that occurs not less than six months following the date of commencement of the applicable Delayed Remarketing Period and ending on the sixth June 1 or December 1, the 2012AB Bonds shall be repaid in six equal (or as equal as possible) semiannual installments on the special mandatory redemption date established herein. The final installment will be due and payable no later than the sixth special mandatory redemption date after the commencement of the applicable Delayed Remarketing Period.

The Annual Requirements presents the 2012AB Bonds as amortizing in six semiannual payments as set forth in the Delayed Remarketing Period, to be fully paid off in a period of three years after the respective index tender date established herein. If the bonds are successfully remarketed or refunded into a new bond in the future, and, therefore, not subject to the three-year amortization schedule after the initial index tender date, the total principal payments due in 2016 will reduce by \$16,666,667 to \$27,215,000, total principal payments in 2017 will reduce by \$33,333,333 to \$68,960,000, total principal payments in 2018 will reduce by \$50,000,000 to \$27,645,000, total principal payments in 2019 will reduce by \$50,000,000 to \$28,360,000, total principal payments in 2020 will reduce by \$33,333,333 to \$27,985,000, and total principal payments in 2021 will reduce by \$16,666,667 to \$27,865,000.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

F. Notes Payable - The University was indebted for notes payable for the purposes shown in the following table:

Purpose	Financial Institution	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through June 30, 2014	Principal Outstanding June 30, 2014
Real Property Purchase	Bank of America	3.550%	02/14/2024	\$ 9,250,000	\$ 4,390,172	\$ 4,859,828
Real Property Purchase	Bank of America	1.305%	06/30/2015	411,896	249,396	162,500
Real Property Purchase	Aviva	5.000%	01/01/2022	36,500,000	1,398,367	35,101,633
Real Property Purchase	Wells Fargo	0.755%	10/02/2016	4,705,000	0	4,705,000
Total Notes Payable				\$ 50,866,896	\$ 6,037,935	\$ 44,828,961

The UNC-Chapel Hill Foundation, part of the University’s reporting entity, has a line of credit agreement issued by Bank of America with a commitment amount of up to \$3,000,000 to finance the costs of projects benefiting the Foundation and/or the University, subject to the approval of the Board of Directors of the Foundation. Prior to the maturity date of June 30, 2013, the Foundation renewed the line of credit in the same commitment amount and with a new maturity date of June 30, 2015. Under the commitment, advances under the line of credit accrue interest at the variable rate of the LIBOR Market Index plus 1.15%. An unused commitment fee is due each quarter calculated as 0.24% of the difference between the commitment amount and the average balance outstanding for the quarter and paid in arrears on a quarterly basis. If the Foundation utilizes the line of credit to purchase an asset on behalf of the University, and later sells such asset to the University, the University reimburses the Foundation the principal amount of the draw and all accrued interest and associated transaction expenses.

On July 1, 2009, the UNC Chapel Hill Foundation, Inc. and Chapel Hill Foundation Real Estate Holdings Inc., (collectively, the “Borrowers”; individually, the “Foundation”, former, or “Real Estate Holdings”, the latter), entered into a loan agreement with the Bank of America, N.A. for \$45,750,000 to fund the acquisition of student housing and rental real property.

On December 15, 2011, Real Estate Holdings transferred the condominiumized unit of Granville Towers to a newly established single asset limited liability corporation Granville Towers, LLC of which Real Estate Holdings is the sole member. On the same date, Granville Towers LLC obtained a loan from Aviva Life and Annuity Company in the amount of \$36,500,000 (Aviva Loan) for which the proceeds were used to pay down the referenced purchase financing with Bank of America in the original amount of \$45,750,000. This Aviva loan is secured by a first deed of trust on the condominium unit of Granville Towers. In general, the loan

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

is non-recourse to both Real Estate Holdings and the Foundation, except for in the following instances: fraud, misrepresentation; delinquent taxes or other assessments; misapplication of potential condemnation awards or loss between the difference in the loan amount and insurance proceeds; environmental issue on the property; and a bankruptcy filing. Loan payments are based upon a 30-year amortization, but the loan carries an actual maturity date of January 1, 2022. During the committed term of this loan, the interest rate is fixed at 5%, and the monthly payments of principal and interest in the combined amount of \$195,939.89; all outstanding principal and accrued but unpaid interest is due at said maturity.

