

# STATE OF NORTH CAROLINA

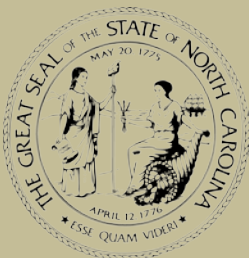
OFFICE OF THE STATE AUDITOR  
BETH A. WOOD, CPA



## NORTH CAROLINA STATE UNIVERSITY

RALEIGH, NORTH CAROLINA  
FINANCIAL STATEMENT AUDIT REPORT  
FOR THE YEAR ENDED JUNE 30, 2016

A CONSTITUENT INSTITUTION OF THE UNIVERSITY OF NORTH CAROLINA SYSTEM  
AND A COMPONENT UNIT OF THE STATE OF NORTH CAROLINA



**NC OSA**  
The Taxpayers' Watchdog

STATE OF NORTH CAROLINA  
**Office of the State Auditor**



**Beth A. Wood, CPA**  
State Auditor

2 S. Salisbury Street  
20601 Mail Service Center  
Raleigh, NC 27699-0600  
Telephone: (919) 807-7500  
Fax: (919) 807-7647  
<http://www.ncauditor.net>

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## AUDITOR'S TRANSMITTAL

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The Honorable Pat McCrory, Governor  
The General Assembly of North Carolina  
Board of Trustees, North Carolina State University

We have completed a financial statement audit of North Carolina State University for the year ended June 30, 2016, 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



Beth A. Wood, CPA  
State Auditor

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Article V, Chapter 147 of the *North Carolina General Statutes*, gives the Auditor broad powers to examine all books, records, files, papers, documents, and financial affairs of every state agency. The Auditor also has the power to summon people to produce records and to answer questions under oath.



# INDEPENDENT AUDITOR'S REPORT

STATE OF NORTH CAROLINA  
**Office of the State Auditor**



**Beth A. Wood, CPA**  
State Auditor

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Fax: (919) 807-7647  
<http://www.ncauditor.net>

## **INDEPENDENT AUDITOR'S REPORT**

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Board of Trustees  
North Carolina State University  
Raleigh, North Carolina

### Report on the Financial Statements

We have audited the accompanying financial statements of North Carolina State University (University), 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, 2016, 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 NC State Investment Fund, Inc., which represent 18 percent, 10 percent, and 1 percent, respectively, of the assets, net position, and revenues of the University; nor the financial statements of the North Carolina State University Foundation, Inc., the NC State Student Aid Association, Inc., or The North Carolina Agricultural 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, is based solely on the reports 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 assurance about whether the financial statements are free from material

misstatement. The financial statements of the North Carolina State University Foundation, Inc., the NC State Student Aid Association, Inc., and The North Carolina Agricultural 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 respective financial position of North Carolina State University and its discretely presented component units, as of June 30, 2016, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### Emphasis of Matter

As discussed in Note 20 to the financial statements, during the year ended June 30, 2016, the University adopted new accounting guidance, Governmental Accounting Standards Board Statement No. 72 – *Fair Value Measurement and Application*. Our opinion is not modified with respect to this matter.

### Other Matters – Required Supplementary Information

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

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 31, 2016 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

October 31, 2016



# **MANAGEMENT'S DISCUSSION AND ANALYSIS**



## Introduction

Management's Discussion and Analysis of the financial report provides an overview of the accompanying basic financial statements. It includes comparative financial analysis with discussion of significant changes from the prior year. The overview also includes information on currently known facts, decisions, or conditions affecting the financial affairs of the University.

## Financial Highlights

NC State University's net position increased by \$73.4 million to \$1.99 billion in fiscal year 2016. Net position represents the University's equity. It is the residual of all the other elements of the statement of financial position, the assets and deferred outflows of resources less liabilities and deferred inflows of resources. As required by the Governmental Accounting Standards Board (GASB), NC State University implemented GASB Statement No. 72, *Fair Value Measurement and Application* in fiscal year 2016. Based on GASB Statement No. 72, the University restated Endowment Fund holdings in real estate from investments to capital assets. Although total net position was not affected, the net position balances related to the reclassified real estate were moved to net investment in capital assets. Using the restated 2015 balances, unrestricted net position grew \$33.9 million supported by increases in tuition and fees and sales and services. Restricted expendable net position increased \$15.5 million, driven by the increase in capital projects net position funded by capital appropriations and commercial paper proceeds. Restricted nonexpendable net position increased \$14.7 million, and net investment in capital assets increased by \$9.3 million.

Revenues increased by \$43.1 million or 3.0%, to \$1.49 billion in fiscal year 2016. Revenues represent amounts received or accrued that are operating, nonoperating, or other revenues on the accompanying financial statements. Increases in tuition and fees, state appropriations, sales and services and research contracts and grants were major factors in the revenue growth. These increases were partially offset by decreases in investment income and student financial aid grants.

Operating expenses grew 5.0% in 2016, up \$67.7 million compared to fiscal year 2015. Operating expenses represent amounts paid or accrued for operating purposes. Instruction, research, auxiliary enterprises, institutional support and depreciation showed the largest increases, while other functional categories had small increases or decreases.

## Using the Financial Statements

The University's financial statements are 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 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.

North Carolina State University is a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*. Also, NC State blends two component units as if they were part of the University, and three entities are reported as

discretely presented component units based on the nature and significance of their relationship to the University. Note 1A provides detailed information on the University's financial reporting entity.

The University's three financial statements are used to evaluate financial position as of June 30<sup>th</sup> and the results of operations for the fiscal year then ended. The *Statement of Net Position* provides information relative to the evaluation of financial position. The *Statement of Revenues, Expenses, and Changes in Net Position* provides information relative to the evaluation of the results of operations. Its ending net position agrees to the total net position on the *Statement of Net Position*.

The financial statements also include a *Statement of Cash Flows*. This statement is used to identify the University's sources and uses of cash. The ending cash on the *Statement of Cash Flows* agrees to the total cash reported on the *Statement of Net Position*. Also, this statement reconciles the net operating loss reported in the *Statement of Revenues, Expenses, and Changes in Net Position* to the net cash used by operating activities.

In using the financial statements, the *Notes to the Financial Statements* accompanying the financial statements should be read in conjunction with the financial statements. The notes provide information regarding the significant accounting principles applied in the financial statements, authority for and associated risk of deposits and investments, detailed information on long-term liabilities, detailed information on accounts receivable, accounts payable, revenues and expenses, required information on pension plans and other postemployment benefits, insurance against losses, commitments and contingencies, and accounting changes. If necessary, the disclosures include a discussion of adjustments to prior periods and events subsequent to the University's financial statement period. Overall, these disclosures provide information to better understand details, risk, and uncertainty associated with amounts reported in the financial statements.

### **Comparative Condensed Financial Statement Information**

#### **Statement of Net Position**

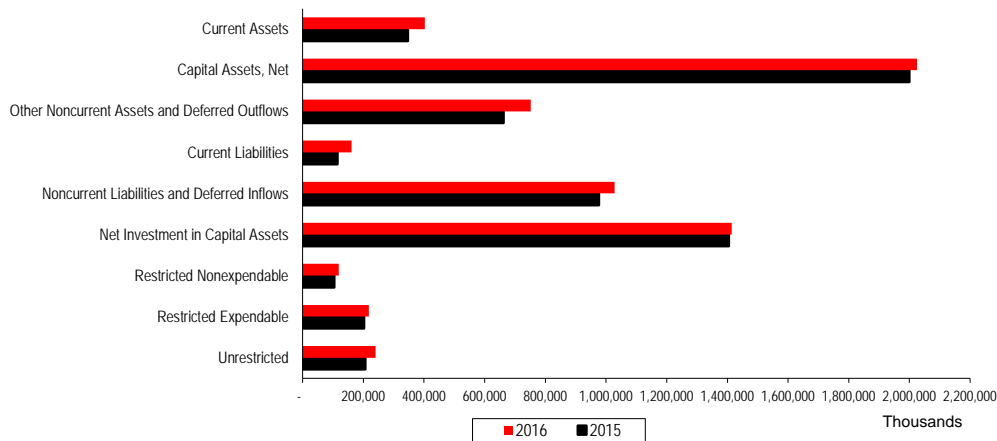
The *Statement of Net Position* provides information regarding the University's assets, deferred outflows and inflows of resources, liabilities, and net position as of June 30, 2016. Asset and liability balances are classified as either current or noncurrent. Assets classified as current are those that are available to pay for current liabilities or current year expenditures. Liabilities classified as current are those that are due and payable in the next fiscal year. The net position balances are classified as either net investment in capital assets, restricted or unrestricted. In addition, net position balances classified as restricted are classified as either nonexpendable or expendable. Overall, the *Statement of Net Position* provides information to evaluate the financial strength of the University and its ability to meet current and long-term obligations.

Following is a comparative analysis on the condensed balances reported in the *Statement of Net Position* as of June 30, 2016 and June 30, 2015. The 2015 balances were restated in response to the fiscal year 2016 implementation of GASB Statement No. 72, *Fair Value Measurement and Application*. GASB Statement No. 72 defines investments as assets held primarily for the purpose of income or profit and as having a present service capacity based solely on the ability to generate cash or to be sold to generate cash. The NC State Endowment Fund held real property that had been classified as investments in real estate. However, this real estate had operational purposes, not just the generation of profit. Based

on the provisions of GASB Statement No. 72, \$21.9 million in investments were reclassified to capital assets and the related net position moved to Net Investments in Capital Assets.

	2016	2015 (As Restated)	Increase/ (Decrease)
<b>Assets</b>			
Current Assets	\$ 403,005,557	\$ 347,304,826	\$ 55,700,731
Capital Assets, Net	2,025,328,291	1,999,505,101	25,823,190
Other Noncurrent Assets	706,572,216	619,611,354	86,960,862
<b>Total Assets</b>	<b>3,134,906,064</b>	<b>2,966,421,281</b>	<b>168,484,783</b>
<b>Deferred Outflows of Resources</b>			
Accumulated Decrease in Fair Value of Hedging Derivatives	13,837,267	11,808,389	2,028,878
Deferred Outflows Related to Pensions	31,284,957	30,789,269	495,688
<b>Total Deferred Outflows of Resources</b>	<b>45,122,224</b>	<b>42,597,658</b>	<b>2,524,566</b>
<b>Liabilities</b>			
Current Liabilities	161,035,104	114,987,149	46,047,955
Noncurrent Liabilities:			
Long Term Liabilities	682,735,164	649,413,731	33,321,433
Other Noncurrent Liabilities	327,500,338	235,849,957	91,650,381
<b>Total Liabilities</b>	<b>1,171,270,606</b>	<b>1,000,250,837</b>	<b>171,019,769</b>
<b>Deferred Inflows of Resources</b>			
Deferred Inflows Related to Pensions	17,506,004	90,871,239	(73,365,235)
<b>Net Position</b>			
Net Investment in Capital Assets	1,413,824,172	1,404,535,777	9,288,395
Restricted			
Nonexpendable	119,263,539	104,600,621	14,662,918
Expendable	217,731,322	202,260,477	15,470,845
Unrestricted	240,432,645	206,499,988	33,932,657
<b>Total Net Position</b>	<b>\$ 1,991,251,678</b>	<b>\$ 1,917,896,863</b>	<b>\$ 73,354,815</b>

The following graph illustrates the assets, deferred outflows, liabilities and net position of the University as of June 30, 2016, as compared to restated June 30, 2015 balances.



Assets totaled \$3.13 billion, an increase of \$168.5 million over the prior year. This change in assets includes an increase in current assets of \$55.7 million, capital asset growth of \$25.8 million and an increase in other noncurrent assets of \$87.0 million.

Current assets increased by \$55.7 million in fiscal year 2016. This increase was primarily the result of a \$53.8 million increase in cash and cash equivalents, driven by the management flexibility carryforward change from 2.5% to 5% and the \$32.6 million liquidation of an Intermediate Term Fund investment on June 30, 2016. Accounts receivable grew by \$6.2 million but this was largely offset by a \$5.2 million decrease in due from primary government. The drop in due from primary government was related to state contracts and grants, and the largest decreases were in amounts due from the Department of Transportation and the Department of Public Instruction.

The capital asset growth of \$25.8 million is due to construction funding from commercial paper financing, capital appropriations and capital grants and gifts. The University added \$30 million in commercial paper funding in 2016, received \$9.0 million in capital appropriations resources and \$9.5 million in capital gifts and grants. Further discussion of capital asset activity is included below.

The \$87.0 million increase in other noncurrent assets is made up of increases in restricted cash and partially offsetting decreases in other long-term investments. Restricted cash and cash equivalents increased \$116.0 million in fiscal year 2016. This large increase was caused by the Hofmann timber deed proceeds of \$78.0 million received on June 30 and capital allotment increases of \$29.2 million. Other long-term investments decreased \$33.2 million with the \$32.6 million liquidation of an Intermediate Term Fund investment.

The deferred outflows of resources for the University's swap agreements and the deferred outflows for pensions are shown in a separate section of the financial statements. GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which was implemented in fiscal year 2013, established deferred sections of the financial statements. Most of the \$2.5 million increase in deferred outflows is related to the accumulated decrease in the fair value of hedging derivatives account. This \$2.0 million change is due to market fluctuations. The deferred outflows for pensions account reflects the University's allocated portion of deferred outflows for the TSERS cost-sharing pension plan. Amounts in this account are amortized over time as pension expense. The \$0.5 million increase in the deferred outflows of pension for pensions is due to changes in the pension contributions and the University's proportionate share of contributions to the plan.

Liabilities totaled \$1.17 billion, an increase of \$171.0 million over the prior year. The increase in liabilities is attributable to an increase in current liabilities of \$46.0 million and an increase in noncurrent liabilities of \$125.0 million.

Current liabilities totaled \$161.0 million. These liabilities include accounts payable and accrued liabilities, due to other entities, unearned revenue, and the current portion of University debt. The current liabilities increase of \$46.0 million was primarily caused by the increase in short-term debt. The University issued an additional \$30.0 million in commercial paper in fiscal year 2016 to help fund Reynolds Coliseum and Carmichael Gym renovations. Accounts payable and accrued liabilities also increased \$9.8 million, mainly due to a \$5.8 million increase in construction payables and \$1.0 million in timber deed payables. Unearned revenue rose \$5.6 million, with the largest increases in advance football ticket sales, contract and grant unearned revenues and the current part of the Hofmann Forest timber deed earnings.

Noncurrent liabilities totaled \$1.01 billion, and include deposits payable, funds held for other entities, funds held in trust in the investment pool, unearned revenue, long-term liabilities and the hedging derivative liability. The primary factors in the \$125.0 million increase in noncurrent liabilities was unearned revenue and long-term liabilities. The \$78.0 million Hofmann Forest timber deed drove the large new unearned revenue balance. Long-term liabilities increased \$33.3 million, with the pension liability being the major cause. The net pension liability rose \$53.7 million due to differences in the expected and actual earnings in the Teachers' and State Employees' Retirement System (TSERS) pension plan. Still within long-term liabilities, the pension liability increase was partially offset by a \$14.8 million decrease in bonds payable and \$4.4 million decrease in notes payable. These decreases are due to regular principal payments and also paying off the Series 2005A bonds and a note on the golf course clubhouse. Funds held for others and funds held in trust for pool participants increased by a total of \$13.4 million, driven by increases in deposits by foundations. The hedging derivative liability increases and decreases based on market values and showed a \$2.0 million increase in fiscal year 2016. Other noncurrent liabilities increased or decreased by small amounts.

Deferred inflows for pensions was new for fiscal year 2015, required by the implementation of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. This \$17.5 million deferred inflows of resources is another allocation of the TSERS cost-sharing pension plan balances. The \$73.4 million drop in deferred inflows is driven by the higher pension liability related to the difference between projected and actual investment earnings. These deferred inflows for pensions are amortized over time as pension expense.

Net position totaled \$1.99 billion, an increase of \$73.4 million over the prior year. Unrestricted net position increased by \$33.9 million, with major factors being tuition and fees and sales and services revenues. Restricted expendable net position rose \$15.5 million and the largest increase was in capital projects net position, which is related to the additional commercial paper and capital appropriations funding. Restricted nonexpendable net position grew by \$14.7 million with endowed professorships showing the largest gain due to new gifts and matching funding from UNC General Administration. Net investment in capital assets rose \$9.3 million to \$1.41 billion as capital projects were completed and equipment was capitalized during the fiscal year.

The University's current assets are more than sufficient to cover current liabilities, with a ratio of 2.5 times compared to 3.0 times in the prior year. The University's total assets are significantly more than the University's liabilities with a ratio of 2.7 times as compared to 3.0 times in the prior year. These financial ratios are indicators of NC State's financial strength and its ability to meet current and long-term obligations.

