

STATE OF NORTH CAROLINA

EAST CAROLINA UNIVERSITY

GREENVILLE, NORTH CAROLINA

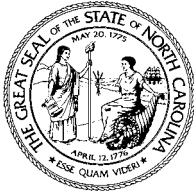
FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2014

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR



Beth A. Wood, CPA
State Auditor

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AUDITOR'S TRANSMITTAL

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

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

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

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

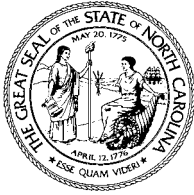
A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
East Carolina University
Greenville, North Carolina

Report on the Financial Statements

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

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of East Carolina University Foundation, Inc. and Consolidated Affiliates, the University's discretely presented component unit. Those statements were audited by other auditors, whose report has been furnished to us, and our opinions, insofar as they relate to the amounts included for discretely presented component unit, are based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. The financial statements of East Carolina University Foundation, Inc. and Consolidated Affiliates were not audited in accordance with *Government Auditing Standards*.

INDEPENDENT AUDITOR'S REPORT (CONTINUED)

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 report of the other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of East Carolina University and its discretely presented component unit, as of June 30, 2014, and the changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 18 to the financial statements, during the year ended June 30, 2014, the East Carolina University adopted new accounting guidance, Governmental Accounting Standards Board Statement No. 65 – *Items Previously Reported as Assets and Liabilities*. Our opinion is not modified with respect to this matter.

Other Matters – Required Supplementary Information

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

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 11, 2014 on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University's internal control over financial reporting and compliance.



Beth A. Wood, CPA
State Auditor

Raleigh, North Carolina

November 11, 2014

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EAST CAROLINA UNIVERSITY MANAGEMENT'S DISCUSSION AND ANALYSIS

Introduction

East Carolina University (ECU or University) provides this Management's Discussion and Analysis as supplementary information to assist in understanding the financial statements and related notes for the fiscal year ended June 30, 2014. The University is one of the 16 Universities in the University of North Carolina System (UNC System), a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report (CAFR)*. The University's financial report includes three financial statements:

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

It also includes two financial statements from the discretely presented component unit:

- ECU Foundation, Inc. and Consolidated Affiliates Consolidated Statement of Financial Position; and
- ECU Foundation, Inc. and Consolidated Affiliates Consolidated Statement of Activities and Changes in Net Assets.

The University's basic financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) principles, which establish standards for external financial reporting for public colleges and universities. Please note that although the University's Foundation identified under guidance from GASB standards is reported in the component unit financial statements, this Management's Discussion and Analysis excludes it except where specifically noted.

This discussion and analysis provides an overview of the University's financial position and activities for the year ended June 30, 2014, emphasizing current year data and significant changes between the prior and current fiscal year. Comparative information for the year ended June 30, 2013 has been provided where applicable. This overview has been prepared by management and should be read in conjunction with the financial statements and the notes to the financial statements that are included in this annual report. The Statement of Net Position reveals the University's overall financial position; the Statement of Revenues, Expenses and Changes in Net Position provides a summation of the results of operations, and the Statement of Cash Flows identifies the sources of cash and how cash was used during the year.

Statement of Net Position

The Statement of Net Position presents a fiscal snapshot of the University's financial position at a point-in-time, specifically, as of June 30, 2014 and includes all assets and liabilities of the University. The assets are available to continue the operations of the University and the

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

liabilities are amounts owed to vendors, investors, and lending institutions. Assets and liabilities are classified as either current or noncurrent. The difference between total assets and total liabilities is net position. Net position represents the residual interest in the University's assets net of its liabilities and is an indicator of the current financial strength of the University. The change in net position is an indicator of whether the overall financial condition of the University has improved or worsened during the year. The following table presents a summarized comparison of the University's assets, liabilities and net position at June 30, 2014 and 2013.

Condensed Statement of Net Position

(Dollars in Thousands)

	<u>2014</u>	<u>2013 (Restated)</u>	<u>Increase/ (Decrease)</u>	<u>Percent Change</u>
Assets				
Current Assets	\$ 284,556	\$ 287,261	\$ (2,705)	(0.9) %
Capital Assets, Net	898,042	874,772	23,270	2.7 %
Other Noncurrent Assets	<u>146,010</u>	<u>82,849</u>	<u>63,161</u>	76.2 %
Total Assets	<u>1,328,608</u>	<u>1,244,882</u>	<u>83,726</u>	6.7 %
Liabilities				
Current Liabilities	61,635	61,006	629	1.0 %
Noncurrent Liabilities:				
Long-Term Liabilities	217,712	168,400	49,312	29.3 %
Other Noncurrent Liabilities	<u>24,007</u>	<u>24,127</u>	<u>(120)</u>	(0.5) %
Total Noncurrent Liabilities	<u>241,719</u>	<u>192,527</u>	<u>49,192</u>	25.6 %
Total Liabilities	<u>303,354</u>	<u>253,533</u>	<u>49,821</u>	19.7 %
Net Position				
Net Investment in Capital Assets	737,359	723,428	13,931	1.9 %
Restricted	76,747	58,766	17,981	30.6 %
Unrestricted	<u>211,148</u>	<u>209,155</u>	<u>1,993</u>	1.0 %
Total Net Position	<u>\$ 1,025,254</u>	<u>\$ 991,349</u>	<u>\$ 33,905</u>	3.4 %

The condensed statement above indicates a stronger financial position compared to last fiscal year with total assets increasing by \$83.7 million. This was only partially offset by an increase in total liabilities of \$49.8 million for a net increase of \$33.9 million in the University's total net position.

Capital assets (net of depreciation) increased by \$23.3 million and other noncurrent assets increased \$63.2 million from the previous fiscal year end. Capital assets will be discussed in detail in the capital assets section of this discussion and analysis. A substantial portion of the increase in noncurrent assets is for higher restricted cash and endowment investment balances at fiscal yearend. Noncurrent restricted cash balances were \$50.6 million more than at the previous June 30th. The increase in cash is largely accounted for by \$45.4 million of unspent funds received from the sale of bonds to finance the construction of a new student housing

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

facility. Endowment investments increased \$6.8 million and reflects \$1.9 million in new endowment monies and a more favorable market.

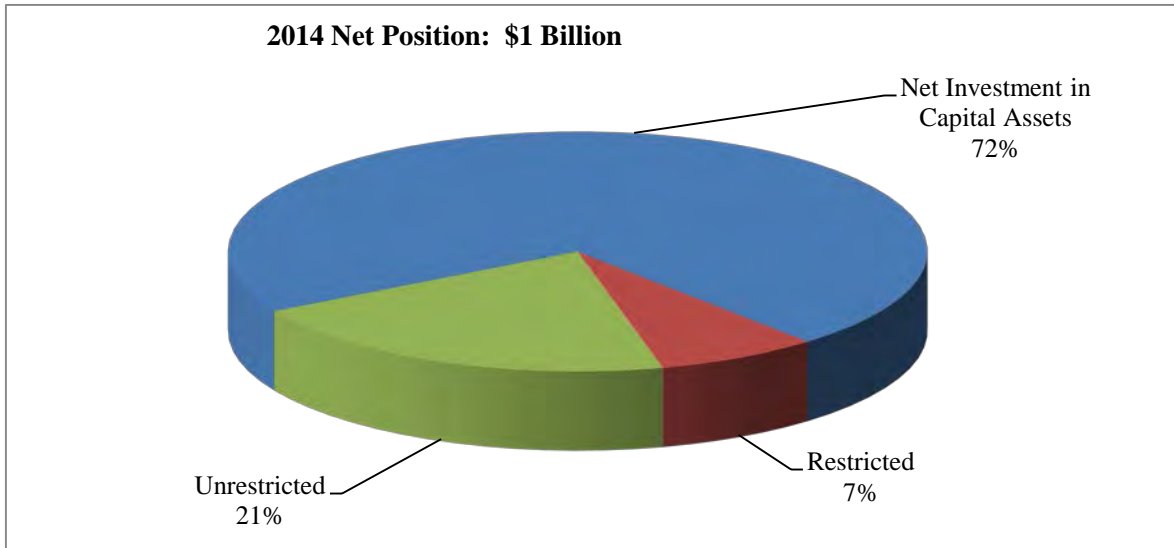
Noncurrent long-term liabilities increased by \$49.3 million, which is a 29.3 percent change from the prior year. The change is largely attributed to the net effect of the \$53.7 million raised through the sale of bonds for the new student housing facility and the \$4.1 premium on the sale less the \$10.6 million of scheduled payments made on bonds, certificates of participation and notes. The changes in long-term liabilities are described in greater detail in Note 7 to the financial statements.