On December 15, 2011, the Borrowers executed a modification agreement with Bank of America with respect to the above loan in the original amount of \$45,750,000. The original principal balance of \$45,750,000 was paid down by \$36,500,000 with proceeds from the Aviva loan; the original maturity date of July 1, 2012, was extended to December 15, 2014; and the interest rate was changed to LIBOR plus 1.37%. Interest payments are made quarterly, and the principal balance of the loan is due at maturity. The loan is unsecured, but is governed by a loan agreement with financial and other covenants on the Borrowers.

On February 14, 2014, the Borrowers executed another modification agreement with Bank of America with respect to the above loan in the original amount of \$45,750,000. The original principal balance of \$45,750,000 was paid down by \$36,500,000 with proceeds from the Aviva loan; the original maturity date of July 1, 2012, was extended to December 15, 2014; and the interest rate was changed to LIBOR plus 1.37%. This loan was then paid down by \$4,250,000. The remaining \$5,000,000 was then refinanced with a fixed interest rate of 3.550% and a final maturity date of February 14, 2024. Interest and principal payments are made monthly.

In addition, on October 3, 2013, the Kenan-Flagler Business School Foundation, part of the University's reporting entity, entered into a line of credit agreement with Wells Fargo Bank, N.A. in the aggregate principal amount up to \$30,000,000 to finance the construction of the Paul J. Rizzo Conference Center Phase III addition. Advances under the line of credit note accrue interest at the variable rate of the LIBOR Market Index Rate plus 0.60%. The line of credit note has a maturity date of October 2, 2016. At June 30, 2014, the total amount of draws against the line of credit note was \$4,705,000.

- G. Annuities Payable** - The University participates in split-interest agreements with donors that require benefits payments for a specified

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

period to a designated beneficiary out of assets held in trust for this purpose. At the end of the predetermined period (e.g., the lifetime of the beneficiary specified by the donor), the remaining assets of the trust revert to the University for its use or for a purpose specified by the donor. At the end of each fiscal year, annuities and life income payable to the beneficiaries is calculated using IRS issued 90CM table, taking into consideration beneficiary's age and the amount of the gift, and using IRS issued Life Table 90CM.

NOTE 9 - DERIVATIVE INSTRUMENTS

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

Type	Notional Amount	Change in Fair Value		Fair Value at June 30, 2014	
		Classification	Increase (Decrease)	Classification	Asset (Liability)
<i>Hedging Derivative Instruments</i>					
<i>Cash Flow Hedges</i>					
Pay-fixed interest rate swap	\$100,000,000	Deferred outflow of resources	\$ (1,060,537)	Hedging derivative liability	\$ (20,565,757)
Pay-fixed interest rate swap	\$150,000,000	Deferred outflow of resources	(1,702,552)	Hedging derivative liability	(62,624,324)
			<u>\$ (2,763,089)</u>		<u>\$ (83,190,081)</u>
<i>Investment Derivative Instruments</i>					
Pay fixed interest rate swap					
2001B bonds	\$17,765,000	Investment income	\$ 375,299	Accounts payable	\$ (3,828,479)
Foreign equities futures	(a)	Investment income	\$ 487,642	Other investments	21,615,531
U.S dollar equity futures	\$58,474,380	Investment income	19,010,657	Other investments	58,905,483
			<u>\$ 19,873,598</u>		<u>\$ 76,692,535</u>

(a) 2 billion yen

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

Type	Objective	Notional Amount	Effective Start Date	Termination End Date	Terms
Pay-Fixed Interest Rate Swap	Hedge changes in cash flows on variable rate debt	\$ 100,000,000	12/01/07	12/01/36	Pay 3.314%, Receive 67% 1 Mo. LIBOR
Pay-Fixed Interest Rate Swap	Hedge changes in cash flows on variable rate debt	150,000,000	12/01/11	12/01/41	Pay 4.375%, Receive 67% 1 Mo. LIBOR

The fair values of interest rate swaps at the University were provided by its financial advisor. The method used by the financial advisor calculated the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

rates. These payments were then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

Hedging Derivative Risks

Interest rate risk: The University is exposed to interest rate risk on its interest rate swaps which is largely offset (or expected to be offset) by rates paid on variable-rate debt. In addition, the fair values of these instruments are highly sensitive to changes in interest rates. Because rates have declined significantly since the effective dates of the swaps, both of the swaps have a negative fair value as of June 30, 2014. The fair values are calculated as of June 30, 2014. As rates rise, the value of the swaps will increase, and as rates fall the fair value of the swaps will decrease.

Basis risk: The University is exposed to basis risk on the swaps to the extent there is a mismatch between variable bond rates paid and swap index rates received.