### **Statement of Revenues, Expenses, and Changes in Net Position**

The *Statement of Revenues, Expenses, and Changes in Net Position* provides information regarding the University's activities for the year ending June 30, 2016. The activity balances are classified as operating, nonoperating, or other revenues, expense, gains or losses. Activities classified as operating include all revenues of the University except those considered nonoperating or those associated with funds received to enhance capital assets or permanent endowments. Operating expenses are all expenses except those related to interest expense on financing activities, loss on disposal of capital assets, and investment expenses (shown as net against investment income). Activities classified as nonoperating include state appropriations, noncapital gifts and grants revenue, investment income (net of

investment expenses), and gains or losses on disposal of capital assets. Activities classified as other include capital gifts or grants and additions to permanent endowments. Overall, the *Statement of Revenues, Expenses, and Changes in Net Position* provides information to evaluate the University's management of operations and maintenance of financial strength.

Following is a comparative analysis on the condensed balances reported in the *Statement of Revenues, Expenses, and Changes in Net Position* for the fiscal years ended June 30, 2016, and June 30, 2015.

	2016	2015	Increase/ (Decrease)
<b>Operating Revenues</b>			
Student Tuition and Fees, Net	\$ 291,175,319	\$ 270,139,559	\$ 21,035,760
Federal Appropriations	13,847,694	16,930,633	(3,082,939)
Grants and Contracts	278,330,058	269,113,771	9,216,287
Sales and Services, Net	238,447,749	224,940,804	13,506,945
Other	14,551,643	18,427,520	(3,875,877)
<b>Total Operating Revenues</b>	<b>836,352,463</b>	<b>799,552,287</b>	<b>36,800,176</b>
<b>Operating Expenses</b>			
Salaries and Benefits	857,250,567	829,085,258	28,165,309
Supplies and Materials	127,911,047	118,371,721	9,539,326
Services	251,765,902	223,104,891	28,661,011
Scholarships and Fellowships	43,820,372	45,376,020	(1,555,648)
Utilities	32,028,497	35,750,321	(3,721,824)
Depreciation/Amortization	88,721,461	82,078,817	6,642,644
<b>Total Operating Expenses</b>	<b>1,401,497,846</b>	<b>1,333,767,028</b>	<b>67,730,818</b>
Net Operating Loss	(565,145,383)	(534,214,741)	30,930,642
<b>Nonoperating Revenues (Expenses)</b>			
State Appropriations	502,533,982	481,548,424	20,985,558
Noncapital Grants - Student Financial Aid	44,705,577	48,061,723	(3,356,146)
Other Noncapital Grants and Gifts	72,024,499	68,457,698	3,566,801
Investment Income	1,569,316	19,742,861	(18,173,545)
Other	(14,855,864)	(12,785,462)	2,070,402
<b>Net Nonoperating Revenues</b>	<b>605,977,510</b>	<b>605,025,244</b>	<b>952,266</b>
<b>Gain Before Other Revenues</b>	<b>40,832,127</b>	<b>70,810,503</b>	<b>(29,978,376)</b>
Capital Appropriations, Gifts, and Grants	18,483,657	18,518,437	(34,780)
Additions to Permanent Endowments	14,039,031	11,524,687	2,514,344
<b>Increase in Net Position</b>	<b>73,354,815</b>	<b>100,853,627</b>	<b>(27,498,812)</b>
<b>Beginning Net Position</b>	<b>1,917,896,863</b>	<b>1,817,043,236</b>	<b>100,853,627</b>
<b>Ending Net Position</b>	<b>\$ 1,991,251,678</b>	<b>\$ 1,917,896,863</b>	<b>\$ 73,354,815</b>

Fiscal year 2015-2016 total revenues are \$1,491,595,178 and total expenses are \$1,418,240,363.

Fiscal year 2014-2015 total revenues are \$1,448,540,778 and total expenses are \$1,347,687,151.

## Operating and Nonoperating Activities

The following illustrates the relationships of operating and nonoperating revenue sources and expense functions to total revenue/expenses for the fiscal year 2016 and 2015, and the consistency of relationships between the two years. The pension expense was allocated to the other functional captions for fiscal year 2015 to be consistent with the required presentation for fiscal year 2016 reporting.

**Operating and Nonoperating Revenues**

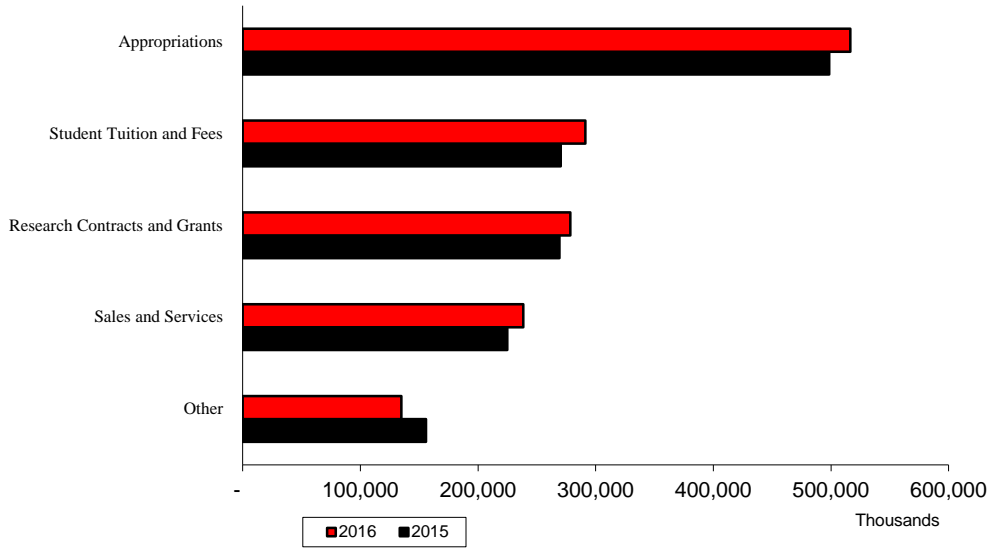
Title	% to Total 2016	% to Total 2015
State Appropriations	35%	34%
Research Contracts and Grants	19%	19%
Student Tuition and Fees	20%	19%
Sales and Services	16%	16%
Noncapital Grants and Gifts	8%	8%
Federal Appropriations	1%	1%
Other	1%	3%
Total	100%	100%

**Operating and Nonoperating Expenses**

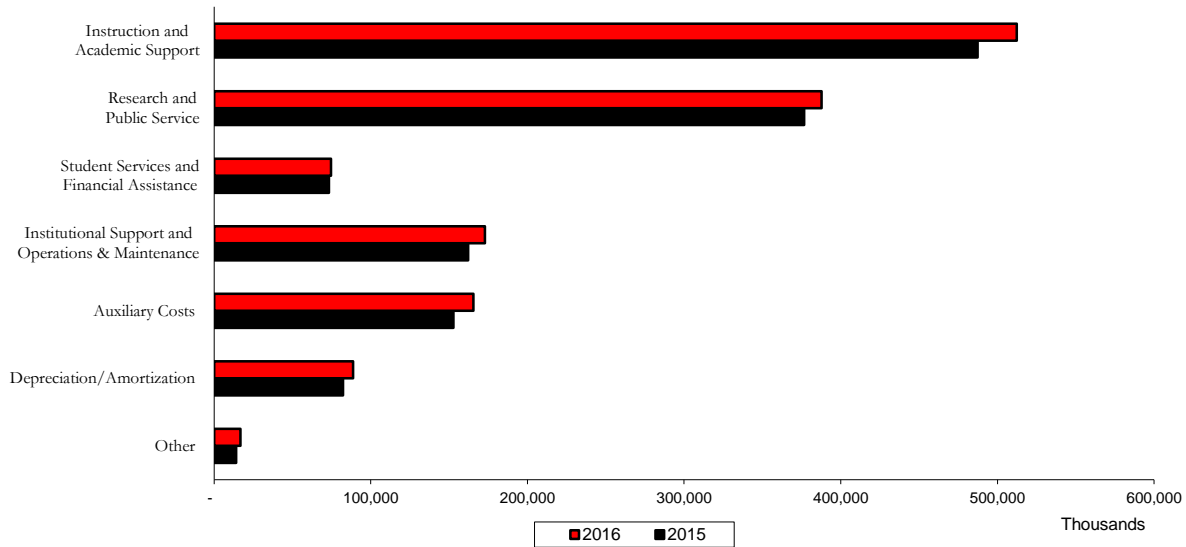
Title	% to Total 2016	% to Total 2015
Instruction	30%	30%
Research	19%	19%
Public Service	8%	9%
Auxiliary Enterprises	12%	11%
Operations & Maintenance of Plant	6%	6%
Academic Support	6%	6%
Institutional Support	7%	6%
Depreciation/Amortization	6%	6%
Student Financial Aid	3%	4%
Student Services	2%	2%
Other	1%	1%
Total	100%	100%

The following graphs illustrate the University's operating and nonoperating revenues/expenses by source/function (*in thousands*). As in the chart above, the pension expense was allocated to the other functional captions for fiscal year 2015, to be consistent with the required fiscal year 2016 reporting presentation.

**Operating and Nonoperating Revenues**



**Operating and Nonoperating Expenses**



Total revenues (operating, nonoperating, and other) increased \$43.1 million or 3.0% compared to the prior year. Student tuition and fees increased \$21.0 million, as rates increased in 2016 for resident and nonresident students. The largest tuition change was a 6% increase for nonresident undergraduates. State appropriations were also up by



\$21.0 million or 4.4%, due to enrollment growth, employee bonus funding and other small adjustments. Sales and services revenues grew \$13.5 million or 6.0%. Dining grew \$6.6 million and there were smaller increases in various services including veterinary services, the bookstore, housing and athletics. Research contracts and grants rose by \$9.2 million, mostly in federal contracts and grants. Noncapital gifts were up slightly, \$3.1 million or 4.5%. However, investment income decreased \$18.2 million, with \$16.2 million in unrealized losses in the fluctuating market. Also, other operating revenues decreased by \$3.9 million, driven by less patent royalty income. Student financial aid grants dropped \$3.4 million, with decreases in federal and state funding.

Total expenses (operating and nonoperating) increased \$70.6 million or 5.2% compared to the prior year. Salaries and benefits increased \$28.2 million or 3.4% in 2016. The largest salary increases were in instruction, \$16.7 million, and auxiliary enterprises, \$4.8 million. There was a \$750 legislative bonus in fiscal year 2016 but other salary increases and the related benefits also contributed to the salaries growth. The next largest increase in expenses was in services. Services grew \$28.7 million, driven by increases in subcontracts, repairs, maintenance agreements and communications. Research and instruction showed the largest increases in services. Supplies expenses were also up by 9.5 million or 8.1%. Auxiliary enterprises and operations and maintenance of plant had the largest increases, as some items from construction projects were expensed and completed buildings required more supplies. As capital assets rose, the related depreciation/amortization expense also increased by \$6.6 million or 8.1%. With fewer active construction projects, less interest was capitalized during 2016 so interest and fees on debt rose \$4.8 million. Partially offsetting these expense increases, utilities dropped \$3.7 million or 10.4%, due to lower fuel oil and natural gas spending. Tightening government budgets also affected scholarships and fellowships, which decreased by \$1.6 million as financial aid grants were reduced and more funding was used for tuition and fees, dining and housing.

### **Other Activity**

Other activity totaled \$32.5 million, up \$2.5 million from the prior year. The University received an additional \$9.0 million from the state in capital appropriations. However, capital gifts fell \$9.2 million, as the NC State Student Aid Association, Inc. gave the University the Close-King Indoor Practice Facility in the prior year. Capital grants showed minimal growth but additions to permanent endowment was up \$2.5 million.

### **Capital Assets and Long-Term Debt Activities**

#### **Capital Assets**

The University capitalizes assets that have a value or cost equal to or greater than \$5,000 at the date of acquisition and an expected useful life of more than one year except for internally generated software which is capitalized when the value or cost is \$1,000,000 or greater and other intangible assets which are capitalized when the value or cost is \$100,000 or greater. Repairs and renovations that do not extend the life of the building beyond the expected useful life at acquisition, nor increase the future service potential of the building are expensed and not capitalized.

Machinery and equipment are depreciated over their estimated useful lives, generally 4 to 22 years beginning in the year of acquisition. Buildings and general infrastructure are depreciated over their estimated useful lives, generally 10 to 50 years for buildings and 15 to 75 years for general infrastructure beginning in the year that the construction is completed or,

if purchased after construction, when acquired. Computer software is amortized over a useful life of 2 to 15 years. Land, construction in progress, and computer software in development are nondepreciable capital assets. When a construction project is completed, the capital project costs are moved from the construction in progress account to either buildings or general infrastructure as appropriate.

As shown in the following table, the University increased its net capital assets by \$25.8 million during fiscal year 2016. The 2015 balances were restated for \$21.9 million in investments reclassified to capital assets based on the provisions on GASB Statement No. 72.

	2016	2015 (As Restated)	Increase/ (Decrease)
Land	\$ 62,457,494	\$ 59,544,940	\$ 2,912,554
Construction in Progress	61,591,561	54,956,500	6,635,061
Computer Software in Development	323,600	659,874	(336,274)
Buildings	2,228,388,315	2,161,039,192	67,349,123
Machinery and Equipment	359,435,354	342,643,333	16,792,021
General Infrastructure	207,764,589	205,771,161	1,993,428
Computer Software	20,544,306	17,514,419	3,029,887
Total Capital Assets	2,940,505,219	2,842,129,419	98,375,800
Accumulated Depreciation/Amortization	(915,176,928)	(842,624,318)	72,552,610
Net Capital Assets	<u>\$ 2,025,328,291</u>	<u>\$ 1,999,505,101</u>	<u>\$ 25,823,190</u>

In addition to costs incurred, the University had \$20.7 million in outstanding commitments for construction projects with an additional \$0.2 million in software in development contract commitments as of June 30, 2016.

During fiscal year 2016, NC State continued construction on new facilities and work on renovations to modernize the campus. Funding for these improvements came from funds provided by University debt financing and state-issued bonds and certificates of participation.

The University completed all work on Talley Student Center in fiscal year 2016. This completed a multi-year renovation/new building project that is now the hub and heart of the University. Talley is now a foundation for student life at NC State, providing extracurricular opportunities, employment and academic resources that will propel students to success.

The Carmichael Gym locker room renovation was completed in June 2016. The upgrades add approximately 5,000 square feet of fitness center space and repurpose underutilized and inefficient locker rooms. The upgrade finishes in the locker room provide a "health club" look and feel. The renovations also address facility accessibility and safety deficiencies.

A major classroom SCALE-UP project for Cox Hall was completed in March 2016. The primary goal of the Student-Centered Active Learning Environment with Upside-down Pedagogies (SCALE-UP) Project was to establish a highly collaborative, hands-on, computer-rich, interactive learning environment for large-enrollment courses. This project scope included renovating office space into high-technology classrooms on the first floor. The renovations include modifications to the building infrastructure to accommodate this space including new restrooms and a new lactation room. The renovations provided

Scale-Up audio/visual upgrades and associated equipment closets supplying the digital cabling and “brains” for each classroom. Miles of new cabling was installed for this upgrade.

Scale-Up Classrooms came about as a result of the last decade’s success of adult education, computer-rich classrooms, focused on circles of student dialogue and shared information. Scale-up classrooms are a move away from the pedagogical practice of lectures while using a more engaging approach to student research and discovery.

The Ricks Hall upgrade project is Phase 2 of a two phase project to renovate the third floor of Ricks Hall for the Bioinformatics staff. The project includes architectural and mechanical renovations. The architectural renovations involve selective demolition within the 3rd floor with the installation of new offices with new walls, painting, lighting, floor coverings, and doors. The mechanical renovations involve the installation of new subsurface areaways to serve a new basement mechanical room with new mechanical equipment and a future mechanical room. The project will also install new supply and return ductwork from the basement up to the third floor and new variable air volume terminal units. The mechanical work also includes new fire alarm devices, new standpipes, and new fire protection sprinklers on the third floor. New aluminum framed, energy efficient windows will be installed.

**Long-Term Debt Activities**

The University incurs long-term debt and other liabilities to finance construction projects, to purchase equipment using lease arrangements and to provide for accumulated unused vacation benefits for employees. As shown in the following chart, the University increased its long-term debt during fiscal year 2016.

	2016	2015	Increase/ (Decrease)
Bonds Payable	\$ 484,255,411	\$ 499,043,276	\$ (14,787,865)
Net Pension Liability	78,841,126	25,160,037	53,681,089
Notes Payable	71,817,697	76,194,309	(4,376,612)
Capital Leases Payable	541,177	210,875	330,302
Compensated Absences	67,831,331	68,534,279	(702,948)
Total Long-term Liabilities	<u>\$ 703,286,742</u>	<u>\$ 669,142,776</u>	<u>\$ 34,143,966</u>

Long-term liabilities grew by \$34.1 million, due to the increase in the University’s share of the net pension liability for the Teachers’ and State Employees’ Retirement System (TSERS) plan. The primary cause of the \$53.7 million increase in the net pension liability was the difference in the projected and actual investment earnings in the TSERS plan. Principal payments of notes and bonds partially offset the pension liability increase. The final payments for the General Revenue Bonds, Series 2005A and the Carol Johnson Poole Clubhouse Note were made in fiscal year 2016. Also, the University issued \$64.5 million in North Carolina State University at Raleigh Variable Rate General Revenue Bonds, Series 2015 refunding bonds in a current refunding of \$64.5 million of outstanding North Carolina State University at Raleigh Variable Rate General Revenue Bonds, Series 2008A bonds. The refunding was undertaken to convert the bonds from a publicly traded issue to a private placement issue and convert the variable rate index base from SIFMA to LIBOR.