The University's liquidity remains strong. The current ratio, defined as current assets divided by current liabilities, of 4.6 indicates that the University, if needed, could pay its current obligations nearly five times before current assets are exhausted. Working capital, defined as current assets less current liabilities, is \$222.9 million at June 30, 2014 and represents a \$3.3 million decrease or a 1.5 percent change from the prior year. The amount of available working capital is a measure of the University's ability to meet its short term obligations.

The University's net position is made up of three classifications: net investment in capital assets, restricted and unrestricted. The balance in each classification increased \$13.9, \$18 and \$2 million, respectively. The University's total net position at June 30, 2014 was \$1 billion, an increase of \$33.9 million, or 3.4 percent over the prior year. The net investment in capital assets encompasses the University's capital assets net of accumulated depreciation and the unspent principal balances of debt resulting from the acquisition, construction or improvement of those assets. The increase in net investment in capital assets resulted from the net effect of the \$23.3 million increase in capital assets, the net increase of \$46.3 million in capital debt and a \$38.1 million net increase in cash from unspent bond proceeds.

Restricted net position includes the University's permanent endowment fund and expendable funds subject to externally imposed restrictions governing their use. Restricted net assets increased from \$58.8 million to \$76.7 million, an increase of \$18 million or 30.6 percent. Approximately \$4.4 million of the increase was due to a favorable change in the fair market value of endowment investments. In addition, the restricted cash for the dance studio and fourth floor of the School of Dental Medicine capital projects, increased by \$11.8 million as a result of a carry forward of State Appropriations.

Although the unrestricted portion of the University's net position is not subject to externally imposed stipulations, substantially all of the unrestricted funds have been designated for various academic and research programs and initiatives, as well as capital projects. For fiscal year 2014, unrestricted net assets accounted for \$211.1 million of the \$1 billion in net assets, a 1 percent increase from the prior year. The following chart displays the contribution of each category to total net position for 2014.



Statement of Revenues, Expenses and Changes in Net Position

The Statement of Revenues, Expenses, and Changes in Net Position presents the revenues earned and expenses incurred during the fiscal year and provides information to evaluate the University’s management of operations and maintenance of financial strength. Activities are classified and reported as operating, nonoperating, or other. In general, operating revenues are generated by providing goods and services and operating expenses are incurred to acquire or produce the goods and services needed to fulfill the mission of the University. The University consistently shows an operational loss (operating revenues less operating expenses) because public universities are dependent on state appropriations, which is not included in operating revenues. State appropriations and certain noncapital grants and gifts are classified as nonoperating revenues because they are revenues received for which goods and services are not provided. When the nonoperating revenues, net of nonoperating expenses, are added to the operational loss, the University shows an increase in income before other revenues of \$11.6 million. Other revenues are neither operating nor nonoperating and include capital appropriations, capital grants and gifts and additions to endowments. The University shows a \$33.9 million increase in net position as of June 30, 2014 when these other revenues are added. The following table presents a summarized comparison of the statements as of June 30, 2014 and June 30, 2013.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

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

(Dollars in Thousands)

	2014	2013 (Restated)	Increase/ (Decrease)	Percent Change
Operating Revenues				
Student Tuition and Fees, Net	\$ 169,675	\$ 162,272	\$ 7,403	4.6 %
Patient Services, Net	207,316	178,590	28,726	16.1 %
Grants and Contracts	37,173	40,675	(3,502)	(8.6) %
Sales and Services, Net	85,430	80,954	4,476	5.5 %
Other	1,226	1,147	79	6.9 %
Total Operating Revenues	500,820	463,638	37,182	8.0 %
Operating Expenses				
Salaries and Benefits	540,914	524,631	16,283	3.1 %
Supplies and Materials	81,700	79,651	2,049	2.6 %
Services	111,891	97,177	14,714	15.1 %
Scholarships and Fellowships	39,879	38,568	1,311	3.4 %
Utilities	19,522	18,778	744	4.0 %
Depreciation/Amortization	25,939	24,546	1,393	5.7 %
Other Operating Expenses	422	314	108	34.4 %
Total Operating Expenses	820,267	783,665	36,602	4.7 %
Operating Loss	(319,447)	(320,027)	580	(0.2) %
Nonoperating Revenues (Expenses)				
State Appropriations	275,658	285,530	(9,872)	(3.5) %
Noncapital Grants and Gifts	61,066	57,237	3,829	6.7 %
Other Nonoperating Expenses	(5,723)	(6,162)	439	(7.1) %
Net Nonoperating Revenues	331,001	336,605	(5,604)	(1.7) %
Income Before Other Revenues	11,554	16,578	(5,024)	(30.3) %
Capital Appropriations	6,260	1,065	5,195	487.8 %
Capital Grants and Gifts	14,192	23,925	(9,733)	(40.7) %
Additions to Endowments	1,899	1,335	564	42.2 %
Increase in Net Position	33,905	42,903	(8,998)	(21.0) %
Net Position-July 1	991,349	948,446	42,903	4.5 %
Net Position-June 30	\$ 1,025,254	\$ 991,349	\$ 33,905	3.4 %

Fiscal year 2013-2014 total revenues are \$868,194 and total expenses are \$834,289.

Fiscal year 2012-2013 total revenues are \$838,902 and total expenses are \$795,999.