Termination risk: The swap agreements use the International Swaps and Derivatives Association (ISDA) Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. Termination could result in the University being required to make an unanticipated termination payment. The swaps may mandatorily terminate if the University fails to perform under terms of the contract.

Investment Derivative Risks

Interest Rate Risk: The University is exposed to interest rate risk on its interest rate swap. The fair value of this instrument is highly sensitive to interest rate changes. Because rates have changed since the effective date of the swap, the swap has a negative fair value of \$3,828,479 as of June 30, 2014. The negative fair value may be countered by a reduction in total interest payments required under the variable-rate bonds, creating lower synthetic interest rates. Because the coupons on the University's variable-rate bonds adjust to changing interest rates, the bonds do not have corresponding fair value increases. The negative fair value is the calculated value as of June 30, 2014. As the yield curve rises, the value of the swap will increase and as rates fall, the value of the swap decreases. The University pays 5.24% and receives the Securities Industry and Financial Markets Association (SIFMA) Swaps Index rate. On June 30, 2014, SIFMA was 0.06%. The interest rate swap has a notional amount of \$17,765,000 and matures November 1, 2025.

Foreign Currency Risk: Futures contracts based in foreign currency obligate the buyer to purchase an asset (or seller to sell an asset), such as a physical commodity or a financial instrument, at a predetermined future

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

date and price. See Note 2 Deposits and Investments for further information about the University's exposure to foreign currency risk.

NOTE 10 - LEASE OBLIGATIONS

- A. Capital Lease Obligations** - Capital lease obligations for machinery and equipment 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:

<u>Fiscal Year</u>	<u>Amount</u>
2015	\$ 316,229
2016	200,937
Total Minimum Lease Payments	517,166
Amount Representing Interest (4.380% - 4.834% Rate of Interest)	32,302
Present Value of Future Lease Payments	<u>\$ 484,864</u>

Machinery and equipment acquired under capital lease amounted to \$722,214 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 \$176,943 at June 30, 2014.

- B. Operating Lease Obligations** - Future minimum lease payments under non-cancelable operating leases for equipment, buildings and land consist of the following at June 30, 2014:

<u>Fiscal Year</u>	<u>Amount</u>
2015	\$ 7,976,744
2016	5,163,382
2017	3,869,871
2018	2,846,339
2019	1,750,672
2020-2024	3,928,971
Total Minimum Lease Payments	<u>\$ 25,535,979</u>

Rental expense for all operating leases during the year was \$26,079,719

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 11 - REVENUES

A summary of eliminations and allowances by revenue classification is presented as follows:

	Gross Revenues	Internal Sales Eliminations	Less Scholarship Discounts	Less Allowance for Uncollectibles	Less Indigent Care and Contractual Adjustments	Net Revenues
Operating Revenues						
Student Tuition and Fees	\$ 457,408,097	\$ 0	\$ 96,034,750	\$ (397,213)	\$ 0	\$ 361,770,560
Patient Services	\$ 821,049,513	\$ 0	\$ 0	\$ 43,092,419	\$ 465,902,646	\$ 312,054,448
Sales and Services						
Professional Income	\$ 143,703,045	\$ 5,052,956	\$ 0	\$ 0	\$ 0	\$ 138,650,089
Residential Life	78,839,069	74,952	10,560,647			68,203,470
Athletic	55,116,675	28,782				55,087,893
Dining	34,882,475	500				34,881,975
Utilities	135,215,055	105,201,053				30,014,002
Parking	27,068,406	369,730				26,698,676
Other	61,438,662	36,359,819				25,078,843
Student Stores	25,888,283	4,091,869	1,016,219			20,780,195
Telecommunications	21,148,510	10,476,393				10,672,117
UNC Management Company	9,157,062					9,157,062
Health, Physical Education, and Recreation Services	8,544,926	2,100	200,784			8,342,042
Trademark License Program	7,030,001					7,030,001
School of Government	5,688,358					5,688,358
Rental Property	4,609,131					4,609,131
Gene Therapy Center	3,192,802	297,406				2,895,396
KFBS Center	2,330,784					2,330,784
Printing/Carolina Copy	3,050,269	1,312,513				1,737,756
Performing Arts Series	1,651,091					1,651,091
Doubletree Carolina Inn	1,640,400					1,640,400
Repairs and Maintenance	30,255,475	28,686,370				1,569,105
ERP Student Fees	1,416,481					1,416,481
Student Union Services	502,185	234,843				267,342
Materials Management and Distribution	20,362,928	20,306,743				56,185
Total Sales and Services	\$ 682,732,073	\$ 212,496,029	\$ 11,777,650	\$ 0	\$ 0	\$ 458,458,394
Nonoperating - Noncapital Gifts	\$ 97,442,914	\$ 0	\$ 0	\$ 26,766	\$ 0	\$ 97,416,148