**Economic Factors That Will Affect the Future**

The State of North Carolina continues to experience moderate, steady economic growth. Employment growth is improving as employment markets continue to stabilize. The state's economic growth is projected to keep pace with that of the nation as a whole. The state's unemployment rate decreased to 4.7% as of July 2016. The main drivers of revenue, employment and personal income, remain stable. Employment gains continue to improve prospects for better income growth over the next few years. The state ended FY 15-16 with over \$450 million of revenue earmarked to the Savings Reserve, bringing the total reserve to almost \$1.6 billion, which is about 7.5% of the prior year General Fund operating budget.

The North Carolina General Assembly passed and the Governor signed a 2016-17 Appropriation Bill that adjusted NC State University's state appropriated funds for 2016-17 as follows. The Appropriation bill included recurring state operating funds of \$1.9 million for anticipated 2016-17 enrollment change, although in future years the University is planning for only very gradual enrollment change that is focused on graduate students. The University received \$6.9 million for repairs and renovations for facilities and infrastructure, \$7 million for a 1.5% continuing salary increase and associated benefits for eligible employees, and \$10 million in additional tuition receipts from increases approved by the UNC Board of Governors in February, 2015 for the second year of the biennium. The University was allocated a \$10.7 million continuing and \$691,000 one-time state appropriated budget reduction for FY 16-17, which was allocated to campus.

The University's projected enrollment growth through 2025 flattens and somewhat stabilizes undergraduate and master's degree enrollment with a focus on growing doctoral enrollment, especially in the STEM (Science, Technology, Engineering, Mathematics) disciplines. The quality of the undergraduate student body continues to increase. Retention and graduation rates continue to improve with graduating student debt at a very modest level among major public research universities. The University continues to be rated as one of the country's best values in higher education.



# FINANCIAL STATEMENTS

**North Carolina State University**  
**Statement of Net Position**  
**June 30, 2016**

**Exhibit A-1**  
**Page 1 of 2**

**ASSETS**

Current Assets:	
Cash and Cash Equivalents	\$ 209,752,180
Restricted Cash and Cash Equivalents	101,792,199
Receivables, Net (Note 5)	72,890,879
Due from Primary Government	6,883,419
Due from State of North Carolina Component Units	2,614,871
Inventories	5,927,680
Notes Receivable, Net (Note 5)	3,144,329
	<hr/>
Total Current Assets	403,005,557
	<hr/>
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	176,042,224
Endowment Investments	209,047,256
Restricted Investments	198,784,761
Other Investments	114,747,421
Notes Receivable, Net (Note 5)	7,950,554
Capital Assets - Nondepreciable (Note 6)	124,372,655
Capital Assets - Depreciable, Net (Note 6)	1,900,955,636
	<hr/>
Total Noncurrent Assets	2,731,900,507
	<hr/>
Total Assets	3,134,906,064
	<hr/>

**DEFERRED OUTFLOWS OF RESOURCES**

Accumulated Decrease in Fair Value of Hedging Derivatives	13,837,267
Deferred Outflows Related to Pensions	31,284,957
	<hr/>
Total Deferred Outflows of Resources	45,122,224
	<hr/>

**LIABILITIES**

Current Liabilities:	
Accounts Payable and Accrued Liabilities (Note 7)	45,594,682
Due to Primary Government	7,671,671
Due to State of North Carolina Component Units	514,053
Unearned Revenue	42,255,442
Interest Payable	4,347,678
Short-Term Debt (Note 8)	40,100,000
Long-Term Liabilities - Current Portion (Note 9)	20,551,578
	<hr/>
Total Current Liabilities	161,035,104
	<hr/>
Noncurrent Liabilities:	
Deposits Payable	2,834,127
Funds Held for Others	30,873,700
U. S. Government Grants Refundable	5,026,290
Funds Held in Trust for Pool Participants	199,492,467
Unearned Revenue	75,436,487
Hedging Derivative Liability (Note 10)	13,837,267
Long-Term Liabilities, Net (Note 9)	682,735,164
	<hr/>
Total Noncurrent Liabilities	1,010,235,502
	<hr/>
Total Liabilities	1,171,270,606
	<hr/>

**DEFERRED INFLOWS OF RESOURCES**

Deferred Inflows Related to Pensions	17,506,004
	<hr/>

**North Carolina State University**  
**Statement of Net Position**  
**June 30, 2016**

**Exhibit A-1**  
**Page 2 of 2**

**NET POSITION**

Net Investment in Capital Assets	1,413,824,172
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	11,576,865
Endowed Professorships	91,436,822
Departmental Uses	7,951,186
Loans	8,298,666
Expendable:	
Scholarships and Fellowships	28,774,194
Research	14,618,087
Endowed Professorships	65,708,515
Departmental Uses	33,183,853
Loans	1,110,201
Capital Projects	59,319,171
Debt Service	15,017,301
Unrestricted	<u>240,432,645</u>
Total Net Position	<u><u>\$ 1,991,251,678</u></u>

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

**North Carolina State University**  
**Statement of Revenues, Expenses, and**  
**Changes in Net Position**  
**For the Fiscal Year Ended June 30, 2016**

**Exhibit A-2**

**REVENUES**

Operating Revenues:

Student Tuition and Fees, Net (Note 12)	\$ 291,175,319
Federal Appropriations	13,847,694
Federal Grants and Contracts	158,076,378
State and Local Grants and Contracts	36,305,745
Nongovernmental Grants and Contracts	83,947,935
Sales and Services, Net (Note 12)	238,447,749
Interest Earnings on Loans	259,520
Other Operating Revenues, Net (Note 12)	14,292,123
	<hr/>
Total Operating Revenues	836,352,463

**EXPENSES**

Operating Expenses:

Salaries and Benefits	857,250,567
Supplies and Materials	127,911,047
Services	251,765,902
Scholarships and Fellowships	43,820,372
Utilities	32,028,497
Depreciation/ Amortization	88,721,461
	<hr/>
Total Operating Expenses	1,401,497,846
	<hr/>
Operating Loss	(565,145,383)

**NONOPERATING REVENUES (EXPENSES)**

State Appropriations	502,533,982
Noncapital Grants - Student Financial Aid	44,705,577
Noncapital Grants	793,723
Noncapital Gifts	71,230,776
Investment Income (Net of Investment Expense of \$1,041,058)	1,569,316
Interest and Fees on Debt	(16,742,517)
Federal Interest Subsidy on Debt	1,136,485
Other Nonoperating Revenues	750,168
	<hr/>
Net Nonoperating Revenues	605,977,510
	<hr/>
Income Before Other Revenues	40,832,127
Capital Appropriations	9,013,500
Capital Grants	2,508,299
Capital Gifts	6,961,858
Additions to Endowments	14,039,031
	<hr/>
Increase in Net Position	73,354,815

**NET POSITION**

Net Position - July 1, 2015	<hr/> 1,917,896,863
Net Position - June 30, 2016	<hr/> <hr/> \$ 1,991,251,678

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



**North Carolina State University**  
**Statement of Cash Flows**  
**For the Fiscal Year Ended June 30, 2016**

**Exhibit A-3**  
**Page 1 of 2**

**CASH FLOWS FROM OPERATING ACTIVITIES**

Received from Customers	\$ 826,173,442
Payments to Employees and Fringe Benefits	(876,612,264)
Payments to Vendors and Suppliers	(408,956,030)
Payments for Scholarships and Fellowships	(43,820,372)
Loans Issued	(874,571)
Collection of Loans	2,076,555
Interest Earned on Loans	258,211
Other Receipts	14,313,885
	<hr/>
Net Cash Used by Operating Activities	(487,441,144)

**CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES**

State Appropriations	502,533,982
Noncapital Grants - Student Financial Aid	44,705,577
Noncapital Grants	214,926
Noncapital Gifts	71,230,776
Additions to Endowments	14,039,031
Proceeds from Hofmann Forest Timber Deed	76,976,007
William D. Ford Direct Lending Receipts	110,989,300
William D. Ford Direct Lending Disbursements	(112,575,224)
Related Activity Agency Receipts	56,207,299
Related Activity Agency Disbursements	(46,750,262)
External Participation in Investment Fund Receipts	25,902,256
External Participation in Investment Fund Disbursements	(12,910,099)
Other Receipts	2,812,560
	<hr/>
Net Cash Provided by Noncapital Financing Activities	733,376,129

**CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES**

Proceeds from Capital Debt	64,455,000
Capital Appropriations	9,013,500
Capital Grants	2,708,911
Capital Gifts	3,780,267
Proceeds from Sale of Capital Assets	381,741
Acquisition and Construction of Capital Assets	(106,793,582)
Principal Paid on Capital Debt and Leases	(52,424,667)
Interest and Fees Paid on Capital Debt and Leases	(16,765,396)
Federal Interest Subsidy on Debt Received	1,136,485
Other Payments	(435,209)
	<hr/>
Net Cash Used by Capital Financing and Related Financing Activities	(94,942,950)

**CASH FLOWS FROM INVESTING ACTIVITIES**

Proceeds from Sales and Maturities of Investments	58,594,886
Investment Income	3,217,548
Purchase of Investments and Related Fees	(41,055,157)
	<hr/>
Net Cash Provided by Investing Activities	20,757,277
	<hr/>
Net Increase in Cash and Cash Equivalents	171,749,312
Cash and Cash Equivalents - July 1, 2015	315,837,291
	<hr/>
Cash and Cash Equivalents - June 30, 2016	\$ 487,586,603

**North Carolina State University**  
**Statement of Cash Flows**  
**For the Fiscal Year Ended June 30, 2016**

**Exhibit A-3**  
**Page 2 of 2**

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

Operating Loss	\$ (565,145,383)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:	
Depreciation/ Amortization Expense	88,721,461
Allowances and Write-Offs	(74,969)
Pension Expense	8,589,794
Changes in Assets, Liabilities, and Deferred Outflows of Resources:	
Receivables, Net	(6,154,998)
Due from Primary Government	5,240,017
Inventories	803,458
Notes Receivable, Net	1,242,744
Accounts Payable and Accrued Liabilities	3,291,899
Due to Primary Government	102,068
Due to State of North Carolina Component Units	(236,411)
Unearned Revenue	4,068,204
Deferred Outflows for Contributions Subsequent to the Measurement Date	(28,562,190)
Compensated Absences	(702,947)
Deposits Payable	1,376,109
	<hr/>
Net Cash Used by Operating Activities	<u>\$ (487,441,144)</u>

**RECONCILIATION OF CASH AND CASH EQUIVALENTS**

Current Assets:	
Cash and Cash Equivalents	\$ 209,752,180
Restricted Cash and Cash Equivalents	101,792,199
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	<hr/> 176,042,224
Total Cash and Cash Equivalents - June 30, 2016	<u>\$ 487,586,603</u>

**NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES**

Assets Acquired through the Assumption of a Liability	\$ 350,919
Assets Acquired through a Gift	3,181,591
Change in Fair Value of Investments	(3,415,953)
Loss on Disposal of Capital Assets	(742,156)
Amortization of Bond Premiums/Discounts	(1,322,866)

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

**North Carolina State University Foundations**  
**Statement of Financial Position**  
**June 30, 2016**

**Exhibit B-1**

	North Carolina State University Foundation, Inc.	NC State Student Aid Association, Inc.	The North Carolina Agricultural Foundation, Inc.
<b>ASSETS</b>			
Cash and Cash Equivalents	\$ 19,964,337	\$ 7,649,157	\$ 17,611,893
Current Investments		8,046,884	
Intermediate Investments	6,201,887		18,258,283
Long-Term Investments	230,492,053	24,242,162	76,817,480
Closely Held Stock			4,890
Cash Surrender Value of Life Insurance		114,620	
Assets Held in Charitable Trusts and Annuities	21,871,415	1,271,453	
Donated Property and Land	1,096,350		32,605,980
Land and Property Held for Others	1,000,000		
Receivables, Net	500,371	236,791	4,445,783
Pledges Receivable/Promises	63,937,451	22,992,908	7,122,930
Land Held for Investment		7,353,929	
Prepaid Expenses		37,505	
Notes/Loans Receivable, Net			2,046,739
Cash Restricted for Long-Term Purposes		6,618,203	
Property and Equipment, Net	6,710,523	29,913,142	82,848
Other Assets	245,988		74,145
Total Assets	<u>\$ 352,020,375</u>	<u>\$ 108,476,754</u>	<u>\$ 159,070,971</u>
<b>LIABILITIES</b>			
Accounts Payable and Accrued Expenses	\$ 523,895	\$ 1,619,429	\$ 350,972
Due to Others	1,805,046	1,586,416	169,245
Life Income Funds Payable	13,853,734		4,052,534
Deferred Revenue		2,334,099	212,980
Contingent Liability			219,738
Funds Held for Others	929,710		
Long-Term Debt		22,089,250	
Total Liabilities	<u>17,112,385</u>	<u>27,629,194</u>	<u>5,005,469</u>
<b>NET ASSETS</b>			
Unrestricted	12,347,845	25,926,288	3,084,710
Temporarily Restricted	97,642,601	18,877,286	70,785,602
Permanently Restricted	224,917,544	36,043,986	80,195,190
Total Net Assets	<u>334,907,990</u>	<u>80,847,560</u>	<u>154,065,502</u>
Total Liabilities and Net Assets	<u>\$ 352,020,375</u>	<u>\$ 108,476,754</u>	<u>\$ 159,070,971</u>

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

**North Carolina State University Foundations**  
**Statement of Activities**  
**For the Fiscal Year Ended June 30, 2016**

**Exhibit B-2**

	North Carolina State University Foundation, Inc.	NC State Student Aid Association, Inc.	The North Carolina Agricultural Foundation, Inc.
<b>CHANGES IN UNRESTRICTED NET ASSETS</b>			
Revenues and Gains:			
Contributions	\$ 3,414	\$ 11,410,146	\$ 1,700,292
Clubs Income		239,755	
Donated Services and Salaries	1,227,000		1,288,000
Disposal of Other Assets			
Leasehold Improvements	154,788		
Net Investment Income	(896,500)	(1,067,013)	(20,764)
Advertising Income		795,973	
Special Events		219,677	
Interest and Dividends	181,823		221,258
Other Income	2,397,101	100,983	49,001
Net Assets Released from Restrictions: Program or Time Restrictions	16,524,864		12,897,919
Net Assets Released from Restrictions: Facility Improvements		9,307,227	
Total Unrestricted Revenues, Gains, and Other Support	<u>19,592,490</u>	<u>21,006,748</u>	<u>16,135,706</u>
Expenses and Losses:			
Scholarships and Fellowships	5,674,551		3,312,116
University Support	6,724,269	12,161,122	7,051,158
University Facilities Support	475,186	9,258,627	1,051,323
Other Contracted Services	950,532		
Other Current Services	620,137		2,019,434
Administrative	662,191	1,337,520	376,000
Fund Raising	3,236,326	2,478,754	2,193,201
Other	1,970,773		
Total Expenses	<u>20,313,965</u>	<u>25,236,023</u>	<u>16,003,232</u>
Loss on Sale of Asset		4,375	
Total Expenses and Losses	<u>20,313,965</u>	<u>25,240,398</u>	<u>16,003,232</u>
Increase (Decrease) in Unrestricted Net Assets	<u>(721,475)</u>	<u>(4,233,650)</u>	<u>132,474</u>
<b>CHANGES IN TEMPORARILY RESTRICTED NET ASSETS</b>			
Contributions	11,311,915	6,489,935	10,582,392
Grant Revenue			499,081
Change in Pledges Receivables	(3,541,484)		(272,260)
Donated Property			95,000
Disposal of Other Assets	(36,358)	(4,375)	(41,491)
Vaughn Towers		3,257,904	
Net Investment Income	(2,798,915)	12,226	(1,164,883)
Royalties			
Interest and Dividends	153,778		329,425
Other Income	2,737,057		870,241
Net Assets Released from Restrictions: Program or Time Restrictions	(16,524,864)		(12,897,919)
Net Assets Released from Restrictions: Facility Improvements		(9,307,227)	
Increase (Decrease) in Temporarily Restricted Net Assets	<u>(8,698,871)</u>	<u>448,463</u>	<u>(2,000,414)</u>
<b>CHANGES IN PERMANENTLY RESTRICTED NET ASSETS</b>			
Contributions	5,909,850	316,353	4,593,253
Change in Pledges Receivables	(1,214,982)		(2,121,749)
Donated Property			1,342,463
Disposal of Other Assets	(214,616)		(225,575)
Net Investment Income	(1,847,798)		18,503
Change in Value of Split Interest Agreements and Trusts	1,050,412	(23,571)	(120,324)
Interest and Dividends	99,685		96,842
Other Income	193,334		355,864
Increase in Permanently Restricted Net Assets	<u>3,975,885</u>	<u>292,782</u>	<u>3,939,277</u>
Increase (Decrease) in Net Assets	<u>(5,444,461)</u>	<u>(3,492,405)</u>	<u>2,071,337</u>
Net Assets at Beginning of Year	<u>340,352,451</u>	<u>84,339,965</u>	<u>151,994,165</u>
Net Assets at End of Year	<u>\$ 334,907,990</u>	<u>\$ 80,847,560</u>	<u>\$ 154,065,502</u>

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



# NOTES TO THE FINANCIAL STATEMENTS

**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. North Carolina State University (University) is a constituent institution of the multi-campus University of North Carolina 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. See below for further discussion of the University's component units.