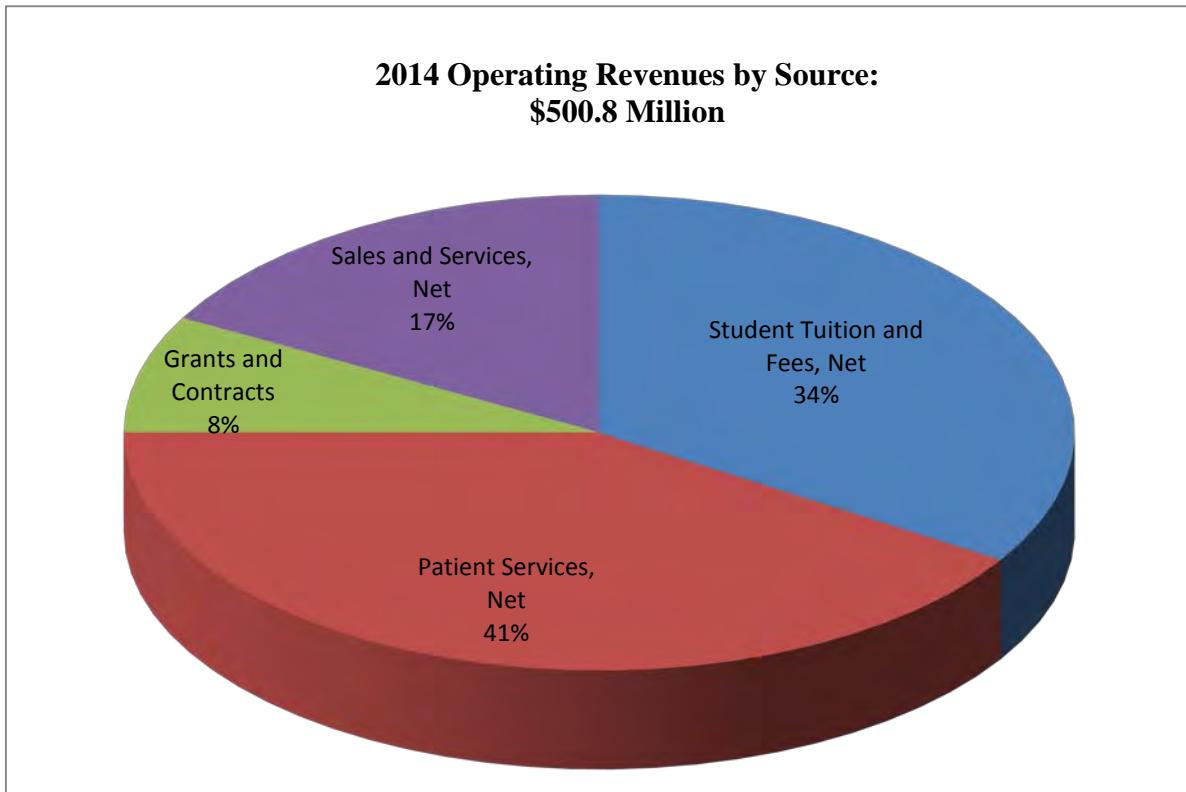
Operating revenues are generated by providing goods and services related to instruction, research, and public service missions. The most significant change in operating revenues is the increase in patient services revenues, net of the allowance for uncollectible accounts and

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

indigent care and contractual adjustments. Patient services, net increased \$28.7 million, or 16.1 percent. The increase is due to a number of factors including:

- new revenues generated after purchasing East Carolina Neurology, Inc. on July 31, 2013,
- an increase in pharmacy sales in neurology and hemophilia,
- an increase in Medicaid payments received and accrued,
- an increase in payments received from Vidant Medical Center for graduate medical education (GME) per contract and for new programs,
- an increase in contract revenues received after improving and strengthening billing efforts, and
- the growth in dental revenues as more dental learning service centers have been established across the State.

The following chart shows each component of operating revenues as it relates to total operating revenues as a whole:



Operating expenses are the day-to-day expenses incurred to carry out the mission of the University. Operating expenses are reported by natural classification. Amounts changed at varying rates with an overall increase of \$36.6 million, or 4.7 percent. Salaries and benefits

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

increased \$16.3 million, or 3.1 percent, in 2014. Approximately \$4.9 million of the increase is for salaries in the new neurology practice. Additional staffing was also hired for the new dental community service learning centers. Salaries relating to the dental program increased approximately \$3 million. Services increased \$14.7 million, or 15.1 percent. Some of the major causes of the increase include: a \$2.2 million increase in contracted costs for food services due to an increase in the number of students on meal plans, a \$2.6 million increase in contractual services largely due to the implementation of an electronic health record system and new medical contracts, a \$1 million increase in information technology costs due to the implementation of the electronic health record system and a patient portal, a \$1.4 million increase in student housing costs for renting apartments because the Belk dorm was closed, a \$.8 million increase in rent for commercial space such as for a new neurology practice and a \$1.4 million payment for withdrawing from Conference USA. The following chart shows each component of operating expenses as it relates to total operating expenses as a whole and the consistency between the two years.

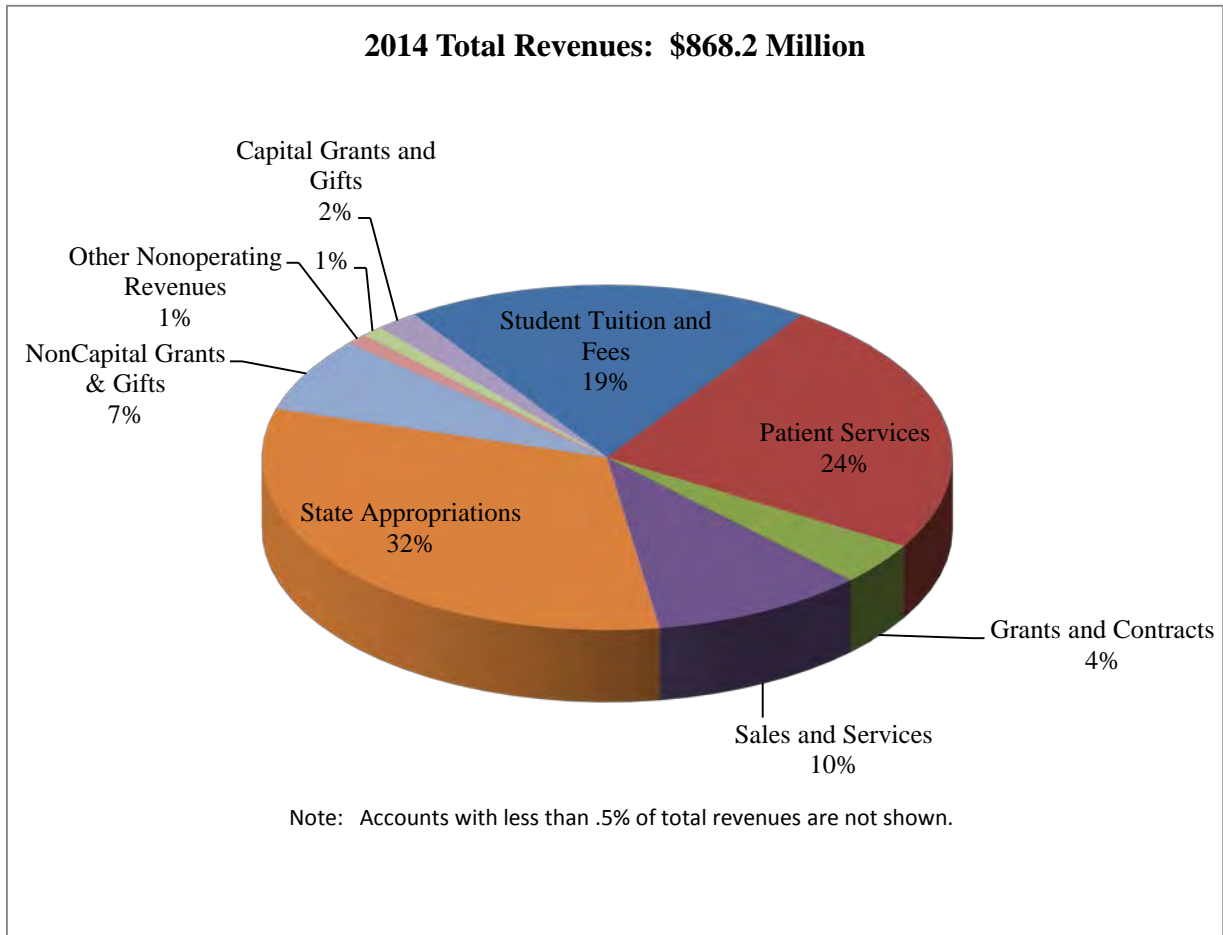
2014 OPERATING EXPENSES: \$820.3 Million		
	% to Total 2014	% to Total 2013
Salaries and Benefits	66%	67%
Supplies and Materials	10%	10%
Services	14%	13%
Scholarships and Fellowships	5%	5%
Utilities	2%	2%
Depreciation / Amortization	3%	3%
	100%	100%

Nonoperating revenues and expenses are not generated by the principal operations of the University. Total net nonoperating revenues decreased by \$5.6 million or 1.7 percent from the prior year. The most significant decrease occurred in state appropriations which decreased \$9.9 million, or 3.5 percent as a result of ongoing state budget cuts. This was partially offset by an increase in noncapital grants and gifts, primarily for a \$2.4 million increase in funds for Pell grants and a \$2.2 million gift from the Pirate Club.