NOTE 12 - OPERATING EXPENSES BY FUNCTION

The University's operating expenses by functional classification are presented as follows:

	Salaries and Benefits	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation and Amortization	Total
Instruction	\$ 535,722,605	\$ 23,293,360	\$ 116,650,268	\$ 0	\$ 156,227	\$ 0	\$ 675,822,460
Research	301,616,103	46,163,724	198,955,564		16,863		546,752,254
Public Service	64,717,636	6,409,031	63,541,804		248,563		134,917,034
Academic Support	76,317,132	11,299,240	30,928,380		135,765		118,680,517
Student Services	17,589,377	1,070,914	14,146,236		545		32,807,072
Institutional Support	66,078,406	7,733,448	26,383,208		42,611		100,237,673
Operations and Maintenance of Plant	44,897,626	11,554,574	19,955,303		73,605,231		150,012,734
Student Financial Aid				112,449,587			112,449,587
Auxiliary Enterprises	360,817,609	52,382,291	245,271,946		10,951,094		669,422,940
Depreciation and Amortization						130,438,445	130,438,445
Total Operating Expenses	\$ 1,467,756,494	\$ 159,906,582	\$ 715,832,709	\$ 112,449,587	\$ 85,156,899	\$ 130,438,445	\$ 2,671,540,716

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 13 - PENSION PLANS

Each permanent full-time employee, as a condition of employment, is a member of either the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Eligible employees can elect to participate in the Optional Retirement Program at the time of employment; otherwise they are automatically enrolled in 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 University had a total payroll of \$1,214,902,099, of which \$457,366,996 was covered under the TSERS. Total employer and employee contributions for pension benefits for the year were \$39,745,192 and \$27,442,020, 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 University made 100% of its annual required contributions for the years ended June 30, 2014, 2013, and 2012, which were \$39,745,192, \$38,341,452, and \$33,975,672, 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.

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Administrators and eligible faculty of the University may join the Program instead of the TSERS. The Board of Governors of The University of North Carolina is responsible for the administration of the Program and designates the companies authorized to

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

offer investment products or the trustee responsible for the investment of contributions under the Program and approves the form and contents of the contracts and trust agreements.

Participants in the Program are immediately vested in the value of employee contributions. The value of employer contributions is vested after five years of participation in the Program. Participants become eligible to receive distributions when they terminate employment or retire.

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contribution rates are set each year by the North Carolina General Assembly. For the year ended June 30, 2014, these rates were set at 6.84% of covered payroll for employers and 6% of covered payroll for members. The University assumes no liability other than its contribution.

For the current fiscal year, the University had a total payroll of \$1,214,902,099, of which \$528,702,624 was covered under the Optional Retirement Program. Total employer and employee contributions for pension benefits for the year were \$36,163,259 and \$31,722,157, respectively.

NOTE 14 - OTHER POSTEMPLOYMENT BENEFITS

A. Health Benefits - The University 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 or the Optional Retirement Program. 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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 University contributed 5.4% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the Fund. Required contribution rates for the years ended June 30, 2013, and 2012, were 5.3% and 5.0%, respectively. The University made 100% of its annual required contributions to the Plan for the years ended June 30, 2014, 2013, and 2012, which were \$53,247,759, \$51,582,373, \$47,027,478, respectively. The University 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 University 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 and the Optional Retirement Program. 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 University made a statutory contribution of 0.44% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. Required contribution rates for the years ended June 30, 2013, and 2012, were 0.44% and 0.52%, respectively. The University made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2014, 2013, and 2012, which were \$4,338,706, \$4,282,310, and \$4,890,858, respectively. The University 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 15 - RISK MANAGEMENT

The University 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 reduction in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

Public Officers and Employees Liability Insurance – 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 per employee through a contract with a private insurance company. The University pays the premium, based on a composite rate, directly to the private insurer.

UNC Investment Fund, LLC (blended component unit) Liability Insurance – The UNC Investment Fund, LLC (UNC Investment Fund) is exposed to various risks of loss related to torts, theft of assets, and errors and omissions. The UNC Management Company, Inc. (Management Company) is a separate legal entity from The University of North Carolina System and the University. However, the Management Company's employees conduct UNC Investment Fund's affairs. Therefore, exposures to loss are handled by the purchase of commercial insurance by the Management Company. This insurance is independent of the risk management programs of The University of North Carolina System and the University.