**Blended Component Units** - Although legally separate, the NC State Investment Fund, Inc. (Investment Fund) and the NC State University Partnership Corporation (Corporation), component units of the University, are reported as if they were part of the University.

The Investment Fund is governed by a board consisting of six ex officio directors and five elected directors. The Investment Fund's purpose is to support the University by operating an investment fund for charitable, nonprofit foundations, associations, trusts, endowments, and funds that are organized and operated primarily to support the University. The Investment Fund is a governmental external investment pool. Because the elected directors of the Investment Fund are appointed by the members of the North Carolina State University Board of Trustees and the Investment Fund's primary purpose is to benefit North Carolina State University, its financial statements have been blended with those of the University.

The Corporation is governed by a five member Board of Directors appointed based on their positions held with North Carolina State University. Additional members of the board may be appointed by the Chancellor of North Carolina State University. The Corporation's purpose is to support and benefit the University with the aims of creating new knowledge and improving the lives of the people of North Carolina. The Corporation formed NC State University Centennial Development, LLC on January 25, 2002 to construct, own and operate a golf course located on the North Carolina State University Centennial Campus. In addition, the Corporation formed NC State Upfit, LLC on October 27, 2006 to

develop, construct, own, finance, manage and otherwise upfit facilities and other infrastructure on Centennial Campus. Also, the Corporation formed NC State CBC Land I, LLC on June 1, 2007 to acquire, develop, own, lease, hold, manage, sell, and otherwise exercise all right of ownership of land and flex lab facilities on Centennial Biomedical Campus. Additionally, the Corporation formed NC State American Home, LLC on August 8, 2007 and changed its name to Bell Tower Holdings, LLC on December 14, 2009. The purposes of Bell Tower Holdings, LLC are to acquire, develop, own, lease, hold, manage, sell and otherwise exercise all right of ownership of real property and enter into any related agreements for assisting with the acquisition, development, financing, construction, management and operation of real property. On March 31, 2008 the Corporation formed NC State CC Holdings I, LLC to acquire, develop, own, lease, hold, manage, sell and otherwise exercise all right of ownership of land and facilities on Centennial Campus. Leaders in Innovation and Nonwovens Commercialization, LLC (LINC), was established on July 9, 2012 to foster economic development and creation of new knowledge by facilitating commercialization of technologies developed at the Nonwovens Institute at NC State University. Because the Corporation's Board consists of University employees and members appointed by the Chancellor and its sole purpose is to support and benefit the University, the Corporation and the LLCs are considered part of the University for financial reporting purposes.

Separate financial statements for the Investment Fund and for the Corporation and the LLCs may be obtained from the Foundations Accounting and Investments Office, Campus Box 7207, Raleigh, NC 27695, or by calling (919) 513-7149. Other related foundations and similar non-profit corporations for which the University is not financially accountable are not part of the accompanying financial statements.

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

**Discretely Presented Component Units** - The North Carolina State University Foundation, Inc. (Foundation), NC State Student Aid Association, Inc. (Athletic Club) and The North Carolina Agricultural Foundation, Inc. (Agricultural Foundation) are legally separate nonprofit corporations and are reported as discretely presented component units based on the nature and significance of their relationship to the University.

The Foundation, Athletic Club and Agricultural Foundation are legally separate, tax-exempt component units of the University. These entities act primarily as fund-raising organizations to supplement the resources that are available to the University in support of its programs. Separate Boards of Directors govern these entities independent of the University's Board of Trustees. Although the University does not control the timing or amount of receipts from these entities, the majority of resources, or income thereon that these entities hold and invest are restricted to the

activities of the University by the donors. Because these restricted resources held by these entities can only be used by, or for the benefit of the University, these entities are considered component units of the University and are reported in separate financial statements because of the difference in their reporting model, as described below.

The Foundation, Athletic Club and Agricultural Foundation 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 their financial information in the University's financial reporting entity for these differences.

During the year ended June 30, 2016, the Foundation distributed \$15,475,629 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from the Foundations Accounting and Investments Office, Campus Box 7207, Raleigh, NC 27695, or by calling (919) 513-7149.

During the year ended June 30, 2016, the Athletic Club distributed \$15,140,969 to the University for both restricted and unrestricted purposes. Complete financial statements for the Athletic Club can be obtained from the NC State Student Aid Association, PO Box 37100, Raleigh, NC 27627, or by calling (919) 865-1500.

During the year ended June 30, 2016, the Agricultural Foundation distributed \$14,553,966 to the University for both restricted and unrestricted purposes. Complete financial statements for the Agricultural Foundation can be obtained from the Foundations Accounting and Investments Office, Campus Box 7207, Raleigh, NC 27695, or by calling (919) 513-7149.

- 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 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, include 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, money market 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** – To the extent available, investments are recorded at fair value based on quoted market prices in active markets on a trade-date basis. Additional information regarding the fair value measurement of investments is disclosed in Note 3. Because of the inherent uncertainty in the use of estimates, values that are based on estimates may differ from the values that would have been used had a ready market existed for the investments. The net increase (decrease) in the fair value of investments is recognized as a component of investment income.

Endowment investments include the principal amount of gifts and bequests that, according to donor restrictions, must be held in perpetuity or for a specified period of time, 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.

Restricted investments include funds of affiliated entities that are neither part of the University's reporting entity nor reported discretely but invested through the Investment Fund.

**F. Receivables** - Receivables consist of tuition and fees charged to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from the federal government, state and local governments, and private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants. Receivables are recorded net of estimated uncollectible amounts.

**G. Inventories** - Inventories, consisting of expendable supplies and merchandise for resale, are valued at cost using the first-in, first-out

method. Exceptions are the bookstore, which uses the retail inventory method, and physical plant, which uses the moving weighted average method.

- H. **Capital Assets** - Capital assets are stated at cost at date of acquisition or acquisition value at date of donation in the case of gifts. Donated capital assets acquired prior to July 1, 2015 are stated at fair value as of the date of donation. 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 of \$5,000 or greater at the date of acquisition and an estimated useful life of more than one year except for internally generated software which is capitalized when the value or cost is \$1,000,000 or greater and other intangible assets which are capitalized when the value or cost is \$100,000 or greater.

Depreciation and amortization are computed using the straight-line over the estimated useful lives of the assets in the following manner:

<u>Asset Class</u>	<u>Estimated Useful Life</u>
Buildings	10-50 years
Machinery & Equipment	4-22 years
General Infrastructure	15-75 years
Computer Software	2-15 years

The University does not capitalize its Arts and Design or Historic collections. These collections adhere to the University's policy to maintain for public exhibition, education, or research; protect, keep unencumbered, care for, and preserve; and requires proceeds from their sale to be used to acquire other collection items. Accounting principles generally accepted in the United States of America permit collections maintained in this manner to be charged to operations at time of purchase rather than be capitalized.

- 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, 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 pool more fully described in Note 2.

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

Revenue bonds payable are reported net of unamortized premiums or discounts. The University amortizes bond premiums/discounts over the life of the bonds using the straight-line method. Losses on refunding and issuance costs on bonds payable are not material to the accompanying financial statements and are expensed in the year incurred.

The net pension liability represents the University's proportionate share of the collective net pension liability reported in the State of North Carolina's 2015 *Comprehensive Annual Financial Report*. This liability represents the University's portion of the collective total pension liability less the fiduciary net position of the Teachers' and State Employees' Retirement System. See Note 14 for further information regarding the University's policies for recognizing liabilities, expenses, and deferred outflows and inflows related to pensions.

- L. 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. When classifying compensated absences into current and noncurrent, leave is considered taken using a last-in, first-out (LIFO) method. Also, any accumulated vacation leave in excess of 30 days at year-end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

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.

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.

- M. 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 liabilities 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.

**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 include consideration of deferred outflows and inflows of resources.

- N. 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.
- O. 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 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 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.

- P. **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 Central Stores, the Creamery, Telecommunications, Physical Plant, and Motor Pool. 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.

Cash on hand at June 30, 2016 was \$447,912. The carrying amount of the University's deposits not with the State Treasurer was \$38,110,721 and the bank balance was \$57,590,519. 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 follows the Cash Management Plan (Plan)

approved by the North Carolina Office of the State Controller. As provided by the Plan, imprest checking accounts are established with outside banks when considered effective in meeting management objectives. All imprest checking accounts are authorized by the University Treasurer and are limited to the minimum amount needed for sanctioned purposes. In addition, pursuant to G.S. 116-36(e), the University invests certain endowment funds with outside bank accounts. The University does not have a deposit policy for custodial credit risk. As of June 30, 2016, the University's bank balance exposed to custodial credit risk (amounts that are uninsured and uncollateralized) was \$56,160,921.

- 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.

Additionally, the University has also been delegated authority by the President of The University of North Carolina pursuant to G.S. 116-36.1 and Section 600.2.4.1 of the Policy Manual of the University of North Carolina to invest its trust funds in the same manner as the State Treasurer is required to invest, as discussed below.

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

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

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 Endowment Fund, including those invested in the Investment Fund, a University component unit, 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.

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.

**Short-Term Investment Fund** - At June 30, 2016, the amount shown on the Statement of Net Position as cash and cash equivalents includes \$449,027,970 which represents the University’s equity position in the State Treasurer’s Short-Term Investment Fund (STIF). The STIF (a portfolio within the State Treasurer’s Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission or subject to any other regulatory oversight and does not have a credit rating) had a weighted average maturity of 1.5 years as of June 30, 2016. Assets and shares of the STIF are valued at 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.

**Investment Fund** - The Investment Fund began operations in April 1999 and is classified as a non-rated 2a7-like governmental external investment pool that is not registered with the Securities and Exchange Commission (SEC) as an investment company, but has a policy that it will, and does, operate in a manner consistent with the SEC’s Rule 2a7 of the Investment Company Act of 1940. The Endowment Fund of North Carolina State University, The North Carolina Agricultural Foundation, Inc., and the North Carolina State University Foundation, Inc. represent the Investment Fund’s internal participants. The North Carolina Agricultural Foundation, Inc. and the North Carolina State University Foundation, Inc. are discretely presented component units in the accompanying financial statements. Other affiliated organizations not included in the University’s reporting entity represent the Pool’s external participants. The external portion of the Pool is presented in the accompanying financial statements as “Funds Held in Trust for Pool Participants.” The Investment Fund includes the Long-Term Investment

Pool (LTIP) and the newly created Intermediate Term Fund (ITF) which was established on July 3, 2014 for the collective investment of the participants' excess operating funds.

The Investment Fund is not subject to any formal oversight other than that provided by the Investment Fund Members Board or its Board of Directors. The Members Board is responsible for adopting investment objectives and policies and for monitoring policy implementation and investment performance. The Members Board has chosen not to make individual security selection decisions. The Board of Directors has the responsibility to oversee the allocation of the Investment Fund's portfolio among the asset classes, investment vehicles, and investment managers. Authority to manage the ITF in accordance with the investment policy has been granted jointly to the University's Vice Chancellor and Associate Vice Chancellor for Finance and Administration.

Bank of New York Mellon is the custodian for the Investment Fund and provides the University with quarterly statements defining income and fair value information, which is then allocated among the fund's participants. Each participant holds Master Trust Units of the Investment Fund. The unit price fluctuates based on the investment experience of the investment pool. There are no involuntary participants in the Investment Fund. The University has not provided or obtained any legally binding guarantees during the period to support the value for the Investment Fund's investments. The annual financial report for the Investment Fund may be obtained from the Foundations Accounting and Investment Office, Campus Box 7207, Raleigh, NC 27695 or by calling (919) 513-7149 or at <http://foundationsaccounting.ofa.ncsu.edu/investment-fund>.

The following table presents investments by type and investments subject to interest rate risk at June 30, 2016, for the Investment Fund.

Investment Type	Amount	Investment Maturities (in Years)	
		Less Than 1	1 to 5
Debt Securities			
Collective Investment Funds	\$ 34,817,974	\$ 34,817,974	\$ 0
Debt Mutual Funds	137,760,322		137,760,322
<b>Total Debt Securities</b>	172,578,296	<b>\$ 34,817,974</b>	<b>\$ 137,760,322</b>
Other Securities			
UNC Investment Fund	623,702,676		
Private Equity Limited Partnerships	23,912,641		
<b>Total Investment Fund</b>	<b>\$ 820,193,613</b>		



At June 30, 2016, investments in the Investment Fund had the following credit quality distribution for securities with credit exposure (based on S&P ratings):

	Amount	AAA Aaa	A	BB/Ba and below	Unrated
Collective Investment Funds	\$ 34,817,974	\$ 4,340,803	\$ 4,564,123	\$ 699,498	\$ 25,213,550
Debt Mutual Funds	<u>137,760,322</u>		<u>102,889,694</u>		<u>34,870,628</u>
Totals	<u>\$ 172,578,296</u>	<u>\$ 4,340,803</u>	<u>\$ 107,453,817</u>	<u>\$ 699,498</u>	<u>\$ 60,084,178</u>

**UNC Investment Fund, LLC** - At June 30, 2016, the University's investments include \$623,702,676 which represents the University's equity position in the UNC Investment Fund, LLC (UNC Investment Fund). The UNC Investment Fund is an external investment pool that is not registered with the Securities and Exchange Commission, does not have a credit rating, and is not subject to any regulatory oversight. Investment risks associated with the UNC Investment Fund are included in audited financial statements of the UNC Investment Fund, LLC which may be obtained from UNC Management Company, Inc., 1400 Environ Way, Chapel Hill, NC 27517.

**Non-Pooled Investments** - The following table presents investments by type and investments subject to interest rate risk at June 30, 2016, for the University's non-pooled investments.

***Non-Pooled Investments***

Investment Type	Amount	Investment Maturities (In Years) Less Than 1
Debt Securities		
Money Market Mutual Funds	\$ 569,782	<u>\$ 569,782</u>
Other Securities		
Domestic Stocks	25,587	
Collection and Mineral Rights	<u>65,134</u>	
Total Non-Pooled Investments	<u>\$ 660,503</u>	

At June 30, 2016, the University's non-pooled investments had the following credit quality distribution for securities with credit exposure (based on Moody's and S&P ratings):

	Amount	AAA Aaa
Money Market Mutual Funds	<u>\$ 569,782</u>	<u>\$ 569,782</u>

**Total Investments** - The following table presents the total investments at June 30, 2016:

Investment Type	Amount
Debt Securities	
Collective Investment Funds	\$ 34,817,974
Debt Mutual Funds	137,760,322
Money Market Mutual Funds	569,782
Other Securities	
UNC Investment Fund	623,702,676
Private Equity Limited Partnerships	23,912,641
Domestic Stocks	25,587
Collections and Mineral Rights	65,134
<b>Total Investments</b>	<b>\$ 820,854,116</b>

Total investments include \$298,274,678 held in the UNC Investment Fund for the North Carolina State University Foundation, Inc. and the North Carolina Agricultural Foundation, Inc. This amount is excluded from the University prepared financial statements and included in the accompanying component unit financial statements.

**NOTE 3 - FAIR VALUE MEASUREMENTS**

To the extent available, the University's investments and derivatives are recorded at fair value as of June 30, 2016. GASB Statement No. 72 - *Fair Value Measurement and Application*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This statement establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Inputs are used in applying the various valuation techniques and take into account the assumptions that market participants use to make valuation decisions. Inputs may include price information, credit data, interest and yield curve data, and other factors specific to the financial instrument. Observable inputs reflect market data obtained from independent sources. In contrast, unobservable inputs reflect the entity's assumptions about how market participants would value the financial instrument. Valuation techniques should maximize the use of observable inputs to the extent available.

A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. The following describes the hierarchy of inputs used to measure fair value and the primary valuation methodologies used for financial instruments measured at fair value on a recurring basis:

- Level 1 Investments whose values are based on quoted prices (unadjusted) for identical assets or liabilities in active markets that a government can access at the measurement date.

Level 2 Investments with inputs – other than quoted prices included within Level 1 – that are observable for an asset or liability, either directly or indirectly.

Level 3 Investments classified as Level 3 have unobservable inputs for an asset or liability and may require a degree of professional judgment.