The most significant change in other revenues occurred in capital grants and gifts which decreased \$9.7 million, or 40.7 percent from the prior year. The decrease is attributed to reduced capital grant funding received from the state as various, large construction projects were completed in 2013 including the UNC Coastal Studies Institute, the School of Dental Medicine in Greenville and the School of Dental Medicine in Elizabeth City. The University received \$6.3 million in capital appropriations from the state in 2014 for various repair and renovation projects an increase from the \$1.1 million in capital appropriations received in 2013.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

The following chart illustrates the University's total revenues by source (operating, nonoperating and other revenues) which total \$868.2 million for fiscal year-end 2014.



Capital Assets

Capital assets for the University are comprised of non-depreciable and depreciable assets. Non-depreciable assets include land, construction in progress and computer software in development. Depreciable assets include buildings, machinery and equipment, general infrastructure and computer software. Buildings which have been completed or that are construction in progress comprise 77.6 percent of the University's capital assets.

A vital aspect for enhancing and maintaining the quality of the University's academic, research, and service programs and its residential life is the acquisition, construction and improvement of its capital assets. The University continues to implement its long-range plan to modernize its complement of older teaching and research facilities, balanced with new construction.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

Capital assets at June 30, 2014 and June 30, 2013, were as follows:

Capital Assets

(Dollars in Thousands)

	<u>2014</u>	<u>2013</u>	<u>Increase/ (Decrease)</u>	<u>Percent Change</u>
Land	\$ 46,002	\$ 44,520	\$ 1,482	3.3 %
Construction in Progress	31,130	29,875	1,255	4.2 %
Computer Software in Development	673	967	(294)	(30.4) %
Buildings	872,965	837,475	35,490	4.2 %
General Infrastructure	101,162	100,574	588	0.6 %
Machinery and Equipment	131,693	126,771	4,922	3.9 %
Computer Software	13,893	13,925	(32)	(0.2) %
Total Capital Assets	1,197,518	1,154,107	43,411	3.8 %
Accumulated Depreciation	299,476	279,335	20,141	7.2 %
Capital Assets, Net	\$ 898,042	\$ 874,772	\$ 23,270	2.7 %

Capital additions consist primarily of replacement, renovation and new construction of capital assets as well as significant investments in equipment, including information technology. The University had \$898 million in capital assets at fiscal year-end 2014 which is a net increase of \$23.3 million from the prior year.

Several major construction projects were completed in fiscal year 2014 and the costs were removed from construction in progress and added to buildings. These include the Auxiliary Gym Expansion, the fourth floor of the East Carolina Hearth Institute (ECHI), the renovation of White Hall dormitory, and the Schools of Dental Medicine in Sylva and in Lillington. The increase in buildings and equipment resulted in a corresponding increase in accumulated depreciation.

The University and the State Construction Office accepted completion of the Auxiliary Gym on August 29, 2013. The Auxiliary Gym project included the construction of a 46,000 square foot practice facility that adjoins the current Minges Coliseum. The facility provides two practice courts, offices, video review rooms, lockers, equipment storage and training facilities. Additionally, the project included renovations to current facilities such as new elevators and HVAC upgrades. When the ECHI was built, the fourth floor was left as 37,800 square feet of floor shell space. This space was up-fitted into an open wet laboratory for interdisciplinary research as well as cardiovascular robotics surgical training and houses the Robotic Surgery Center and the Diabetes and Obesity Institute. Major renovations were made to the White Hall dormitory including adding drywall, removing built-in furniture, re-finishing all bedroom walls, removing and replacing carpet, and adding fire-proof steel. The School of Dental Medicine opened its third and fourth community service learning centers in Lillington and Sylva, respectively. These dental clinics provide training for post-graduate dentists in residency programs and fourth-year dental students, comprehensive services in underserved areas and poor counties in North Carolina and economic development for rural areas of North Carolina.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

Outstanding commitments on construction projects increased significantly, \$35 million, from \$20.8 million at yearend 2013 to \$55.8 million at yearend 2014 and is primarily due to large commitments on the Belk Residence Hall demolition and replacement project which was later renamed Gateway East and Gateway West. Significant construction projects that are in progress at the end of fiscal year 2014 include this project, two student unions, and community service learning centers in Spruce Pine, Lumberton, and Davidson and Brunswick counties. The Spruce Pine, Lumberton and Davidson county clinics are now operational and accepting patients.

The Belk Residency Hall demolition and replacement project and construction of Gateway East and Gateway West is funded from housing receipts and has been approved at a project cost of \$56 million. The Belk Residence Hall has been raised and is being replaced with two residential housing wings and community center and pool for use by students. This building will have modern campus living facilities and approximately 205,000 square feet.

The New Student Union, Parking Structure and Health Sciences Campus Student Services Building project was recently approved by the Legislature at a project cost of \$156.3 million. Permanent financing has not yet been approved. The project will be funded from an increase in student fees and from campus sources including dining, Dowdy Student Stores, Ledonia Wright Cultural Center, parking, student health and student recreation. Plans call for the new student union on main campus to cover 210,000 square feet. The facility will provide a new home for the Ledonia Wright Cultural Center, a 250-seat multi-purpose auditorium, office space for student government and student groups, multi-venue dining facilities, retail and service points, and a dividable ballroom. The project includes a 700-car parking deck to the west of the current student center. The University plans to begin construction on the health sciences campus student services facility first. It will be a 68,000 square-foot building housing a recreation and wellness center, student health services, student organizations, multipurpose spaces, a career center, meeting rooms, a lounge, a convenience store and a food court. It will be located between the ECHI and the Laupus Library.

In order to continue to provide quality educational experiences, it is imperative the University maintains a constant level of growth in regards to capital assets. A plan of this nature will assist the University in avoiding obsolescence and will also provide a marketing tool for attracting more students to the school. The University currently maintains a list of planned projects for the coming years. These projects are awaiting external review, approval and funding by the North Carolina Legislature or the approval for the University to proceed by issuing debt to construct the projects. The projects consist of a mix of new construction, repairs and renovations and infrastructure upgrades.

More detailed information on the University's capital assets is presented in Note 5 to the financial statements.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

Debt

The University uses revenue bonds, certificates of participation, notes payable and capital leases to finance construction projects and purchase equipment. As reflected in the following chart, total debt increased by \$46.3 million in 2014.