Fire and Other Property Loss – The University 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 University for operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. The University has opted to purchase additional coverages offered by the Fund. Examples of this additional coverage include special form (all-risk) and business interruption insurance for certain property exposures. Losses covered by the Fund are subject to a \$5,000 per occurrence deductible.

Automobile Liability Insurance – 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 University pays premiums to the North Carolina Department of Insurance for the coverage.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Employee and Computer Fraud – The University 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. Universities are 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.

Other authorized coverage not handled by the North Carolina Department of Insurance is purchased through the state's insurance agent of record. Examples include, but are not limited to, fine arts, boiler and machinery, medical professional liability, athletic accident and revenues, and study abroad health insurance.

Comprehensive Major Medical Plan – University 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 University's primary responsibility is to arrange for and provide the necessary treatment for work related injury. The University is responsible for paying medical benefits and compensation in accordance with the North Carolina Workers' Compensation Act. The University retains the risk for workers' compensation.

Liability Insurance Trust Fund – The University participates in the Liability Insurance Trust Fund (Trust Fund), a claims-servicing public entity risk pool for healthcare professional liability protection. The Trust Fund services professional liability claims, managing separate accounts for each participant from which the losses of that participant are paid. Although participant assessments are determined on an actuarial basis, ultimate liability for claims remains with the participants and, accordingly, the insurance risks are not transferred to the Trust Fund.

The Trust Fund is an unincorporated entity created by Chapter 116, Article 26, of the *North Carolina General Statutes* and The University of North Carolina Board of Governors Resolution of June 9, 1978. The Trust Fund is a self-insurance program established to provide professional medical malpractice liability covering The University of North Carolina Hospitals at Chapel Hill (UNC Hospitals) and The University of North Carolina at Chapel Hill Faculty Physicians (UNC Faculty Physicians), the program participants. The Trust Fund provides coverage for program participants and individual health care practitioners working as employees, agents, or officers of program participants.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The Trust Fund is exempt from federal and state income taxes, and is not subject to regulation by the North Carolina Department of Insurance.

Participation in the Trust Fund is open to the University of North Carolina, any constituent institution of the University of North Carolina, the UNC Hospitals, and any health care institution, agency or entity that has an affiliation agreement with the University of North Carolina, with a constituent institution of the University of North Carolina, or with the UNC Hospitals. Only UNC Faculty Physicians and UNC Hospitals have participated in the Trust Fund to date. Participants provide management and administrative services to the Trust Fund at no cost.

The Trust Fund is governed by the Liability Insurance Trust Fund Council (the Council). The Council consists of 13 members as follows: one member each appointed by the State Attorney General, the State Insurance Commissioner, the Director of the Office of State Budget and Management, the State Treasurer (each serving at the pleasure of the appointer); and nine members appointed by the UNC System's Board of Governors.

The Trust Fund establishes claim liabilities based on estimates of the ultimate cost of claims (including future expenses and claim adjustment expenses) that have been reported but not settled and of claims incurred but not reported. Claim liabilities are recomputed annually based on an independent actuary's study to produce current estimates that reflect recent settlements, claims frequency, inflation, and other factors. Participant assessments are determined at a level to fund claim liabilities, discounted for future investment earnings. Each participant is required by statute to maintain a fund balance of \$100,000 at all times. Participants are subject to additional premium assessments in the event of deficiencies.

For the period July 1, 2013 through June 30, 2014, the Trust Fund provided coverage on an occurrence basis of \$3,000,000 per individual and \$7,000,000 in the aggregate per claim. Effective July 1, 2006, in lieu of purchasing commercial reinsurance, participants contributed approximately \$10,000,000 to a reimbursement fund for future losses. Prior to July 1, 2006, the Trust Fund entered into an excess of loss agreement with an unaffiliated reinsurer.

For the fiscal year ending June 30, 2014, the Trust Fund purchased a direct insurance policy to cover the first \$1,000,000 per occurrence and \$3,000,000 in the aggregate for dental residents. North Carolina General Statutes Chapter 116 was amended during 1987 to authorize the Trust Fund to borrow necessary amounts up to \$30,000,000, in the event that the Trust Fund may have insufficient funds to pay existing and future claims. Any such borrowing would be repaid from the assets and revenues of program participants. No line of credit or borrowing has been established pursuant to this authorization. The

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Council believes adequate funds are on deposit in the Trust Fund to meet estimated losses based upon the results of the independent actuary's report.