The following table summarizes the University’s investments within the fair value hierarchy at June 30, 2016:

	Fair Value	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
<b>Investments by Fair Value Level</b>				
<b>Debt Securities</b>				
Collective Investment Funds	\$ 34,817,974	\$ 34,817,974	\$ 0	\$ 0
Debt Mutual Funds	137,760,322	137,760,322		
Money Market Mutual Funds	569,782	569,782		
<b>Total Debt Securities</b>	<b>173,148,078</b>	<b>173,148,078</b>		
<b>Other Securities</b>				
Short-Term Investment Fund	449,027,970		449,027,970	
UNC Investment Fund	623,702,676			623,702,676
Domestic Stocks	25,587			25,587
<b>Total Investments by Fair Value Level</b>	<b>1,245,904,311</b>	<b>\$ 173,148,078</b>	<b>\$ 449,027,970</b>	<b>\$ 623,728,263</b>
<b>Investments Measured at the Net Asset Value (NAV)</b>				
Private Equity Limited Partnerships	23,912,641			
Collection and Mineral Rights	65,134			
<b>Total Investments Measured at the NAV</b>	<b>23,977,775</b>			
<b>Total Investments Measured at Fair Value</b>	<b>\$ 1,269,882,086</b>			
<b>Derivative Instruments</b>				
<b>Hedging Derivative Instruments</b>				
Interest Rate Swaps	\$ 13,837,267	\$ 0	\$ 13,837,267	\$ 0

**Short-Term Investment Fund** - Ownership interest of the STIF is determined on a fair market valuation basis as of fiscal year end in accordance with the STIF operating procedures. Valuation of the underlying assets is performed by the custodian.

**UNC Investment Fund** - Ownership interests of the UNC Investment Fund are determined on a market unit valuation basis each month and in accordance with the UNC Investment Fund’s operating procedures.

**Debt and Equity Securities** – Debt and equity securities classified as Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities.

**Domestic Stock** - Domestic stock classified as Level 3 of the fair value hierarchy are valued at book value. There is no readily determinable fair value.

**Derivative Instruments** - Derivative instruments classified as Level 2 of the fair value hierarchy are valued at present value using discounted cash flows.

The valuation of investments measured at the Net Asset Value (NAV) per share (or its equivalent) is presented on the following table.

Investments Measured at the NAV

	Fair Value	Unfunded Commitments	Redemption Frequency (If Currently Eligible)	Redemption Notice Period
Private Equity Limited Partnerships	\$ 23,912,641	\$ n/a	n/a	n/a
Collections and Mineral Rights	<u>65,134</u>	n/a	n/a	n/a
Total Investments Measured at the NAV	<u>\$ 23,977,775</u>			

**A. Private Equity Limited Partnerships** - Private equities include venture capital partnerships, buy-outs, and international funds. The valuation of the underlying private companies requires significant judgment and interpretation by the general partners of the underlying investment partnerships due to the absence of quoted market values, inherent lack of liquidity and the long-term nature of such investments. Private companies are initially valued based upon transaction price, with subsequent adjustments to values which reflect the consideration of available market data, including primarily observations of the trading multiples of public companies considered comparable to the private companies being valued. Valuations are also adjusted to give consideration to the financial condition and operating results specific to the issuer, the lack of liquidity inherent in a non-public investment, credit markets, and the fact that comparable public companies are not identical to the companies being valued.

**B. Art Collection:** The Kamphoefner art collection, with an estimated value of \$27,300, was gifted to the Endowment Fund in 1979. This collection is to be held for the use of the D. H. Hill Library at NC State University.

**Mineral Rights:** Virginia Rock and Mineral rights were gifted to the Endowment Fund in 1987. This was a gift for the use of the NC State Geology Department. There have been three sales of these mineral rights since the original receipt of the gift. The most recent sale from July 2016 was used to adjust the value per acre.

**NOTE 4 - ENDOWMENT INVESTMENTS**

Investments of the University’s endowment funds are pooled, unless required to be separately invested by the donor. If a donor has not provided specific instructions, state law permits the Board of Trustees to authorize for expenditure the net appreciation, realized and unrealized, of the investments of the endowment funds. Under the “Uniform Prudent Management of Institutional Funds Act” (UPMIFA), authorized by the North Carolina General Assembly on March 19, 2009, the Board may also 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, or applicable State of NC law. However, a majority of the University's endowment donor agreements prohibit spending of nonexpendable balances and therefore the related nonexpendable balances are not eligible for expenditure. During the year, the Board did not appropriate expenditures from eligible nonexpendable endowment funds.

Investment return of the University's endowment funds is predicated on the total return concept (yield plus appreciation). Annual payouts from the University pooled endowment funds are determined by applying 4% (the Board approved spending rate) to the average market value of the long term investment pool (for a 20 quarter period), divided by the number of investment units in the pool to determine the "average spending amount" per unit of investment. The individual endowment fund payout or spending budget is then determined by applying the "average spending amount" to the number of investment units held by the individual endowment fund. To the extent that the total return for the current year exceeds the payout, the excess is added to principal. If current year earnings do not meet the payout requirements, the University uses accumulated income and appreciation from restricted and unrestricted, expendable net position endowment balances to make up the difference. At June 30, 2016, net appreciation of \$119,322,265 was available to be spent, of which \$111,655,019 was restricted to specific purposes. The remaining portion of net appreciation available to be spent is classified as unrestricted net position.

**NOTE 5 - RECEIVABLES**

Receivables at June 30, 2016 were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
<b>Current Receivables:</b>			
Students	\$ 1,291,997	\$ 1,234,081	\$ 57,916
Student Sponsors	2,633,779		2,633,779
Accounts	31,822,462	1,765,040	30,057,422
Intergovernmental	39,787,552		39,787,552
Interest on Loans	465,440	416,901	48,539
Federal Interest Subsidy on Debt	305,671		305,671
	<u>\$ 76,306,901</u>	<u>\$ 3,416,022</u>	<u>\$ 72,890,879</u>
<b>Total Current Receivables</b>			
<b>Notes Receivable:</b>			
<b>Notes Receivable - Current:</b>			
Federal Loan Programs	\$ 2,831,415	\$ 10,476	\$ 2,820,939
Institutional Student Loan Programs	325,635	2,245	323,390
	<u>\$ 3,157,050</u>	<u>\$ 12,721</u>	<u>\$ 3,144,329</u>
<b>Total Notes Receivable - Current</b>			
<b>Notes Receivable - Noncurrent:</b>			
Federal Loan Programs	\$ 8,376,561	\$ 672,990	\$ 7,703,571
Institutional Student Loan Programs	384,189	137,206	246,983
	<u>\$ 8,760,750</u>	<u>\$ 810,196</u>	<u>\$ 7,950,554</u>
<b>Total Notes Receivable - Noncurrent</b>			

**NOTE 6 - CAPITAL ASSETS**

A summary of changes in the capital assets for the year ended June 30, 2016 is presented as follows:

	Balance July 1, 2015 (As restated)	Increases	Decreases	Balance June 30, 2016
Capital Assets, Nondepreciable:				
Land	\$ 59,544,940	\$ 2,912,554	\$ 0	\$ 62,457,494
Construction in Progress	54,956,500	46,149,722	39,514,661	61,591,561
Computer Software in Development	<u>659,874</u>	<u>2,693,613</u>	<u>3,029,887</u>	<u>323,600</u>
<b>Total Capital Assets, Nondepreciable</b>	<u>115,161,314</u>	<u>51,755,889</u>	<u>42,544,548</u>	<u>124,372,655</u>
Capital Assets, Depreciable:				
Buildings	2,161,039,192	74,192,113	6,842,990	2,228,388,315
Machinery and Equipment	342,643,333	27,241,779	10,449,758	359,435,354
General Infrastructure	205,771,161	1,993,428		207,764,589
Computer Software	<u>17,514,419</u>	<u>3,029,887</u>		<u>20,544,306</u>
<b>Total Capital Assets, Depreciable</b>	<u>2,726,968,105</u>	<u>106,457,207</u>	<u>17,292,748</u>	<u>2,816,132,564</u>
Less Accumulated Depreciation/Amortization for:				
Buildings	572,653,899	60,268,623	6,696,723	626,225,799
Machinery and Equipment	203,903,022	19,944,948	9,472,128	214,375,842
General Infrastructure	58,456,045	5,093,750		63,549,795
Computer Software	<u>7,611,352</u>	<u>3,414,140</u>		<u>11,025,492</u>
<b>Total Accumulated Depreciation/Amortization</b>	<u>842,624,318</u>	<u>88,721,461</u>	<u>16,168,851</u>	<u>915,176,928</u>
<b>Total Capital Assets, Depreciable, Net</b>	<u>1,884,343,787</u>	<u>17,735,746</u>	<u>1,123,897</u>	<u>1,900,955,636</u>
<b>Capital Assets, Net</b>	<u>\$ 1,999,505,101</u>	<u>\$ 69,491,635</u>	<u>\$ 43,668,445</u>	<u>\$ 2,025,328,291</u>

During the year ended June 30, 2016, the University incurred \$21,835,312 in interest costs related to the acquisition and construction of capital assets. Of this total, \$17,354,384 was charged in interest expense, and \$4,480,928 was capitalized.

Due to the implementation of GASB 72, \$21,878,102 of assets previously classified as investments in real estate are now shown as land and buildings.

**NOTE 7 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**

Accounts payable and accrued liabilities at June 30, 2016 were as follows:

	Amount
<b>Current Accounts Payable and Accrued Liabilities</b>	
Accounts Payable	\$ 19,386,637
Accounts Payable - Capital	12,388,491
Accrued Payroll	9,399,284
Contract Retainage	2,401,344
Other	<u>2,018,926</u>
<b>Total Current Accounts Payable and Accrued Liabilities</b>	<u>\$ 45,594,682</u>

**NOTE 8 - SHORT-TERM DEBT – COMMERCIAL PAPER PROGRAM AND LINE OF CREDIT**

The University has available Commercial Paper Program financing for short-term debt credit up to \$100,000,000 to finance capital construction projects. The University's available funds are pledged to the Commercial Paper Program financing with the anticipation of converting to general revenue bond financing in the future. As of June 30, 2016, \$40,000,000 in Tax-Exempt Commercial Paper was outstanding.

The NC State University Partnership Corporation, through the NC State University Centennial Development LLC has available a Line of Credit, from SunTrust Bank, up to \$250,000 for operations at the Lonnie Poole Golf Course. The line is unsecured and must maintain a zero balance for at least 30 consecutive days during each twelve months. As of June 30, 2016, \$100,000 was outstanding.

Short-term debt activity for the year ended June 30, 2016 was as follows:

	Balance July 1, 2015	Draws	Repayments	Balance June 30, 2016
Commercial Paper Program	\$ 10,000,000	\$ 240,000,000	\$ 210,000,000	\$ 40,000,000
Partnership Corporation - Line of Credit		100,000		100,000
	<u>\$ 10,000,000</u>	<u>\$ 240,100,000</u>	<u>\$ 210,000,000</u>	<u>\$ 40,100,000</u>

**NOTE 9 - LONG-TERM LIABILITIES**

**A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities for the year ended June 30, 2016 is presented as follows:**

	Balance July 1, 2015	Additions	Reductions	Balance June 30, 2016	Current Portion
Revenue Bonds Payable	\$ 475,555,000	\$ 64,455,000	\$ 77,920,000	\$ 462,090,000	\$ 13,985,000
Plus: Unamortized Premium	23,488,276		1,322,865	22,165,411	
Total Revenue Bonds Payable, Net	<u>499,043,276</u>	<u>64,455,000</u>	<u>79,242,865</u>	<u>484,255,411</u>	<u>13,985,000</u>
Net Pension Liability	25,160,037	53,681,089		78,841,126	
Notes Payable	76,194,309		4,376,612	71,817,697	3,034,536
Capital Leases Payable	210,875	350,919	20,617	541,177	154,589
Compensated Absences	68,534,279	39,826,483	40,529,431	67,831,331	3,377,453
Total Long-Term Liabilities	<u>\$ 669,142,776</u>	<u>\$ 158,313,491</u>	<u>\$ 124,169,525</u>	<u>\$ 703,286,742</u>	<u>\$ 20,551,578</u>

Additional information regarding capital lease obligations is included in Note 11.  
Additional information regarding the net pension liability is included in Note 14.

**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, 2016	Principal Outstanding June 30, 2016
<u>GENERAL REVENUE</u>						
Housing System Projects/Doak Field Projects	2003B	3.54% swap*	10/01/2027	\$ 45,660,000	\$ 3,240,000	\$ 42,420,000
Various Construction Projects	2005A	5%	10/01/2015	81,615,000	81,615,000	
Various Construction Projects	2008A	3.86% swap*	10/01/2028	66,605,000	66,605,000	
Various Construction Projects	2008B	4% - 4.25%	10/01/2020	26,955,000	25,485,000	1,470,000
Various Construction Projects	2010A	4% - 5%	10/01/2022	18,065,000	6,685,000	11,380,000
Various Construction Projects	2010B	5.079% - 6.027%**	10/01/2035	59,565,000		59,565,000
Advance Refund Series 2003A	2012	4% - 5%	10/01/2018	16,265,000	6,100,000	10,165,000
Adv Refund 2005A / Wolf Ridge Housing	2013A	2% - 5%	10/01/2042	132,440,000		132,440,000
Adv Refund 2005A / Talley Student Union	2013B	0.849% - 4%	10/01/2041	141,650,000	1,455,000	140,195,000
Refund 2008A	2015	3.86% swap*	10/01/2028	64,455,000		64,455,000
<b>Total Revenue Bonds Payable (principal only)</b>				<u>\$ 653,275,000</u>	<u>\$ 191,185,000</u>	462,090,000
Plus: Unamortized Premium						22,165,411
<b>Total Revenue Bonds Payable, Net</b>						<u>\$ 484,255,411</u>

\* For variable rate debt, interest rates in effect at June 30, 2016 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.

**C. Demand Bonds** - Included in bonds payable is a variable rate demand bond issue. 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 regard to the following demand bond, the University has entered into take out agreements, which would convert the demand bonds not successfully remarketed into another form of long-term debt.

**North Carolina State University at Raleigh Variable Rate General Revenue Bonds, Series 2003B**

On June 20, 2003 the University issued tax-exempt variable rate revenue demand bonds in the amount of \$45,660,000 that have a final maturity date of October 1, 2027. The bonds are subject to mandatory sinking fund redemption that began on October 1, 2004. The University's proceeds of this issuance were used to pay a portion of the costs of certain improvements on the campus of the University, to refund certain debt previously incurred for that purpose, and to pay the costs incurred in connection with the issuance of the 2003B bonds.

While bearing interest at a weekly rate, the bonds are subject to purchase on demand with seven days notice and delivery to the paying agent, U.S. Bank National Association. Effective October 15, 2015, U.S. Bank National Association has been appointed as the successor trustee for all of the outstanding series of General Revenue Bonds issued on



behalf of North Carolina State University at Raleigh. Upon notice from the paying agent, the Remarketing Agent, Wells Fargo Bank, N.A., has agreed to exercise its best efforts to remarket the bonds for which a notice of purchase has been received.

Under a Standby Bond Purchase Agreement (Agreement) between the Board of Governors of the University of North Carolina and Wells Fargo Bank, N.A., a Liquidity Facility has been established for the Trustee (U.S. Bank National Association) to draw amounts sufficient to pay the purchase price and accrued interest on bonds delivered for purchase when remarketing proceeds or other funds are not available. Effective November 18, 2015, Wells Fargo Bank, N.A. issued a substitute liquidity facility and the prior liquidity facility issued by Bayerische Landesbank was simultaneously terminated. This Agreement requires a commitment fee equal to 0.36% of the available commitment, payable quarterly in arrears, beginning on February 1, 2016 and on each May 1, August 1, and November 1 thereafter until the expiration date or the termination date of the Agreement.

Under the Agreement, any bonds purchased through the Liquidity Facility become Liquidity Provider Bonds and shall, from the date of such purchase and while they are Liquidity Provider Bonds, bear interest at the Base rate (the greater of the bank prime commercial lending rate plus 1.00%, the federal funds rate plus 2.00%, and 7.00%). Upon remarketing of Liquidity Provider Bonds and the receipt of the sales price by the Liquidity Provider, such bonds are no longer considered Liquidity Provider Bonds. Payment of the interest on the Liquidity Provider Bonds is due the first business day of each quarter in which Liquidity Provider Bonds are outstanding. At June 30, 2016, there were no Liquidity Provider Bonds held by the Liquidity Facility. The Liquidity Facility is scheduled to expire on November 18, 2020, unless otherwise extended based on the terms of the Agreement.

Upon expiration or termination of the Agreement, the University is required to redeem (purchase) the Liquidity Provider Bonds held by the Liquidity Facility in 6 semi-annual installments, beginning 181 days from the date of the last draw at the Term Loan Rate (Base Rate + 1.00%). In the event the outstanding \$42,420,000 of demand bonds was "put" and not resold, the University would be required to pay \$16.2 million a year for three years under this agreement assuming an 8.00% interest rate.