Debt Summary

Dollars in Thousands

	2014	2013 (Restated)	Increase/ (Decrease)
Revenue Bonds Payable	\$ 187,415	\$ 140,965	\$ 46,450
Bond Discounts/Charges	7,392	4,037	3,355
Certificates of Participation	0	1,095	(1,095)
Capital Leases Payable	220	350	(130)
Notes Payable	11,322	13,603	(2,281)
Total Debt	\$ 206,349	\$ 160,050	\$ 46,299

On February 13, 2014 the University issued \$53.7 million in Series 2014A tax-exempt General Revenue Bonds. The bonds were issued to provide funds for the demolition of the Belk Residency Hall and the construction of Gateway East and Gateway West. The \$46.3 million increase in debt is the net result of the addition of this new debt less the scheduled bond payments made by the University.

In January 2014, Moody's assigned a rating of Aa2 and Standard & Poor's assigned a rating of AA- to the Series 2014A General Revenue bonds. At the same time, these rating agencies affirmed the same ratings (Moody's – Aa2 and Standard & Poor's – AA-) on the various other debt issued for the University.

See Notes 7 and 8 to the financial statements for additional information on debt administration.

Economic and Strategic Outlook

The University's financial position remains strong and total net position grew by \$33.9 million due to effective institutional planning and continued support from the State to meet educational needs. During the recent legislative session, State budget cuts were again necessary to balance the budget for fiscal year 2015 and the UNC System divided legislatively imposed budget cuts with the 16 universities in the System. The University's share of this budget cut is \$3.3 million in State appropriations. The University did receive a small increase of \$.3 million to fund enrollment growth and \$3.2 million to fund increases in salaries and benefits. The Legislature approved tuition increases on 14 campuses, including a 6% increase at the University, but reduced appropriations by the amount estimated to be generated by the tuition increases. The University's amount of reduced appropriations is \$2.8 million. In addition the Legislature has asked the UNC Board of Governors to consider reducing state funds for centers and institutions, speaker series, and other nonacademic

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

activities in an amount up to \$15 million. Any savings realized from the reductions could be used to match private gifts for the Distinguished Professors Endowment Trust Fund or implement provisions of UNC's Strategic Plan. The University's share of this cut, if any, is unknown at this time.

The University is prepared for these budget cuts and recognizes that fiscal pressure, appropriations reductions, and reallocation actions are likely to continue for many years to come. The University Committee on Fiscal Sustainability examined the long-term fiscal well-being of the University and made recommendations in its May 1, 2014 report to improve the institution's ability to cope with mounting financial pressures in the short and longer term. Nine task force committees have been formed to focus on these recommendations in areas such as marketing and communications, enrollment management, reduction and/or consolidation of departments and colleges and Foundations curriculum. The University continues to work with the Board of Governors and the NC Legislators on more favorable legislation.

The University has a vibrant and expanding School of Dental Medicine that continues to spread its reach across the state. In addition to the dental clinic in Greenville and the four community service learning centers already opened, the University plans to open three new service learning centers in the current fiscal year in Spruce Pine, Davidson County and Lumberton. An additional service learning center is planned for opening in the following year in Brunswick County.

ECU Physicians (ECUP) is the clinical practice plan of the University's Brody School of Medicine within the Health Sciences Division. In its 2013 Session, the North Carolina General Assembly enacted legislation that eliminated both State medical schools (ECU and UNC) from receiving payments through the Setoff Debt Collection Act (SODCA). The SODCA allows ECUP and other state agencies to garnish NC tax return refunds and lottery winnings on patients with delinquent accounts.

ECUP management estimates the lost SODCA revenues for FY 2014 to be approximately \$6.4 million. By June 30, 2014, the North Carolina General Assembly had not enacted any modifications to the legislation enacted in 2013 that disqualified ECUP from receiving SODCA revenues. However, before adjourning in August 2014, the General Assembly modified the 2013 legislation to allow ECUP to submit patients, with some form of insurance (either private or public) and who have an outstanding balance due to ECUP, through the SODCA process. While this is a very positive development, management has not yet been able to estimate the amount of SODCA revenues that will be regained as a result of this legislative action.

The Upper Payment Limit (UPL) is a federally funded program which provides additional payments to public medical schools for services provided to Medicaid patients. The additional payments enable the public medical schools to receive payments for Medicaid services that are close to what would have been paid by commercial insurance carriers for the same services.

MANAGEMENT DISCUSSION AND ANALYSIS (CONCLUDED)

The North Carolina General Assembly enacted legislation in its 2013 session restricting future UPL payments by limiting the number of physicians to those physicians employed by ECUP as of May 22, 2013. This statutory restriction prevents services from any physicians employed after May 22, 2013 from receiving UPL payments. As of June 30, 2014, the North Carolina General Assembly had not enacted any modifications to this 2013 legislation. Fortunately, before adjourning the 2014 Session, the General Assembly modified this legislation and state law now allows ECUP eligible medical providers to be capped at 418, which will allow a slight increase in the number of eligible providers. This effectively removes the threatened reduction in UPL revenues resulting from the 2013 legislation.

The North Carolina Department of Health and Human Services (NCDHHS) launched NCTracks, a new multi-payer Medicaid Management Information System in July 2013. NCTracks is the system used to reimburse health care providers for services provided to North Carolina Medicaid beneficiaries. The implementation of NCTracks encountered multiple problems resulting in reimbursement delays from Medicaid to health care providers, including ECUP. The reimbursement delays impacts ECUP on two different levels. The first level is the payment from NC Medicaid for services rendered to Medicaid patients. At Fiscal Year 2014 year-end, delayed revenues from Medicaid were estimated to be \$300,000. The second level is the delay in payments from Medicaid created delays in submitting requests for reimbursement through the UPL mechanism. The estimated delayed reimbursement related to UPL payments is \$3 million. The total fiscal year impact to ECU Physicians related to the NCTracks implementation problems is \$3.3 million. It is unknown how long these delays will continue.

Contacting the University's Financial Management

This financial report is designed to provide our citizens, investors and creditors with a general overview of the University's finances and show accountability for all funds received. If you have any questions or need additional financial information, please contact the Financial Director for East Carolina University, at (252)737-1140.

East Carolina University
Statement of Net Position
June 30, 2014

Exhibit A-1

Page 1 of 2

ASSETS

Current Assets:

Cash and Cash Equivalents	\$ 193,658,604.81
Restricted Cash and Cash Equivalents	23,038,928.88
Receivables, Net (Note 4)	56,772,793.90
Due from State of North Carolina Component Units	1,430,000.00
Due from University Component Units	22,451.12
Inventories	5,302,016.91
Notes Receivable, Net (Note 4)	1,075,814.25
Prepaid Assets	3,255,053.02
	<hr/>
Total Current Assets	284,555,662.89

Noncurrent Assets:

Restricted Cash and Cash Equivalents	76,567,121.43
Receivables (Note 4)	3,834,432.24
Endowment Investments	45,087,380.19
Restricted Investments	1,604,615.45
Investment in Joint Ventures	6,011,328.84
Prepaid Assets	3,142,875.34
Notes Receivable, Net (Note 4)	9,762,199.88
Capital Assets - Nondepreciable (Note 5)	77,805,560.30
Capital Assets - Depreciable, Net (Note 5)	820,236,555.64
	<hr/>
Total Noncurrent Assets	1,044,052,069.31

Total Assets	<hr/> <hr/> 1,328,607,732.20
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DEFERRED OUTFLOWS OF RESOURCES

Total Deferred Outflows of Resources	<hr/> 0.00
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LIABILITIES