The Trust Fund has purchased annuity contracts to settle claims for which the claimant has signed an agreement releasing the Fund from further obligation. The related claim liabilities have been removed from estimated malpractice costs.

The Council may choose to terminate the Trust Fund, or the respective participants may choose to terminate their participation. In the event of such termination by either the Council or a participant, an updated actuarial study will be performed to determine amounts due to or from the participants based on loss experience up to the date of termination.

At June 30, 2014, University assets in the Trust Fund totaled \$28,053,080 while University liabilities totaled \$21,595,850 resulting in net assets of \$6,457,230.

Additional disclosures about the funding status and obligations of the Trust Fund are set forth in the Audited Financial Statements of the Liability Insurance Trust Fund. Copies of this report may be obtained from The University of North Carolina Health Care System, 211 Friday Center Drive, Hedrick Building, Room 2029, Chapel Hill, NC 27517.

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 0.16% for the current fiscal year.

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 16 - COMMITMENTS AND CONTINGENCIES

A. Commitments - The University has commitments of \$85,016,077 for various capital improvements projects that include construction and completion of new buildings, and renovations of existing buildings.

The UNC Investment Fund, LLC (UNC Investment Fund) has entered into agreements with limited partnerships to invest capital. These agreements represent the funding of capital over a designated period of time and are subject to adjustments. As of June 30, 2014, the UNC Investment Fund had approximately \$705,910,512 unfunded committed capital.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

B. Pending Litigation and Claims – The University 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. University management believes that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.

C. Other Contingent Receivables – The University has received notification of other gifts and grants for which funds have not been disbursed by the resource provider and for which conditions attached to the gift or grant have not been satisfied or, in the case of permanent endowments, cannot begin to be satisfied. In accordance with accounting principles generally accepted in the United States of America, these amounts have not been recorded on the accompanying financial statements. The purpose and amount of other contingent receivables at year end are as follows:

<u>Purpose</u>	<u>Amount</u>
Pledges to permanent endowments	<u>\$ 32,781,394</u>

NOTE 17 - RELATED PARTIES

There are 14 separately incorporated nonprofit foundations associated with the University. These foundations are the Botanical Garden Foundation, Inc., The Dental Alumni Association, Inc., The Dental Foundation of North Carolina, Inc., The Educational Foundation, Inc., The General Alumni Association, The School of Government Foundation, Inc., The Morehead-Cain Scholarship Fund, The Pharmacy Foundation of North Carolina, Inc., The School of Journalism and Mass Communication Foundation of North Carolina, Inc., The University of North Carolina at Chapel Hill Public Health Foundation, Inc., The University of North Carolina at Chapel Hill School of Nursing Foundation, Inc., The School of Social Work Foundation, Inc., James B. Hunt, Jr. Institute for Educational Leadership and Policy Foundation, Inc. and Carolina for Kibera, Inc. Some of these organizations serve, in conjunction with the University's component units (See Note 1A), as the primary fundraising arm of the University through which individuals, corporations, and other organizations support University programs by providing scholarships, fellowships, faculty salary supplements, and unrestricted funds to specific colleges and the University's overall academic environment. The alumni associations provide educational opportunities or other services to alumni. The University's financial statements do not include the assets, liabilities, net position, or operational transactions of these

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

organizations, except for support from each organization to the University. This support totaled \$30,526,004 for the year ended June 30, 2014.

NOTE 18 - INVESTMENT IN JOINT VENTURE

The University is a member of the Southern Observatory for Astronomical Research Consortium (SOAR), a joint venture accounted for under the equity method. The University is partners with Michigan State University, the National Optical Astronomy Observatory, and the Ministry of Science, Technology and Innovation of the Federal Republic of Brazil. SOAR designed, constructed, and now operates a 4.1-meter telescope with instrumentation and related support buildings located at Cerro Pachon, a mountain in central Chile. The SOAR agreement allocates the University 16.7% of observing time until 2023. The audited financial statements for SOAR may be obtained from the University Controller's Office, Campus Box 1270, Chapel Hill, NC 27599-1270, or by calling (919) 962-1370.