**D. Annual Requirements** - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2016, are as follows:

Fiscal Year	Annual Requirements				
	Revenue Bonds Payable			Notes Payable	
	Principal	Interest	Interest Rate Swaps, Net	Principal	Interest
2017	\$ 13,985,000	\$ 16,271,713	\$ 2,332,081	\$ 3,034,536	\$ 2,726,449
2018	14,510,000	15,865,763	2,201,596	3,558,787	2,602,284
2019	14,140,000	15,454,088	2,065,932	4,012,877	2,458,647
2020	14,685,000	15,135,710	1,924,745	4,505,104	2,296,412
2021	15,245,000	14,861,176	1,778,035	4,987,707	2,114,936
2022 - 2026	86,105,000	69,267,358	5,595,179	33,126,932	7,125,177
2027 - 2031	110,415,000	55,732,813	256,380	18,591,754	826,431
2032 - 2036	68,525,000	34,379,066			
2037 - 2041	85,205,000	17,712,900			
2042 - 2046	39,275,000	1,889,900			
<b>Total Requirements</b>	<b>\$ 462,090,000</b>	<b>\$ 256,570,487</b>	<b>\$ 16,153,948</b>	<b>\$ 71,817,697</b>	<b>\$ 20,150,336</b>

Interest on the variable rate 2003B general revenue bonds is calculated at 0.40% at June 30, 2016. Interest rate is reset each week by the remarketing agent based upon University credit ratings and market conditions. Interest on the variable rate 2015 general revenue bonds is calculated at 0.8037% at June 30, 2016. Interest rate is reset each month based upon 1 month LIBOR.

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 10 Derivative Instruments.

**E. Bond Defeasance** - The University has extinguished long-term debt obligations by the issuance of new long-term debt instruments as follows:

On November 18, 2015 the University issued \$64,455,000 in North Carolina State University at Raleigh Variable Rate General Revenue Refunding Bonds, Series 2015. The bonds were issued for a current refunding of \$64,455,000 of North Carolina State University at Raleigh Variable Rate General revenue Bonds, Series 2008A. The refunding was undertaken to convert the bonds to a private placement with BB&T Community Holdings Co., eliminate the need for a standby credit facility and to change the index basis from SIFMA to 1 month LIBOR. There is no economic gain or loss on this transaction.

**Prior Year Defeasances** - During prior years, the University defeased certain bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the University's financial statements. Prior year defeased bonds were called on October 1, 2015. At June 30, 2016, the outstanding balance of prior year defeased bonds was \$0.

**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, 2016	Compounded Interest	Principal Outstanding June 30, 2016
Energy Conservation Loan	BB&T	3.25%	09/01/2028	\$ 19,700,703	\$ 2,542,262	\$ 707,470	\$ 17,865,911
Energy Conservation Loan	Bank of America	4.07%	08/17/2028	56,060,010	5,631,162	3,522,938	53,951,786
Carol Johnson Poole Clubhouse	Suntrust	Variable	07/30/2016	3,049,447	3,049,447		
<b>Total Notes Payable</b>				<u>\$ 78,810,160</u>	<u>\$ 11,222,871</u>	<u>\$ 4,230,408</u>	<u>\$ 71,817,697</u>

**NOTE 10 - DERIVATIVE INSTRUMENTS**

Derivative instruments held at June 30, 2016 are as follows:

Type	Notional Amount	Change in Fair Value		Fair Value at June 30, 2016	
		Classification	Decrease	Classification	Liability
<i>Hedging Derivative Instruments</i>					
<i>Cash Flow Hedges</i>					
Pay-Fixed Interest Rate Swap 2003B Bonds	\$ 24,655,000	Deferred Outflow of Resources	\$ 1,403,594	Hedging Derivative Liability	\$ 5,629,388
Pay-Fixed Interest Rate Swap 2015 Bonds	\$ 48,400,000	Deferred Outflow of Resources	<u>\$ 625,284</u>	Hedging Derivative Liability	<u>\$ 8,207,879</u>
<b>Total Derivative Instruments</b>			<u>\$ 2,028,878</u>		<u>\$ 13,837,267</u>

Hedging derivative instruments held at June 30, 2016 are as follows:

Type	Objective	Notional Amount	Effective Date	Maturity Date	Terms
Pay-Fixed Interest Rate Swap	Hedge changes in cash flows on General Revenue 2003B Series Bonds	\$ 24,655,000	06/20/03	10/01/27	Pay 3.54% Receive 75% LIBOR
Pay-Fixed Interest Rate Swap	Hedge changes in cash flows on General Revenue 2015 Series Bonds	\$ 48,400,000	09/01/08	10/01/26	Pay 3.862% Receive SIFMA

As of June 30, 2016, the synthetic interest rates on the swapped portion of the 2003B and 2015 bonds were 3.59% and 4.25% respectively. The fair value of the pay-fixed interest rate swaps was estimated using the discounted cash flows method adjusted for credit risk. This method calculates the fair market value of the instruments.

*Future Swaps:* The University has also entered into a future dated interest rate swap agreement for \$22,382,500 to be effective March 1, 2017, on the General Revenue Series 2015 bonds.

### *Hedging Derivative Risks*

*Credit Risk:* At June 30, 2016, the University was not exposed to credit risk on its interest rate swaps because the swaps had negative fair values. However, should interest rates change and the fair value of the swap becomes positive, the University would be exposed to credit risk in the amount of the derivative's positive fair value. The swap agreements require termination should the University's or the counterparty's credit rating fall below either Baa2 as issued by Moody's or BBB as issued by S&P or Fitch. Also, under the terms of the swap agreements, should one party become insolvent or otherwise default on its obligations, provisions permit the nondefaulting party to accelerate and terminate all outstanding transactions. To mitigate the potential for credit risk, if the counterparty's credit quality falls below A3 as determined by Moody's or A- as determined by S&P, the swap will be collateralized by the counterparty with cash, U.S. government or agency securities. If the counterparty is required to collateralize, then the collateral will be posted with a third party custodian or secured party. The swap agreements entered into by the University are held with separate counterparties. All the counterparties are rated A or better.

*Interest Rate Risk:* The University is exposed to interest rate risk on its interest rate swaps. The fair values of these instruments are highly sensitive to interest rate changes. Because rates have changed since the effective dates of the swaps, both of the swaps have a negative fair value as of June 30, 2016. 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 fair values are the market values as of June 30, 2016. Both of the swaps outstanding have termination dates greater than 10 years. As the yield curve rises, the value of the swaps will increase and as rates fall, the value of the swaps will decrease.

*Basis Risk:* The University is exposed to basis risk on the swaps when the variable payment received is based on an index other than Securities Industry and Financial Markets Association (SIFMA). Should the relationship between London Interbank Offering Rate (LIBOR) and SIFMA move to convergence, the expected cost savings may not be realized. The current outstanding swaps and the related bonds reset rates weekly/monthly and pay monthly. As of June 30, 2016, the SIFMA rate was 0.41% whereas 75% of LIBOR was 0.35%.

*Termination Risk:* The University or the counterparty may terminate any of the swaps if the other party fails to perform under the terms of the contract. If any of the swaps are terminated, the associated variable-rate bonds would no longer carry synthetic interest rates. Also, if at the time of termination the swap has a negative fair value, the University would be liable to the counterparty for that amount.

*Rollover Risk:* By definition, the University is exposed to rollover risk because the swap related to the 2015 bonds terminates October 1, 2026, two years before the related bonds mature on October 1, 2028. It is not the intent of the University, at this time, to re-hedge the bonds.

**NOTE 11 - LEASE OBLIGATIONS**

**A. Capital Lease Obligations** - Capital lease obligations relating to 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, 2016:

<u>Fiscal Year</u>	<u>Amount</u>
2017	\$ 177,071
2018	168,193
2019	132,732
2020	103,699
2021	<u>14,843</u>
Total Minimum Lease Payments	596,538
Amount Representing Interest (9.28% Rate of Interest)	<u>55,361</u>
Present Value of Future Lease Payments	<u>\$ 541,177</u>

Machinery and equipment acquired under capital lease amounted to \$693,019 at June 30, 2016.

Depreciation for the capital assets associated with capital leases is included in depreciation expense, and accumulated depreciation for assets acquired under capital lease totaled \$159,924 at June 30, 2016.

**B. Operating Lease Obligations** - The University entered into operating leases for equipment and property rental. Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2016:

<u>Fiscal Year</u>	<u>Amount</u>
2017	\$ 7,986,337
2018	6,211,743
2019	5,456,268
2020	4,928,265
2021	4,498,783
2022-2026	20,399,946
2027-2031	<u>6,050,030</u>
Total Minimum Lease Payments	<u>\$ 55,531,372</u>

Rental expense for all operating leases during the year was \$9,543,859.

**NOTE 12 - 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	Net Revenues
Operating Revenues:					
Student Tuition and Fees, Net	\$ 384,353,238	\$ 786,343	\$ 92,512,605	\$ (121,029)	\$ 291,175,319
Sales and Services, Net	\$ 326,253,538	\$ 67,501,870	\$ 20,236,097	\$ 67,822	\$ 238,447,749
Other Revenues, Net	\$ 20,168,569	\$ 5,898,208	\$ 0	\$ (21,762)	\$ 14,292,123

**NOTE 13 - 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/ Amortization	Total
Instruction	\$ 361,878,608	\$ 24,116,529	\$ 42,657,531	\$ 0	\$ 5,441	\$ 0	\$ 428,658,109
Research	168,828,741	21,385,218	77,246,361		954,611		268,414,931
Public Service	80,420,990	10,400,241	28,079,282		409,729		119,310,242
Academic Support	45,251,093	18,319,102	20,089,901		20,707		83,680,803
Student Services	18,372,847	2,092,883	7,831,358		202,910		28,499,998
Institutional Support	69,216,676	4,438,557	20,107,650		5,664		93,768,547
Operations and Maintenance of Plant	35,442,516	10,510,234	9,915,554		23,119,349		78,987,653
Student Financial Aid	1,262,882	110,546	840,646	43,820,372			46,034,446
Auxiliary Enterprises	76,576,214	36,537,737	44,997,619		7,310,086		165,421,656
Depreciation/ Amortization						88,721,461	88,721,461
Total Operating Expenses	\$ 857,250,567	\$ 127,911,047	\$ 251,765,902	\$ 43,820,372	\$ 32,028,497	\$ 88,721,461	\$ 1,401,497,846

**NOTE 14 - PENSION PLANS**

**A. Defined Benefit Plan**

*Plan Administration:* The State of North Carolina administers the Teachers' and State Employees' Retirement System (TSERS) plan. This plan is a cost-sharing, multiple-employer, defined benefit pension plan established by the State to provide pension benefits for general employees and law enforcement officers (LEOs) of the State, general employees and LEOs of its component units, and employees of Local Education Agencies (LEAs) and charter schools not in the reporting entity. Membership is comprised of employees of the State (state agencies and institutions), universities, community colleges, and certain proprietary component units along with the LEAs and charter schools. Benefit provisions are established by General Statute 135-5 and may be amended only by the North Carolina General Assembly.

*Benefits Provided:* TSERS provides retirement and survivor benefits. Retirement benefits are determined as 1.82% of the member's average

final compensation times the member's years of creditable service. A member's average final compensation is calculated as the average of a member's four highest consecutive years of compensation. General employee plan members are eligible to retire with full retirement benefits at age 65 with five years of creditable service, at age 60 with 25 years of creditable service, or at any age with 30 years of creditable service. General employee plan members are eligible to retire with partial retirement benefits at age 50 with 20 years of creditable service or at age 60 with five years of creditable service. Survivor benefits are available to eligible beneficiaries of general members who die while in active service or within 180 days of their last day of service and who also have either completed 20 years of creditable service regardless of age, or have completed five years of service and have reached age 60. Eligible beneficiaries may elect to receive a monthly Survivor's Alternate Benefit for life or a return of the member's contributions. The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains of the plan.

*Contributions:* Contribution provisions are established by General Statute 135-8 and may be amended only by the North Carolina General Assembly. Employees are required to contribute 6% of their annual pay. The contribution rate for employers is set each year by the NC General Assembly in the Appropriations Act based on the actuarially-determined rate recommended by the actuary. The University's contractually-required contribution rate for the year ended June 30, 2016 was 9.15% of covered payroll. The University's contributions to the pension plan were \$28,562,190, and employee contributions were \$18,729,305 for the year ended June 30, 2016.

The TSERS Plan's financial information, including all information about the plan's assets, deferred outflows of resources, liabilities, deferred inflows of resources, and fiduciary net position, is included in the State of North Carolina's fiscal year 2015 *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.

*TSERS Basis of Accounting:* The financial statements of the TSERS plan were prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has a legal requirement to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan. The plan's fiduciary net position was determined on the same basis used by the pension plan.

*Methods Used to Value TSERS Investment:* Pursuant to North Carolina General Statutes, the State Treasurer is the custodian and administrator of the retirement systems. The State Treasurer maintains various investment portfolios in its Investment Pool. The pension trust funds are

the primary participants in the Long-term Investment portfolio and the sole participants in the External Fixed Income Investment, Equity Investment, Real Estate Investment, Alternative Investment, Credit Investment, and Inflation Protection Investment portfolios. The investment balance of each pension trust fund represents its share of the fair market value of the net position of the various portfolios within the pool. Detailed descriptions of the methods and significant assumptions regarding investments of the State Treasurer are provided in the 2015 *Comprehensive Annual Financial Report*.

*Net Pension Liability:* At June 30, 2016, the University reported a liability of \$78,841,126 for its proportionate share of the collective net pension liability. The net pension liability was measured as of June 30, 2015. The total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of December 31, 2014, and update procedures were used to roll forward the total pension liability to June 30, 2015. The University's proportion of the net pension liability was based on the present value of future salaries for the University relative to the present value of future salaries for all participating employers, actuarially-determined. As of June 30, 2015, the University's proportion was 2.14%, which was a decrease of .01 from its proportion measured as of June 30, 2014.

*Actuarial Assumptions:* The following table presents the actuarial assumptions used to determine the total pension liability for the TSERS plan at the actuarial valuation date:

Valuation Date	12/31/2014
Inflation	3%
Salary Increases*	4.25% - 9.10%
Investment Rate of Return**	7.25%

\* Salary increases include 3.5% inflation and productivity factor.

\*\* Investment rate of return is net of pension plan investment expense, including inflation.

TSERS currently uses mortality tables that vary by age, gender, employee group (i.e. teacher, general, law enforcement officer) and health status (i.e. disabled and healthy). The current mortality rates are based on published tables and based on studies that cover significant portions of the U.S. population. The healthy mortality rates also contain a provision to reflect future mortality improvements.

The actuarial assumptions used in the December 31, 2014 valuations were based on the results of an actuarial experience study for the period January 1, 2005 through December 31, 2009.

Future ad hoc Cost of Living Adjustment (COLA) amounts are not considered to be substantively automatic and are therefore not included in the measurement.



The projected long-term investment returns and inflation assumptions are developed through review of current and historical capital markets data, sell-side investment research, consultant whitepapers, and historical performance of investment strategies. Fixed income return projections reflect current yields across the U.S. Treasury yield curve and market expectations of forward yields projected and interpolated for multiple tenors and over multiple year horizons. Global public equity return projections are established through analysis of the equity risk premium and the fixed income return projections. Other asset categories and strategies' return projections reflect the foregoing and historical data analysis. These projections are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2015 (the valuation date) are summarized in the following table:

<u>Asset Class</u>	<u>Long-Term Expected Real Rate of Return</u>
Fixed Income	2.2%
Global Equity	5.8%
Real Estate	5.2%
Alternatives	9.8%
Credit	6.8%
Inflation Protection	3.4%

The information above is based on 30-year expectations developed with the consulting actuary for the 2014 asset, liability and investment policy study for the North Carolina Retirement Systems. The long-term nominal rates of return underlying the real rates of return are arithmetic annualized figures. The real rates of return are calculated from nominal rates by multiplicatively subtracting a long-term inflation assumption of 3.19%. All rates of return and inflation are annualized.

*Discount Rate:* The discount rate used to measure the total pension liability was 7.25%. The projection of cash flows used to determine the discount rate assumed that contributions from plan members will be made at the current contribution rate and that contributions from employers will be made at statutorily required rates, actuarially determined. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of the current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

*Sensitivity of the Net Pension Liability to Changes in the Discount Rate:* The following presents the net pension liability of the plan calculated using the discount rate of 7.25%, as well as what the net pension liability

would be if it were calculated using a discount rate that is 1-percentage point lower (6.25%) or 1-percentage point higher (8.25%) than the current rate:

Net Pension Liability (Asset)		
1% Decrease (6.25%)	Current Discount Rate (7.25%)	1% Increase (8.25%)
\$ 237,290,032	\$ 78,841,126	\$ (55,621,041)

*Deferred Inflows of Resources and Deferred Outflows of Resources Related to Pensions:* For the year ended June 30, 2016, the University recognized pension expense of \$8,589,794. At June 30, 2016, the University reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

Employer Balances of Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions by Classification:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference Between Actual and Expected Experience	\$ 0	\$ 8,964,236
Changes of Assumptions		
Net Difference Between Projected and Actual Earnings on Pension Plan Investments		8,541,768
Change in Proportion and Differences Between Agency's Contributions and Proportionate Share of Contributions	2,722,767	
Contributions Subsequent to the Measurement Date	28,562,190	
Total	\$ 31,284,957	\$ 17,506,004

The amount of \$28,562,190 reported as deferred outflows of resources related to pensions will be included as a reduction of the net pension liability in the fiscal year ended June 30, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Schedule of the Net Amount of the Employer's Balances of Deferred Outflows of Resources and Deferred Inflows of Resources That will be Recognized in Pension Expense:

Year ended June 30:	Amount
2017	\$ (9,358,103)
2018	(9,358,103)
2019	(9,175,819)
2020	13,108,788
Total	\$ (14,783,237)

- B. Defined Contribution Plan** - The Optional Retirement Program (Program) is a defined contribution pension 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 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, 2016, 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 \$746,705,027, of which \$281,006,528 was covered under the Optional Retirement Program. Total employer and employee contributions for pension benefits for the year were \$19,220,847 and \$16,860,392, respectively. The amount of pension expense recognized in the current year related to ORP is equal to the employer contributions. The University had forfeitures reflected in pension expense for the current fiscal year of \$720,767.