Current Liabilities:

Accounts Payable and Accrued Liabilities (Note 6)	31,590,847.17
Due to Primary Government	146,689.63
Deposits Payable	1,603,966.57
Funds Held for Others	2,382.80
Unearned Revenue	15,557,505.83
Interest Payable	2,067,397.85
Long-Term Liabilities - Current Portion (Note 7)	10,666,168.04
	<hr/>
Total Current Liabilities	61,634,957.89

Noncurrent Liabilities:

Funds Held for Others	12,068,675.84
U. S. Government Grants Refundable	11,937,966.59
Long-Term Liabilities, Net (Note 7)	217,711,867.11
	<hr/>
Total Noncurrent Liabilities	241,718,509.54

Total Liabilities	<hr/> <hr/> 303,353,467.43
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DEFERRED INFLOWS OF RESOURCES

Total Deferred Inflows of Resources	<hr/> 0.00
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***East Carolina University
Statement of Net Position
June 30, 2014***

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

NET POSITION

Net Investment in Capital Assets	737,358,761.58
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	2,113,216.54
Endowed Professorships	25,768,803.44
Departmental Uses	340,577.27
Loans	1,811,933.67
Expendable:	
Scholarships and Fellowships	5,133,328.13
Endowed Professorships	11,307,527.98
Departmental Uses	748,227.20
Capital Projects	15,600,145.03
Debt Service	12,702,880.95
Other	1,220,662.80
Unrestricted	<u>211,148,200.18</u>
Total Net Position	<u>\$ 1,025,254,264.77</u>

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

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

Exhibit A-2

REVENUES

Operating Revenues:

Student Tuition and Fees, Net (Note 9)	\$ 169,674,857.73
Patient Services, Net (Note 9)	207,315,507.43
Federal Grants and Contracts	17,153,147.88
State and Local Grants and Contracts	9,637,695.65
Nongovernmental Grants and Contracts	10,381,657.91
Sales and Services, Net (Note 9)	85,429,758.23
Interest Earnings on Loans	43,979.42
Other Operating Revenues	<u>1,183,072.61</u>
Total Operating Revenues	<u>500,819,676.86</u>

EXPENSES

Operating Expenses:

Salaries and Benefits	540,913,584.64
Supplies and Materials	81,700,203.44
Services	111,890,618.62
Scholarships and Fellowships	39,879,568.01
Utilities	19,521,918.20
Depreciation/ Amortization	25,938,597.18
Other Operating Expenses	<u>422,279.26</u>
Total Operating Expenses	<u>820,266,769.35</u>
Operating Loss	<u>(319,447,092.49)</u>

NONOPERATING REVENUES (EXPENSES)

State Appropriations	275,657,636.25
Noncapital Grants - Federal Student Financial Aid	32,712,147.24
Noncapital Grants	15,959,715.00
Noncapital Gifts	12,393,677.44
Investment Income (Net of Investment Expense of \$41,805.10)	7,846,065.67
Interest and Fees on Debt	(7,389,019.92)
Federal Interest Subsidy on Debt	454,147.17
Other Nonoperating Expenses	<u>(6,633,424.56)</u>
Net Nonoperating Revenues	<u>331,000,944.29</u>
Income Before Other Revenues	11,553,851.80
Capital Appropriations	6,259,834.00
Capital Grants	11,546,636.26
Capital Gift	2,645,632.10
Additions to Endowments	<u>1,899,558.44</u>
Increase in Net Position	33,905,512.60

NET POSITION

Net Position - July 1, 2013, as Restated (Note 18)	<u>991,348,752.17</u>
Net Position - June 30, 2014	<u>\$ 1,025,254,264.77</u>

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

East Carolina University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2014

Exhibit A-3
Page 1 of 2

CASH FLOWS FROM OPERATING ACTIVITIES

Received from Customers	\$ 480,634,404.94
Payments to Employees and Fringe Benefits	(540,230,326.89)
Payments to Vendors and Suppliers	(210,104,278.96)
Payments for Scholarships and Fellowships	(39,879,568.01)
Loans Issued	(2,117,335.00)
Collection of Loans	1,680,906.41
Interest Earned on Loans	1,420.57
Student Deposits Received	1,644,879.77
Student Deposits Returned	(1,857,375.31)
Other Payments	(6,034,329.34)
	<hr/>
Net Cash Used by Operating Activities	(316,261,601.82)

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

State Appropriations	275,657,636.25
Noncapital Grants - Federal Student Financial Aid	32,253,654.12
Noncapital Grants	15,934,832.29
Noncapital Gifts	12,393,677.44
Additions to Endowments	1,899,558.44
William D. Ford Direct Lending Receipts	147,965,254.90
William D. Ford Direct Lending Disbursements	(147,667,050.00)
Related Activity Agency Receipts	21,467,239.50
Related Activity Agency Disbursements	(20,976,231.36)
	<hr/>
Net Cash Provided by Noncapital Financing Activities	338,928,571.58

CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES

Proceeds from Capital Debt	57,303,070.70
Capital Appropriations	6,259,834.00
Capital Grants	11,546,636.26
Capital Gifts	1,927,972.88
Acquisition and Construction of Capital Assets	(53,339,402.00)
Principal Paid on Capital Debt and Leases	(10,741,520.02)
Interest and Fees Paid on Capital Debt and Leases	(6,945,445.72)
Federal Interest Subsidy on Debt Received	452,304.54
Other Payments	(249,979.39)
	<hr/>
Net Cash Provided by Capital Financing and Related Financing Activities	6,213,471.25

CASH FLOWS FROM INVESTING ACTIVITIES

Proceeds from Sales and Maturities of Investments	2,753,809.04
Investment Income	3,460,228.95
Investment in Joint Ventures	(3,511,500.00)
Purchase of Investments and Related Fees	(5,186,018.32)
	<hr/>
Net Cash Used by Investing Activities	(2,483,480.33)

Net Increase in Cash and Cash Equivalents	26,396,960.68
Cash and Cash Equivalents - July 1, 2013	266,867,694.44
	<hr/>
Cash and Cash Equivalents - June 30, 2014	\$ 293,264,655.12

East Carolina University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2014

Exhibit A-3
Page 2 of 2

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

Operating Loss	\$ (319,447,092.49)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:	
Depreciation/ Amortization Expense	25,938,597.18
Allowances and Write-offs	861,012.63
Nonoperating Other Expenses	(960,594.74)
Changes in Assets and Liabilities:	
Receivables, Net	(21,437,511.55)
Due from State of North Carolina Component Units	(1,250,305.00)
Due from University Component Units	(4,093.94)
Inventories	(429,100.80)
Prepaid Assets	(4,604,265.96)
Notes Receivable, Net	(436,428.59)
Accounts Payable and Accrued Liabilities	2,666,717.79
Due to Primary Government	71,427.45
Unearned Revenue	2,503,965.20
Compensated Absences	478,566.54
Deposits Payable	(212,495.54)
	<hr/>
Net Cash Used by Operating Activities	<u>\$ (316,261,601.82)</u>

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:	
Cash and Cash Equivalents	\$ 193,658,604.81
Restricted Cash and Cash Equivalents	23,038,928.88
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	76,567,121.43
	<hr/>
Total Cash and Cash Equivalents - June 30, 2014	<u>\$ 293,264,655.12</u>