NOTE 19 - BLENDED COMPONENT UNITS

Condensed combining information for the University's blended component units for the year ended June 30, 2014, is presented as follows:

*Condensed Statement of Net Position
June 30, 2014*

	University of North Carolina at Chapel Hill**	UNC Investment Fund, LLC	The University of North Carolina at Chapel Hill Foundation Investment Fund, Inc.	The University of North Carolina at Chapel Hill Foundation, Inc.	UNC Intermediate Pool, LLC	Other Blended Component Units *	Eliminations	Total
ASSETS								
Current Assets	\$ 1,528,609,909	\$ 14,055,731	\$ 0	\$ 29,639,962	\$ 95,797,759	\$ 29,211,055	\$ 0	\$ 1,697,314,416
Capital Assets	3,060,872,144			48,271,125		7,986,092		3,117,129,361
Other Noncurrent Assets	(846,008,728)	4,213,998,685	2,641,333,871	329,641,289	381,957,410	135,008,567	(2,999,185,957)	3,856,745,137
Total Assets	<u>3,743,473,325</u>	<u>4,228,054,416</u>	<u>2,641,333,871</u>	<u>407,552,376</u>	<u>477,755,169</u>	<u>172,205,714</u>	<u>(2,999,185,957)</u>	<u>8,671,188,914</u>
Deferred Outflows of Resources	84,866,413							84,866,413
LIABILITIES								
Current Liabilities	414,281,604	5,464,410	1,299,382	7,513,933	7,989,464	2,612,008	(1,299,382)	437,861,419
Noncurrent Liabilities	2,017,174,064			82,124,563		10,612,378	1,435,436,054	3,545,347,059
Total Liabilities	<u>2,431,455,668</u>	<u>5,464,410</u>	<u>1,299,382</u>	<u>89,638,496</u>	<u>7,989,464</u>	<u>13,224,386</u>	<u>1,434,136,672</u>	<u>3,983,208,478</u>
Deferred Inflows of Resources								
NET POSITION								
Net Investment in Capital Assets	1,637,669,699			23,641,117		1,620,406		1,662,931,222
Restricted - Nonexpendable	(2,413,056,761)	4,222,590,006	2,640,034,489	134,826,154	469,765,705	103,767,588	(4,433,322,629)	724,604,552
Restricted - Expendable	1,317,383,799			113,010,633		34,083,146		1,464,477,578
Unrestricted	854,887,333			46,435,976		19,510,188		920,833,497
Total Net Position	<u>\$ 1,396,884,070</u>	<u>\$ 4,222,590,006</u>	<u>\$ 2,640,034,489</u>	<u>\$ 317,913,880</u>	<u>\$ 469,765,705</u>	<u>\$ 158,981,328</u>	<u>(4,433,322,629)</u>	<u>\$ 4,772,846,849</u>

* Other Blended Component Units include UNC Management Company, Inc., The Kenan-Flagler Business School Foundation, U.N.C. Law Foundation, Inc., and The University of North Carolina at Chapel Hill School of Education Foundation, Inc.

** Negative balances for the University reflect net inter-entity receivables for blended entities where such balances are not separately tracked and reported on.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Condensed Statement of Revenues, Expenses, and Changes in Net Position For the Fiscal Year Ended June 30, 2014

	University of North Carolina at Chapel Hill**	UNC Investment Fund, LLC	The University of North Carolina at Chapel Hill Foundation Investment Fund, Inc.	The University of North Carolina at Chapel Hill Foundation, Inc.	UNC Intermediate Pool, LLC	Other Blended Component Units *	Eliminations	Total
OPERATING REVENUES								
Sales and Services	\$ 1,098,796,809	\$ 0	\$ 0	\$ 12,026,924	\$ 0	\$ 21,459,669	\$ 0	\$ 1,132,283,402
Other Operating Revenues	819,412,154			3,994,605		442,036		823,848,795
Total Operating Revenues	1,918,208,963			16,021,529		21,901,705		1,956,132,197
OPERATING EXPENSES								
Operating Expenses	2,488,627,020			25,176,824		27,298,427		2,541,102,271
Depreciation	130,438,445							130,438,445
Total Operating Expenses	2,619,065,465			25,176,824		27,298,427		2,671,540,716
Operating Income (Loss)	(700,856,502)			(9,155,295)		(5,396,722)		(715,408,519)
NONOPERATING REVENUES (EXPENSES)								
Investment Income	(128,476,980)	659,559,258	374,578,140	40,756,370	9,875,630	18,807,146	(716,727,327)	258,372,237
Other, Net	235,774,400	19,259,853	(72,438,022)	(6,025,715)	459,890,075	(6,073,228)	72,438,022	702,825,385
Net Nonoperating Revenues (Expenses)	107,297,420	678,819,111	302,140,118	34,730,655	469,765,705	12,733,918	(644,289,305)	961,197,622
Additions to Endowments	13,423,888			10,183,768		2,000,848		25,608,504
Increase in Net Position	(580,135,194)	678,819,111	302,140,118	35,759,128	469,765,705	9,338,044	(644,289,305)	271,397,607
NET POSITION								
Net Position, July 1, 2013	1,977,019,264	3,543,770,895	2,337,894,371	282,154,752	0	149,643,284	(3,789,033,324)	4,501,449,242
Net Position, June 30, 2014	\$ 1,396,884,070	\$ 4,222,590,006	\$ 2,640,034,489	\$ 317,913,880	\$ 469,765,705	\$ 158,981,328	\$ (4,433,322,629)	\$ 4,772,846,849