**NOTE 15 - 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 (TSERS) or the Optional Retirement Program (ORP). 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 TSERS and contributions to the Fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and applicable beneficiaries and are not subject to the claims of creditors of the employers making contributions to the Fund. Contribution rates to the Fund, which are intended to finance benefits and administrative expenses on a pay-as-you-go basis, are established by the General Assembly.

For the current fiscal year the University contributed 5.60% of the covered payroll under TSERS and ORP to the Fund. Required contribution rates for the years ended June 30, 2015, and 2014, were 5.49% and 5.40%, respectively. The University made 100% of its annual required contributions to the Plan for the years ended June 30, 2016, 2015, and 2014, which were \$33,217,050, \$31,585,734, and \$29,986,156, 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 TSERS and ORP. 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, 2016, the University made a statutory contribution of .41% of covered payroll under TSERS and ORP to the DIPNC. Required contribution rates for the years ended June 30, 2015, and 2014, were .41% and .44%, respectively. The University made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2016, 2015, and 2014, which were \$2,431,963, \$2,358,862, and \$2,443,316, 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 16 - 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 reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

### **A. Employee Benefit Plans**

#### **1. State Health 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.

#### **2. Death Benefit Plan of North Carolina**

Term life insurance (death benefits) of \$25,000 to \$50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State Treasurer and funded via employer contributions. The employer contribution rate was .16% for the current fiscal year.

### **B. Other Risk Management and Insurance Activities**

#### **1. Automobile, Fire, and Other Property Losses**

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. Losses covered by the Fund are subject to a \$5,000 per occurrence deductible. University departments, as an individual business decision, may also purchase through the Fund primary extended coverage for buildings and contents. Coverage may also be purchased through the Fund for theft, vandalism, sprinkler leakage, or all-risk perils. University departments also have the option to purchase all-risk coverage for computers and "miscellaneous equipment" on a scheduled basis. Flood insurance may also be purchased through the Fund for qualifying assets.

Receipts-supported auxiliary units insure assets for additional perils coverage, as per the options noted above, in addition to the fire and lightning perils. General-funded departments and units insure for the perils of fire and lightning with the exception of certain coastal properties which are also insured for extended coverage perils and the peril of flood.

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.

## **2. 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 via contract with a private insurance company. The University pays the premium, based on a composite rate, directly to the private insurer.

## **3. Employee Dishonesty 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 \$1,000,000 per occurrence. The applicable deductible is \$25,000 per occurrence.

## **4. Statewide Workers' Compensation Program**

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.

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.

## 5. Other Insurance Held by the University

The University purchased other authorized coverage from private insurance companies through the North Carolina Department of Insurance and the State's Agent of Record. The types of insurance policies purchased include: medical professional liability, veterinary professional liability, fine arts property, master crime, inland marine property for musical instruments, campers accident and sickness, athletic accident, boiler and machinery, watercraft, oceanographic equipment, data breach, and nuclear energy liability.

### NOTE 17 - COMMITMENTS AND CONTINGENCIES

- A. Commitments** - The University has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were \$20,666,282 and on other purchases were \$215,000 at June 30, 2016.

The University has amended the Use Agreement for the PNC Arena with the Centennial Authority (a related party) and therein agreed to make scheduled capital contributions totaling \$6,000,000 to the Authority's Building Enhancement Fund over a 15 year period. The total outstanding commitment on this agreement was \$3,100,000 as of June 30, 2016.

- B. Pending Litigation and Claims** - As previously reported, the Environmental Protection Agency (EPA) filed a civil action against the University pursuant to the Comprehensive Environmental Response, Compensation and Liability Act. The complaint sought relief that would cause the University to enter into remediation of a hazardous waste site known as "Lot 86." The University is involved in ongoing discussions and negotiations with the EPA concerning the appropriate means for addressing the remediation. A Consent Decree executed by North Carolina State University and the EPA has been approved by the Court. Remedial clean-up pursuant to the Consent Decree continues. The remediation costs remaining are estimated to be approximately \$2,000,000.

As previously reported, the NC School Boards Association, et. al. filed a civil action against various state officials in their official capacity seeking a judicial determination as to whether the state constitution requires certain monetary payments collected by state agencies to be paid to the local county school funds. On July 1, 2005, the NC Supreme Court held in favor of the school boards with regard to parking fines. The matter was remanded back to the trial court for disposition in accordance with the Superior Court's decision. On August 8, 2008, the Wake County Superior Court issued judgment that the estimated amounts collected from January 1, 1996, to June 30, 2005, by UNC Campuses belong and should have been paid to the public schools of the State by payment to the State's Civil Penalty and Forfeiture Fund. The manner in which the judgment will be settled is uncertain and is to be determined by the

North Carolina General Assembly. At issue for NC State University is approximately \$6,749,207 in transportation fines collected since January 1, 1996, to June 30, 2005. Of this amount, the university has transferred \$2,273,817 to the Office of State Budget and Management leaving approximately \$4,475,390 still outstanding. Since July 2005, the University has been forwarding transportation fine collections, less collection costs, to the Office of State Budget and Management on a monthly basis.

As previously reported, on September 16, 2005, Ward Transformer Company, Inc. and related entities (collectively the "Ward Performing Parties") entered into a Settlement Agreement with the United States Environmental Protection Agency ("EPA"). In the Agreement, the Ward Performing Parties agreed to fund and carry out a removal action to address PCB contamination at and in the vicinity of the 11 acre Ward Transformer facility on Mount Herman Road near the Raleigh-Durham International Airport. It is currently estimated that the removal action will involve the excavation and onsite treatment or offsite disposal of approximately 60,000 cubic yards, or about 220,000 tons, of PCB contaminated soils. Current estimates indicate that the costs may be in the range upwards of \$70 million (the University would be responsible for a portion of this amount). The Ward Performing Parties have notified NC State that they believe that the University is responsible for some of the PCB contamination because NC State allegedly had Ward repair and refurbish transformers during the 1960's through the 1990's. On March 24, 2010, the Court granted the University's Motion to Dismiss based on the 11<sup>th</sup> Amendment sovereign immunity. However, this case is still open pending an appeal by the plaintiffs. In January 2013, the EPA indicated its desire to pursue a global settlement involving all parties for all past and future remediation costs, and indicated that parties not participating in the global settlement negotiations will face enforcement action by the EPA. As the University would not have a sovereign immunity defense available in an enforcement action brought by the EPA, on March 5, 2013, the University communicated its intent to participate in future global settlement negotiations with the EPA. On August 19, 2016, NCSU agreed to pay \$110,000 no later than September 9, 2016 in the global settlement.

The University is a party to other 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 is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.

#### **NOTE 18 - RELATED PARTIES**

**Foundations** - There are 10 separately incorporated nonprofit foundations associated with the University. These foundations are The North Carolina Agricultural Foundation, Inc., North Carolina State University Foundation, Inc.,



North Carolina Tobacco Foundation, Inc., North Carolina State University College of Sciences Foundation, Inc., NC State Engineering Foundation, Inc., North Carolina Veterinary Medical Foundation, Inc., NC State Natural Resources Foundation, Inc., North Carolina Textile Foundation, Inc., NC State Student Aid Association, Inc., and the North Carolina State University Alumni Association, Inc.

These organizations serve 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. As described in Note 1 to the financial statements, The North Carolina Agricultural Foundation, Inc., the North Carolina State University Foundation, Inc. and the NC State Student Aid Association, Inc. are considered component units of the University for reporting purposes and their financial statements are presented separately as part of the University's financial statements. The University's financial statements do not include the assets, liabilities, net position, or operational transactions of the other foundations, except for support from each organization to the University. This support of the foundations, excluding amounts from The North Carolina Agricultural Foundation, Inc., the North Carolina State University Foundation, Inc. and the NC State Student Aid Association, Inc. approximated \$19,882,474 for the year ended June 30, 2016.

**Reynolds Coliseum** - The NC State Student Aid Association has agreed to fund \$20,000,000 of the \$35,000,000 project to renovate the University's Reynolds Coliseum.

**Case Commons Residence Hall** - The NC State Student Aid Association has agreed to fund the construction of an athletics residence hall for the University. The project is estimated to cost approximately \$15,000,000 plus interest, and payments are scheduled to begin in 2018.

**Nonprofit Corporation** - The Centennial Authority (Authority) was created by the 1995 General Assembly (Senate Bill 606) for the purpose of studying, designing, planning, constructing, owning, promoting, financing and operating a regional facility on land owned by the State. Prior to this act, the General Assembly authorized the construction by the University of a facility to be known as the "Entertainment and Sports Arena" (ESA). This facility serves as a regional sports entertainment center and is available for cultural performances, sporting events and other activities of the University or of other entities (the Centennial Center project). With the 1995 legislation, the Centennial Center project was transferred to the Authority.

The Authority entered into a Ground Lease with the State of North Carolina to lease land for the ESA for a period of 99 years at an annual rent of \$1. The University entered into a Use Agreement with the Authority. Both parties agreed that the University shall be the primary and preferred user of all areas of the ESA. The University is required to pay the greater of 10% of gross ticket revenues or \$51,577 for each men's and \$22,559 for each women's basketball

game to compensate the Authority for facility rental and operating expenses. Rent and expense payments for miscellaneous events will be negotiated on an event by event basis based on the availability of the ESA and the anticipated attendance. In fiscal year 2012, the name of the ESA was changed to "PNC Arena."

In fiscal year 2008, the University entered a Capital Improvement Plan Agreement with the Authority to pay \$6,000,000 in quarterly installments over 15 years.

**NOTE 19 - BLENDED COMPONENT UNITS**

Condensed combining information for the University's blended component units for the year ended June 30, 2016 is presented as follows:

*Condensed Statement of Net Position  
June 30, 2016*

	North Carolina State University	NC State Investment Fund, Inc.	NC State University Partnership Corporation	Eliminations	Total
<b>ASSETS</b>					
Current Assets	\$ 363,229,022	\$ 34,225,218	\$ 5,551,317	\$ 0	\$ 403,005,557
Capital Assets	2,004,443,996		20,884,295		2,025,328,291
Other Noncurrent Assets	214,337,260	521,918,935	1	(29,683,979)	706,572,216
Total Assets	2,582,010,278	556,144,153	26,435,612	(29,683,979)	3,134,906,064
Total Deferred Outflows of Resources	45,122,224				45,122,224
<b>LIABILITIES</b>					
Current Liabilities	160,065,864	375,393	593,847		161,035,104
Long-Term Liabilities, Net	679,949,414		2,785,750		682,735,164
Other Noncurrent Liabilities	356,742,187		442,130	(29,683,979)	327,500,338
Total Liabilities	1,196,757,465	375,393	3,821,727	(29,683,979)	1,171,270,606
Total Deferred Inflows of Resources	17,506,004				17,506,004
<b>NET POSITION</b>					
Net Investment in Capital Assets	1,396,273,608		17,550,564		1,413,824,172
Restricted - Nonexpendable	(436,505,221)	555,768,760	2		119,263,539
Restricted - Expendable	217,451,651		279,671		217,731,322
Unrestricted	235,648,995		4,783,650		240,432,645
Total Net Position	\$ 1,412,869,033	\$ 555,768,760	\$ 22,613,885	0	\$ 1,991,251,678

<sup>1</sup> Total investments in the NC State Investment Fund, Inc. audit report included \$298,274,678 held in the Investment Fund for the North Carolina State University Foundation, Inc. and The North Carolina Agricultural Foundation, Inc. This amount is excluded from the University prepared financial statements and included in the accompanying component unit financial statements. See Note 2 to the Financial Statements. It will therefore be excluded from the Condensed Statement of Net Position and the Condensed Statement of Revenues, Expenses, and Changes in Net Position.

<sup>2</sup> Restricted Nonexpendable assets are held in the NC State Investment Fund, Inc. while the associated liabilities are held in North Carolina State University statements resulting in a negative net position before blending.

## NOTES TO THE FINANCIAL STATEMENTS

*Condensed Statement of Revenues, Expenses, and  
Changes in Net Position  
For the Fiscal Year Ended June 30, 2016*

	North Carolina State University	NC State Investment Fund, Inc.	NC State University Partnership Corporation	Eliminations	Total
<b>OPERATING REVENUES</b>					
Operating Revenue	\$ 831,151,521	\$ 0	\$ 8,939,738	\$ (3,738,796)	\$ 836,352,463
<b>OPERATING EXPENSES</b>					
Operating Expenses	1,310,175,252	1,857,782	6,060,008	(5,316,657)	1,312,776,385
Depreciation/Amortization	88,283,225		438,236		88,721,461
Total Operating Expenses	1,398,458,477	1,857,782	6,498,244	(5,316,657)	1,401,497,846
Operating Income (Loss)	(567,306,956)	(1,857,782)	2,441,494	1,577,861	(565,145,383)
<b>NONOPERATING REVENUES (EXPENSES)</b>					
State Appropriations	502,533,982				502,533,982
Noncapital Grants	45,499,300				45,499,300
Noncapital Gifts	71,230,776				71,230,776
Investment Income	(5,688,899)	7,258,215			1,569,316
Other Nonoperating Expenses	(14,822,534)		(33,330)		(14,855,864)
Net Nonoperating Revenues (Expenses)	598,752,625	7,258,215	(33,330)		605,977,510
Capital Appropriations	9,013,500				9,013,500
Capital Grants	2,508,299				2,508,299
Capital Gifts	6,960,812		1,578,907	(1,577,861)	6,961,858
Additions to Endowments	14,039,031				14,039,031
Increase in Net Position	63,967,311	5,400,433	3,987,071		73,354,815
<b>NET POSITION</b>					
Net Position, July 1, 2015	1,348,901,722	550,368,327	18,626,814		1,917,896,863
Net Position, June 30, 2016	\$ 1,412,869,033	\$ 555,768,760	\$ 22,613,885	\$ 0	\$ 1,991,251,678

*Condensed Statement of Cash Flows  
June 30, 2016*

	North Carolina State University	NC State Investment Fund, Inc.	NC State University Partnership Corporation	Total
Net Cash Provided (Used) by Operating Activities	\$ (490,055,767)	\$ 0	\$ 2,614,623	\$ (487,441,144)
Net Cash Provided by Noncapital Financing Activities	733,376,129			733,376,129
Net Cash Used by Capital and Related Financing Activities	(94,740,697)		(202,253)	(94,942,950)
Net Cash Provided (Used) by Investing Activities	(11,385,943)	32,143,220		20,757,277
Net Increase in Cash and Cash Equivalents	137,193,722	32,143,220	2,412,370	171,749,312
Cash and Cash Equivalents, July 1, 2015	310,799,226	2,081,998	2,956,067	315,837,291
Cash and Cash Equivalents, June 30, 2016	\$ 447,992,948	\$ 34,225,218	\$ 5,368,437	\$ 487,586,603

### NOTE 20 - CHANGES IN FINANCIAL ACCOUNTING AND REPORTING

For the fiscal year ended June 30, 2016, the University implemented the following pronouncements issued by the Governmental Accounting Standards Board (GASB):

*GASB Statement No. 72, Fair Value Measurement and Application*

GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement No. 68, and Amendments to Certain Provisions of GASB Statements No. 67 and 68*

GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*

GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*

GASB Statement No. 72 provides guidance for determining a fair value measurement for financial reporting purposes. This statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements.

GASB Statement No. 73 establishes requirements for defined benefit pensions that are not within the scope of Statement No. 68, *Accounting and Financial Reporting for Pensions*, as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the scope of Statement No. 68. It also amends certain provisions of Statement No. 67, *Financial Reporting for Pension Plans*, and Statement No. 68 for pension plans and pensions that are within their respective scopes.

GASB Statement No. 76 reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP.

GASB Statement No. 79 establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes.

#### **NOTE 21 - SUBSEQUENT EVENTS**

On August 12, 2016, Golden LEAF Foundation awarded North Carolina State University a \$45 million grant that will help support a new research facility for the North Carolina Plant Sciences Initiative.