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Assets Acquired through a Gift	\$ 717,659.22
Change in Fair Value of Investments	4,385,836.73
Loss on Investment in Joint Ventures	(3,573,196.00)
Loss on Disposal of Capital Assets	(1,861,367.61)
Bond Issuance Cost Withheld	(174,483.60)
Amortization of Bond Premiums/Discounts	438,571.39

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

East Carolina University Foundation, Inc. and Consolidated Affiliates
Consolidate Statement of Financial Position
June 30, 2014

Exhibit B-1

ASSETS

CURRENT ASSETS

Cash and Cash Equivalents	\$ 4,562,233
Current portion of unconditional promises to give, net	578,801
Prepaid Expenses	34,066
Other Receivables	146,825
	<hr/>
Total Current Assets	5,321,925

INVESTMENTS

Investments	100,578,586
Real Estate Held for Investment	931,449
	<hr/>
Total Investments	101,510,035

CAPITAL ASSETS

Capital Assets, net	<hr/> 7,878,073
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OTHER ASSETS

Life Insurance Policy - Cash Surrender Value	204,795
Student Loans	38,819
Beneficial Interest in Charitable Remainder Trusts	3,240,105
Assets Held in Charitable Remainder Trusts and Annuities	1,500,173
Investment in Joint Venture	1,958,608
Unconditional promises to give, less current portion, net	2,614,512
Other Assets	77,320
	<hr/>
Total Other Assets	9,634,332

TOTAL ASSETS

\$ 124,344,365.00

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES

Accounts Payable	\$ 79,546
Line of Credit	667,425
Accrued Expenses	53,129
Current Portion of Note Payable	307,143
Current Portion of Charitable Gift Annuities Payable	112,047
Agency Payables	682,741
	<hr/>
Total Current Liabilities	1,902,031

LONG-TERM LIABILITIES

Refundable Advances	26,430
Note Payable, Less Current Portion	7,203,938
Interest Rate Swap Agreement	164,287
Charitable Gift Annuities Payable, Less Current Portion	605,203
Liabilities Under Charitable Remainder Trusts	410,221
	<hr/>
Total Long-Term Liabilities	8,410,079
	<hr/>
Total Liabilities	10,312,110

NET ASSETS

Unrestricted	14,632,475
Temporarily Restricted	46,382,707
Permanently Restricted	53,017,073
	<hr/>
Total Net Assets	114,032,255

TOTAL LIABILITIES AND NET ASSETS

\$ 124,344,365

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

***East Carolina University Foundation, Inc. and Consolidated Affiliates
Consolidated Statements of Activities and Changes in Net Assets
For the Fiscal Year Ended June 30, 2014***

Exhibit B-2

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUES, GAINS AND OTHER SUPPORT				
Contributions	\$ 426,814	\$ 5,448,861	\$ 1,669,795	\$ 7,545,470
Gifts in Kind	1,283	83,238		84,521
Contributed Services and Facilities	1,973,332			1,973,332
Return on Investments				
Interest and Dividends	787,700	2,383,942		3,171,642
Net Unrealized and Realized Gains on Investments	2,082,682	9,883,098		11,965,780
Other Income	1,066,640	145,908	14,531	1,227,079
Net loss on sales or transfer of property	(166,712)	6,250	77,685	(82,777)
Revaluation of real estate	(7,610)			(7,610)
Change in Value of Split Interest Agreements		2,490	(816,514)	(814,024)
Net Assets Released from Restrictions	6,067,032	(6,067,032)		
Total Revenues, Gains and Other Support	12,231,161	11,886,755	945,497	25,063,413
EXPENSES AND LOSSES				
Program Services				
Program Development	3,726,753			3,726,753
Scholarships	2,381,861			2,381,861
Total Program Services	6,108,614			6,108,614
General and Administrative	755,312			755,312
Fund Raising	2,081,104			2,081,104
Total Operating Expenses	8,945,030			8,945,030
Bad Debt Losses	100	42,945	18,800	61,845
Total Expenses and Losses	8,945,130	42,945	18,800	9,006,875
Changes in Net Assets	3,286,031	11,843,810	926,697	16,056,538
NET ASSETS				
Net Assets at Beginning of Year	11,404,507	35,210,815	51,360,395	97,975,717
Reclassification of net assets, donor stipulations	(58,063)	(671,918)	729,981	
Net Assets at End of Year	\$ 14,632,475	\$ 46,382,707	\$ 53,017,073	\$ 114,032,255

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

EAST CAROLINA UNIVERSITY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2014

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

- A. Financial Reporting Entity** - The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America (GAAP), the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government serves as a nucleus for a reporting entity when it issues separate financial statements. East Carolina 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 unit is discretely presented in the University's financial statements. See below for further discussion of the University's component unit.

Discretely Presented Component Unit – The East Carolina Foundation, Inc. (Foundation) is a legally separate nonprofit corporation and is reported as a discretely presented component unit based on the nature and significance of its relationship to the University. The East Carolina University Real Estate Foundation, Inc. and Green Town Properties, Inc. are the consolidated affiliates of the Foundation.

The Foundation is a tax-exempt component unit of the University. The Foundation acts primarily as a fund-raising organization to supplement the resources that are available to the University in support of its programs. The Foundation board consists of 63 members. Although the University does not control the timing or amount of receipts from the Foundation, the majority of resources, or income thereon, that the Foundation holds and invests are restricted to the activities of the University by the donors. Because these restricted resources held by the Foundation can only be used by, or for the benefit of the University, the Foundation is considered a component unit of the University and is reported in separate financial statements because of the difference in its reporting model, as described below.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The Foundation is a private nonprofit organization that reports its financial results under the Financial Accounting Standards Board (FASB) Codification. As such, certain revenue recognition criteria and presentation features are different from the Governmental Accounting Standards Board (GASB) revenue recognition criteria and presentation features. No modifications have been made to the Foundation's financial information in the University's financial reporting entity for these differences.

During the year ended June 30, 2014, the Foundation distributed \$6,108,614 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from the University Financial Services Office, 3800 East Tenth Street, Second Floor, Greenville, NC 27858, or by calling (252) 737-1133.

- 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, and deposits held by the State Treasurer in the Short-Term Investment Fund (STIF). The STIF maintained by the State Treasurer has the general

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.

- E. Investments** - Investments generally are reported at fair value. The fair values of all debt and equity securities with readily determinable fair market values are based on quoted market prices. Investments for which a readily determinable fair value does not exist include investments in certain commingled funds, hedge funds, and limited partnerships. These investments are carried at estimated fair value provided by the respective investment fund managers or third party administrators. ECU management, through our investment consultant, reviews and evaluates the values provided by the fund managers, as well as the valuation methods and assumptions used in determining the fair value of such investments. Those estimated fair values may differ significantly from the values that would have been used had a ready market for these investments existed. The net increase or decrease in the fair value of investments is recognized as a component of investment income. The majority of limited partnerships and hedge funds are subject to fair value estimation, which includes discounted cash flow and transaction comparison. The fair value for investments in the UNC Investment Fund is based on amounts reported to the University by UNC Management Company, Inc.

Money market funds not held by a governmental investment pool are reported at cost, if purchased, or at fair value or appraised value at date of gift, if donated.

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.

- F. Receivables** - Receivables consist of tuition and fees charged to students, charges for services rendered to patients, 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, are valued at cost using either first-in, first-out method. Merchandise for resale is valued at the lower of cost or market using the retail inventory method.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

The University capitalizes assets that have a value or cost 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 method over the estimated useful lives of the assets, generally 25 to 75 years for general infrastructure, 30 to 75 years for buildings, 5 to 50 years for equipment, and 5 to 20 years for computer software.