* Other Blended Component Units include UNC Management Company, Inc., The Kenan-Flagler Business School Foundation, U.N.C. Law Foundation, Inc., and The University of North Carolina at Chapel Hill School of Education Foundation, Inc.

** Negative balances for the University reflect net inter-entity receivables for blended entities where such balances are not separately tracked and reported on.

Condensed Statement of Cash Flows June 30, 2014

	University of North Carolina at Chapel Hill	The University of North Carolina at Chapel Hill Foundation, Inc.	Other Blended Component Units *	Total
Net Cash Provided by Operating Activities	\$ (643,753,114)	\$ (7,472,834)	\$ (3,064,605)	\$ (654,290,553)
Net Cash Used by Noncapital Financing Activities	1,031,686,056	9,332,805	(1,991,966)	1,039,026,895
Net Cash Used by Capital and Related Financing Activities	(158,608,786)	(7,971,195)	(1,372,992)	(167,952,973)
Net Cash Provided by Investing Activities	(601,645,800)	5,581,390	5,203,775	(590,860,635)
Net Increase (Decrease) in Cash and Cash Equivalents	(372,321,644)	(529,834)	(1,225,788)	(374,077,266)
Cash and Cash Equivalents, July 1, 2013	1,018,714,444	29,923,296	23,072,808	1,071,710,548
Cash and Cash Equivalents, June 30, 2014	\$ 646,392,800	\$ 29,393,462	\$ 21,847,020	\$ 697,633,282

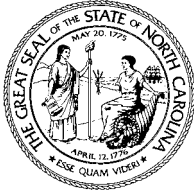
* Other Blended Component Units include UNC Management Company, Inc., The Kenan-Flagler Business School, U.N.C. Law Foundation, Inc., and The University of North Carolina at Chapel Hill School of Education Foundation, Inc.

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

NOTE 20 - SUBSEQUENT EVENTS

On October 9, 2014, the Board of Governors of the University of North Carolina System issued \$265,600,000 in Series 2014 taxable, fixed-rate bonds. These bonds will bear interest from that date. Interest on the bonds will be payable semiannually on each December 1 and June 1, commencing on December 1, 2014. The structure contains serial bonds that will mature from December 1, 2016 to December 1, 2020 issued with coupon rates ranging from 0.76% to 2.36%, and term bonds that with a final maturity of December 1, 2034 issued at a coupon rate of 3.85%. The bonds were issued to provide for the advance refunding of \$250,000,000 in par value of the General Revenue Bonds, Series 2005A. The all-in true interest cost of the refunding bonds is 3.87%, representing a net present value savings to the University of \$21,900,783.17.

Office of the State Auditor



Beth A. Wood, CPA
State Auditor

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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 Trustees
The University of North Carolina at Chapel Hill
Chapel Hill, 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 University of North Carolina at Chapel Hill, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component units, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the University's basic financial statements, and have issued our report thereon dated November 14, 2014. Our report includes a reference to other auditors who audited the financial statements of the UNC Investment Fund, LLC and the discretely presented component units, as described in our report on the University's financial statements. The financial statements of the UNC Investment Fund, LLC and the discretely presented component units were not audited in accordance with *Government Auditing Standards*, and accordingly, this report does not include reporting on internal control over financial reporting or instances of reportable noncompliance associated with the UNC Investment Fund, LLC and the discretely presented component units.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the University'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 University's internal control. Accordingly, we do not express an opinion on the effectiveness of the University'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

**INDEPENDENT AUDITOR'S REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
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GOVERNMENT AUDITING STANDARDS (CONCLUDED)**

deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the University'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.

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 University'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 University'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 University's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Beth A. Wood, CPA
State Auditor

Raleigh, North Carolina

November 14, 2014

ORDERING INFORMATION

Copies of this report may be obtained by contacting the:

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For additional information contact:

Bill Holmes

Director of External Affairs