On August 23, 2016, the University issued an additional \$10 million in Commercial Paper, bringing total outstanding to \$50 million. These funds provide interim funding for the Reynolds Coliseum Renovation and the Carmichael Locker Room Renovation.

**NOTE 22 - DISCRETELY PRESENTED COMPONENT UNITS**

The University's discretely presented component units use the accounting and reporting standards promulgated by FASB. Selected disclosures from the discretely presented component units' audited financial statements follow:

**NORTH CAROLINA STATE UNIVERSITY FOUNDATION, INC.**

**Long-Term Investments**

The Foundation invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statements of financial position.

Investments at June 30, 2016 consisted of:

	<u>Cost</u>	<u>Fair Value</u>
STIF	\$ 250,343	\$ 250,343
NC State Investment Fund , Inc.		
Long-Term Investment Pool (LTIP)	166,104,657	214,207,848
SRI Fund	9,269,614	9,887,699
Wells Fargo - Life Income Funds	<u>5,886,277</u>	<u>6,146,163</u>
Total	<u>\$ 181,510,891</u>	<u>\$ 230,492,053</u>

Investments held by the LTIP at June 30, 2016 were made up of limited partnerships, an investment with a Blackrock Liquid Policy Portfolio ("LPP"), a bundle of exchange-traded funds, and the STIF. As of June 30, 2016, approximately 91.2% of these limited partnerships were with the UNC Management Company, 3.5% were committed to or in other private equity investments with JP Morgan, Blackrock, and SEI, 5.1% was invested in the LPP, and 0.2% was invested in the STIF. The LTIP's net assets were valued at approximately \$683,380,000 at June 30, 2016. The Foundation's investment in the LTIP represents approximately 31.3% of the member equity of the LTIP at June 30, 2016.

The SRI Fund assets are invested in a socially responsible manner through a diversified portfolio of managers that consider environmental, social, and governance issues. As of June 30, 2016, approximately 27.7% of total assets were invested with RBC SRI Wealth Management Group (RBC), 51.9% with Generation IM Global Equity A Fund, and 20.4% with Calvert Bond Portfolio.

The Foundation's investments held by Wells Fargo - Life Income Funds consist of a diversified portfolio of bond and equity mutual funds.

### Life Income Funds

The consolidated financial statements include assets and liabilities of charitable gift annuities and unitrust agreements for which the Foundation is trustee. The grantors and/or beneficiaries retain future income interests in these assets until their death. These life income funds are recorded at fair value at the date of gift. Life income funds at June 30, 2016 have asset balances of \$6,146,163.

The liabilities for distributions to grantors and/or beneficiaries are computed using Internal Revenue Code annuity valuation tables, the distribution terms of the agreements, and the life expectancy of the beneficiaries, and totaled \$3,283,841 at June 30, 2016. Payments from these funds were \$466,547 during the year ended June 30, 2016. An unrestricted reserve account has been established in the Foundation's Charitable Gift Annuity ("CGA") pool to receive 5% from all new CGAs established in order to offset the liabilities for any annuities that reach exhaustion. The goal is to build the unrestricted reserve fund to equal 5% of the total value of the Foundation's CGA pool. As of June 30, 2016, the CGA reserve balance was \$0.

In addition to the above life income funds, the Foundation was named the recipient of an externally managed trust in 2011 which represents irrevocable life income funds with a market value totaling \$18,843,468 and life income funds payable of \$10,569,983 as of June 30, 2016. The Foundation is not serving as trustee for these funds. These life income funds have been reflected in the accompanying consolidated financial statements at their fair value. Estimated future distributions to the beneficiaries have been reflected in the accompanying consolidated financial statements and were computed using Internal Revenue Code annuity valuation tables, the distribution terms of the agreements, and the life expectancy of the beneficiaries.

### Pledges Receivable

Pledges receivable are stated at their present value, estimated by discounting the future cash flows using Federal Reserve rates of return, and are as follows:

Receivable in less than one year	\$ 7,696,632
Receivable in one to five years	57,679,162
Receivable in greater than five years	<u>23,366</u>
Total gross pledges receivable	65,399,160
Less allowance for uncollectible pledges	420,000
Less unamortized discount	<u>1,041,709</u>
Net Pledges Receivable	<u>\$ 63,937,451</u>

An allowance for doubtful accounts has been established and is updated annually to reflect 5% of the Foundation's outstanding pledge balance, excluding three large pledges for which signed memorandums of understanding exist and therefore the Foundation is reasonably assured of

collecting. Such pledges represented approximately \$57.0 million of total pledges receivable at year ended June 30, 2016. Active past due pledges receivable are reviewed semi-annually by the Advancement Services office in order to determine if it is appropriate to write off such pledges.

**NC STATE STUDENT AID ASSOCIATION, INC.**

**Pledges Receivable**

The Association carries its pledges receivable at cost less a discount for pledges receivable due in more than a year and less an allowance for doubtful accounts. On a periodic basis, the Association evaluates its receivables and establishes an allowance for doubtful accounts, based on history of past write-offs and current credit conditions.

Pledges receivable at June 30, 2016 are as follows:

Pledges Receivable	\$ 31,852,944
Less Allowance for Uncollectible Pledges	1,592,647
Less Discount on Pledges	<u>7,267,389</u>
	22,992,908
Less Current Portion	<u>4,331,237</u>
Pledges Due After One Year	<u>\$ 18,661,671</u>

Pledges receivable due in more than one year are reflected at the present value of estimated future cash flows using a discount rate of 6%.

Receivable in Less Than One Year	\$ 4,559,198
Receivable in One to Five Years	11,933,187
Receivable in More Than Five Years	<u>15,360,559</u>
Total Gross Pledges Receivable	31,852,944
Less Allowance for Uncollectible Pledges	1,592,647
Less Discount on Pledges	<u>7,267,389</u>
Net Pledges Receivable	<u>\$ 22,992,908</u>

Under the Vaughn Towers Management and Use Agreement dated March 2013, Goal Line Drive and Wolfpack Pride campaign pledge revenues totaling \$7,206,915 were committed to be paid to NCSU to retire certain facility debt and other obligations related to NCSU's athletic facilities. Payments in the amount of \$1,441,383 are due annually over five years through May 2017. The remaining commitment at June 30, 2016 was \$1,441,383.

**Investments**

The Association held the following investments at June 30, 2016:

	Historical Cost	Market Value
Marketable Equity Securities	\$ 14,074,876	\$ 15,102,501
Other Marketable Debt Securities	6,013,732	6,103,186
U.S. Government Obligations	4,169,782	4,202,121
Alternative Investments	5,864,504	5,795,374
Mutual Funds	1,043,543	1,085,864
Total	<u>\$ 31,166,437</u>	<u>\$ 32,289,046</u>

Investment income (loss) consists of the following:

Interest	\$ 339,528
Dividends	349,159
Realized Gain on Sale of Investments	1,094,344
Unrealized Loss on Investments	(2,583,573)
Investment Expenses	<u>(254,245)</u>
Total	<u>\$ (1,054,787)</u>

**Long-Term Debt**

**Bond Indentures - Vaughn Towers:** In March 2013, the Association refinanced bonds originally issued in 2004 to finance the construction of the Vaughn Towers press box at Carter-Finley Stadium. The refinancing was with Branch Banking & Trust Company (BB&T) through a \$12,660,000 Series 2013 bond, issued through the North Carolina Capital Facilities Finance Agency. The bond pays interest monthly at a variable rate based on the monthly London Interbank Offered Rates (LIBOR). The variable rate was 1.40357% at June 30, 2016. Principal payments of \$1,055,000 are due annually until the bond matures in September 2024. The outstanding bond principal was \$9,495,000 at June 30, 2016.

**Note Payable - Wolves Den:** In June 2015, the Association entered into a note agreement in the amount of \$450,000 with BB&T in order to finance the renovation of a portion of Vaughn Towers into a new premium seating option at Carter-Finley Stadium, referred to as the Wolves Den. Annual principal payments of \$112,500 are payable beginning in January 2016 until the note matures in January 2019. Interest is payable annually at a rate equal to the One Month LIBOR (0.46885% at June 30, 2016) plus 1.15% per annum. The outstanding balance of the note payable was \$337,500 at June 30, 2016.

**Note Payable - North End Zone:** In November 2012, the Association refinanced the existing notes payable originally issued to finance the stadium expansion of the North End Zone area of Carter-Finley Stadium to one note payable to BB&T. Annual principal payments of \$256,750 are payable until the



note matures in November 2016. Interest is payable monthly at a rate equal to the One Month LIBOR (0.46885% at June 30, 2016) plus 1.15% per annum. The Association must maintain a cash flow coverage ratio of 1.00 times debt service. The outstanding note balance was \$256,500 at June 30, 2016.

**Notes Payable - Indoor Practice Facility:** In May 2014, the Association entered into multiple note agreements with Branch Banking and Trust Company (BB&T) in order to finance the construction of a new Indoor Practice Facility for the football program at NCSU. The total financing available through the notes payable is \$14,000,000. The notes mature at various times through May 2026 and bear interest at fixed rates (ranging from 1.84% to 2.75%) and variable rates (One Month LIBOR plus 0.9%). The Association must maintain a debt service coverage ratio of 1.00 to 1.00, maintain unrestricted liquid assets of \$4,000,000 until such point that the credit available and outstanding total to less than \$10,000,000, and meet certain pledge targets. The notes payable are collateralized by pledges and cash received from the related capital campaign. The total outstanding balance of the notes payable was \$12,000,000 at June 30, 2016.

Long-term debt consists of the following at June 30, 2016:

Vaughn Towers Project--Series 2013 Bond	\$	9,495,000
Note Payable--BB&T (Wolves Den)		337,500
Note Payable--BB&T (North End Zone)		256,750
Note Payable--BB&T (Indoor Practice Facility)		<u>12,000,000</u>
		22,089,250
Less Amount Classified as Current Liability		<u>2,624,250</u>
Amount Due After One Year	\$	<u><u>19,465,000</u></u>

Maturities of long-term debt are as follows:

Year Ending June 30		
2017	\$	2,624,250
2018		2,367,500
2019		2,367,500
2020		2,255,000
2021		2,255,000
Thereafter		<u>10,220,000</u>
Total	\$	<u><u>22,089,250</u></u>

**THE NORTH CAROLINA AGRICULTURAL FOUNDATION, INC.**

**Long-Term Investments**

The Foundation invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities

will occur in the near term and that such changes could materially affect the amounts reported in the statements of financial position.

Investments at June 30, 2016 consisted of:

	<u>Cost</u>	<u>Fair Value</u>
STIF	\$ 208,207	\$ 208,207
NC State Investment Fund , Inc.		
Long-Term Investment Pool (LTIP)	49,876,222	67,709,880
Wells Fargo - Life Income Funds	<u>8,674,688</u>	<u>8,899,393</u>
Total	<u>\$ 58,759,117</u>	<u>\$ 76,817,480</u>

Investments held by the LTIP at June 30, 2016 were made up of limited partnerships, an investment with a Blackrock Liquid Policy Portfolio (“LPP”), a bundle of exchange-traded funds, and the STIF. As of June 30, 2016, approximately 91.2% of these limited partnerships were with the UNC Management Company (UNCMC), 3.5% were committed to or in other private equity investments with JP Morgan, Blackrock, and SEI, 5.1% was invested in the LPP, and 0.2% was invested in the STIF. The LTIP’s net assets were valued at approximately \$683,380,000 at June 30, 2016. The Foundation’s investment in LTIP represents approximately 9.91% of the member’s equity of the LTIP at June 30, 2016.

The Foundation’s investments in Life Income Funds consist of a diversified portfolio of bond and equity mutual funds.

**Pledges Receivable**

Pledges receivable consisted of the following at June 30:

Receivable in Less Than One Year	\$ 3,567,591
Receivable in One to Five Years	3,446,661
Receivable in Greater Than Five Years	<u>550,000</u>
Total Gross Pledges Receivable	7,564,252
Less Allowance for Uncollectible Pledges	279,000
Less Unamortized Discount (Discount Rate of 0.55% to 1.44%)	<u>162,322</u>
Net Pledges Receivable	<u>\$ 7,122,930</u>

An allowance for doubtful accounts has been established and is updated annually to reflect 5% of the Foundation’s outstanding pledge balance, excluding the Prestage Family Department of Poultry Science Endowment for Excellence pledge which the Foundation is reasonably assured of collecting. Active past due pledges receivable are reviewed twice yearly by the Advancement Services office in order to determine if it is appropriate to write off such pledges.

Three donors represent approximately \$4.55 million of total undiscounted pledges receivable at June 30, 2016.



# **REQUIRED SUPPLEMENTARY INFORMATION**

**North Carolina State University  
 Required Supplementary Information  
 Schedule of the Proportionate Net Pension Liability  
 Teachers' and State Employees' Retirement System  
 Last Three Fiscal Years**

**Exhibit C-1**

	<u>2015</u>	<u>2014</u>	<u>2013</u>
Proportionate Share Percentage of Collective Net Pension Liability	2.14%	2.15%	2.12%
Proportionate Share of TSERS Collective Net Pension Liability	\$ 78,841,126	\$ 25,160,037	\$ 128,553,827
Covered-Employee Payroll	\$ 308,539,969	\$ 305,353,765	\$ 306,165,883
Net Pension Liability as a Percentage of Covered-Employee Payroll	25.55%	8.24%	41.99%
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	94.64%	98.24%	90.60%

**North Carolina State University  
 Required Supplementary Information  
 Schedule of University Contributions  
 Teachers' and State Employees' Retirement System  
 Last Ten Fiscal Years**

**Exhibit C-2**

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Contractually Required Contribution	\$ 28,562,190	\$ 28,231,407	\$ 26,535,242	\$ 25,503,618	\$ 22,231,989
Contributions in Relation to the Contractually Determined Contribution	<u>28,562,190</u>	<u>28,231,407</u>	<u>26,535,242</u>	<u>25,503,618</u>	<u>22,231,989</u>
Contribution Deficiency (Excess)	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
Covered-Employee Payroll	\$ 312,155,082	\$ 308,539,969	\$ 305,353,765	\$ 306,165,883	\$ 298,817,058
Contributions as a Percentage of Covered-Employee Payroll	9.15%	9.15%	8.69%	8.33%	7.44%

	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Contractually Required Contribution	\$ 15,004,360	\$ 10,741,148	\$ 10,536,565	\$ 9,039,835	\$ 7,478,544
Contributions in Relation to the Contractually Determined Contribution	<u>15,004,360</u>	<u>10,741,148</u>	<u>10,536,565</u>	<u>9,039,835</u>	<u>7,478,544</u>
Contribution Deficiency (Excess)	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
Covered-Employee Payroll	\$ 304,348,067	\$ 300,872,483	\$ 313,588,252	\$ 296,388,035	\$ 281,148,259
Contributions as a Percentage of Covered-Employee Payroll	4.93%	3.57%	3.36%	3.05%	2.66%

**North Carolina State University**  
**Notes to Required Supplementary Information**  
**Schedule of University Contributions**  
**Teachers' and State Employees' Retirement System**  
**Last Ten Fiscal Years**

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*Changes of Benefit Terms:*

										<u>Cost of Living Increase</u>	
<u>2015*</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>		
1.00%	N/A	1.00%	N/A	N/A	N/A	2.20%	2.20%	3.00%	2.00%		

*Changes of assumptions.* In 2008, and again in 2012, the rates of withdrawal, mortality, service retirement and salary increase for active members and the rates of mortality for beneficiaries were adjusted to more closely reflect actual experience. Assumptions for leave conversions and loads were also revised in 2012.

\*Per the 2015 State of North Carolina *Comprehensive Annual Financial Report*, the 1.00% cost of living adjustment applies to retirees whose retirement began on or before July 1, 2013.



# **INDEPENDENT AUDITOR'S REPORT**

STATE OF NORTH CAROLINA  
**Office of the State Auditor**



**Beth A. Wood, CPA**  
State Auditor

2 S. Salisbury Street  
20601 Mail Service Center  
Raleigh, NC 27699-0600  
Telephone: (919) 807-7500  
Fax: (919) 807-7647  
<http://www.ncauditor.net>

**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**

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Board of Trustees  
North Carolina State University  
Raleigh, 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 North Carolina State University (University), 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, 2016, and the related notes to the financial statements, which collectively comprise the University's basic financial statements, and have issued our report thereon dated October 31, 2016. Our report includes a reference to other auditors who audited the financial statements of the NC State Investment Fund, Inc. and the discretely presented component units, as described in our report on the University's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of the North Carolina State University Foundation, Inc., the NC State Student Aid Association, Inc., and The North Carolina Agricultural Foundation, Inc., 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 these entities.

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 opinions 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 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

October 31, 2016

# ORDERING INFORMATION

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Office of the State Auditor  
State of North Carolina  
2 South Salisbury Street  
20601 Mail Service Center  
Raleigh, North Carolina 27699-0600

Telephone: 919-807-7500  
Facsimile: 919-807-7647  
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For additional information contact:  
Bill Holmes  
Director of External Affairs  
**919-807-7513**