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

Revenue bonds payable are reported net of unamortized premiums or discounts. The University amortizes bond premiums/discounts over the life of the bonds using the straight-line. Deferred charges on refundings are amortized over the life of the old debt or new debt (whichever is shorter) using the straight-line method, and are included as Deferred Outflows or Deferred Inflows of Resources on the Statement of Net Position. Issuance costs are expensed.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

- K. 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.

- L. Net Position** - The University's net position is classified as follows:

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

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

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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 inflows and outflows of resources.

- M. 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.
- N. 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 and state appropriations that represent subsidies or gifts to the University, as

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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.

- O. 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, printing and graphics, motor pool, postal services and telecommunications. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

NOTE 2 - DEPOSITS AND INVESTMENTS

- A. Deposits** - Unless specifically exempt, the University is required by *North Carolina General Statute 147-77* to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. However, the University of North Carolina Board of Governors, pursuant to G.S. 116-36.1, may authorize the University to deposit its institutional trust funds in interest-bearing accounts and other investments authorized by the Board of Governors, without regard to any statute or rule of law relating to the investment of funds by fiduciaries. Although specifically exempted, the University may voluntarily deposit institutional trust funds, endowment funds, special funds, revenue bond proceeds, debt service funds, and funds received for services rendered by health care professionals with the State Treasurer. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

At June 30, 2014, the amount shown on the Statement of Net Position as cash and cash equivalents includes \$293,055,159.29 which represents the University's equity position in the State Treasurer's STIF. The STIF (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.3 years as of June 30, 2014. Assets and shares of the STIF are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's STIF) are included in the State of

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

Cash on hand at June 30, 2014 was \$114,376.72. The carrying amount of the University's deposits not with the State Treasurer was \$95,119.11 and the bank balance was \$209,209.55. Custodial credit risk is the risk that in the event of a bank failure, the University's deposits may not be returned to it. The University does not have a deposit policy for custodial credit risk. As of June 30, 2014, the University's was not exposed to custodial credit risk.

B. Investments

University - The University is authorized by The University of North Carolina Board of Governors pursuant to G.S. 116-36.2 and Section 600.2.4 of the Policy Manual of the University of North Carolina to invest its special funds and funds received for services rendered by health care professionals in the same manner as the State Treasurer is required to invest, as discussed below.

G.S. 147-69.1(c), applicable to the State's General Fund, and G.S. 147-69.2, applicable to institutional trust funds, authorize the State Treasurer to invest in 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Investments of the University's component unit, the East Carolina University Foundation, Inc. and Consolidated Affiliates, 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.

UNC Investment Fund, LLC - At June 30, 2014, the University's investments include \$896,473.63 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. Asset and ownership interests of the UNC Investment Fund are determined on a market unit valuation basis each month. 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.

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's Endowment Board has a formal investment policy that addresses interest rate risk. The policy states that fixed income investments should have a duration that is not greater than +/- 40% that of Barclays Capital Aggregate Bond Index in order to minimize interest rate risk. The University has no formal investment policy that addresses interest rate risk for investments other than those under the control of the Endowment Board.

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The University's Endowment Board has a formal investment policy that addresses credit risk. Each fixed income investment manager must assure that no position of any one issuer shall exceed 8% of the manager's portfolio at market value, with the exception of securities issued by the U.S. government and its agencies. Each fixed income portfolio must have an overall weighted average credit rating of "A" or better by Moody's and Standard & Poor's rating services, except where dedicated positions to less than investment grade securities are approved by the investment committee. There shall be no more than 7.5% of bond investments rated below "B" and no more than 25% of the portfolio may be in investments rated below investment

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

grade (below Baa/BBB). Split rated securities will be governed by the lower rating. Investments in corporate securities of any one economic sector may be no more than 25% of the Portfolio value. No more than 60% of the portfolio shall be invested in either corporate or mortgage-backed securities. The University has no formal investment policy that addresses credit risk for investments other than those under the control of the Endowment Board.

Custodial Credit Risk: Custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Currently, the Endowment Fund does not participate in a securities lending program, therefore counterparty risk is not material. With regard to the safety of assets held by the custodian, the Endowment Fund retains title to those assets; as such, in the event of the broker/dealer failure, the assets held do not become assets of the broker/dealer and are protected from any counterparty claimants. Those assets not held in the University's name are invested by the fiscal agent in accordance with a forward delivery agreement and are traded as funds are needed to meet debt service obligations. These assets are held in trust by the fiscal agent and are also protected from any counterparty claimants. The University has no formal investment policy that addresses custodial credit risk for investments other than those under the control of the Endowment Board.

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

Investment Type	Fair Value	Investment Maturities (in Years)		
		Less Than 1	1 to 5	6 to 10
Debt Securities				
U.S. Treasuries	\$ 545,281.68	\$ 457,653.15	\$ 64,925.77	\$ 22,702.76
U.S. Agencies	67,316.70		62,326.55	4,990.15
Debt Mutual Funds	6,663,261.53		1,588,960.92	5,074,300.61
Money Market Mutual Funds	2,105,158.92	2,105,158.92		
Total Debt Securities	9,381,018.83	\$ 2,562,812.07	\$ 1,716,213.24	\$ 5,101,993.52
Other Securities				
UNC Investment Fund	896,473.63			
International Mutual Funds	9,468,712.87			
Equity Mutual Funds	17,936,047.40			
Hedge Funds	7,122,181.00			
Private Equity Limited Partnerships	424,591.36			
Domestic Stocks	285,640.81			
Foreign Stocks	25,352.25			
Other	1,151,977.49			
Total Investments	\$ 46,691,995.64			

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

	Fair Value	AAA Aaa	A	BBB Baa
U.S. Agencies	\$ 67,316.70	\$ 67,316.70	\$ 0.00	\$ 0.00
Debt Mutual Funds	6,663,261.53	21,393.68	5,586,953.60	1,054,914.25
Money Market Mutual Funds	2,105,158.92	2,105,158.92		
Totals	\$ 8,835,737.15	\$ 2,193,869.30	\$ 5,586,953.60	\$ 1,054,914.25

Rating Agency: Moodys / Standard and Poors

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

Investment Type	Held by Counterparty	Held by Counterparty's Trust Dept or Agent not in University's Name
U.S. Treasuries	\$ 98,896.27	\$ 446,385.41
U.S. Agencies	67,316.70	
Domestic Stocks	285,640.81	
Foreign Stocks	25,352.25	
Total	\$ 477,206.03	\$ 446,385.41

Component Units - Investments of the University's discretely presented component unit, the East Carolina University Foundation, Inc. and Consolidated Affiliates, 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. Because the Foundation reports under the FASB reporting model, disclosures of the various investment risks are not required. The following is an analysis of investments by type:

Investment Type	Carrying Value
Common Stock	\$ 294,370
Mutual Funds	75,530,182
Alternative Investments	24,754,034
Total	\$ 100,578,586

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

D. Reconciliation of Deposits and Investments - A reconciliation of deposits and investments for the University as of June 30, 2014, is as follows:

Cash on Hand	\$	114,376.72
Amount of Deposits with Private Financial Institutions		95,119.11
Deposits in the Short-Term Investment Fund		293,055,159.29
Investments		46,691,995.64
Total Deposits and Investments	\$	339,956,650.76
Deposits		
Current:		
Cash and Cash Equivalents	\$	193,658,604.81
Restricted Cash and Cash Equivalents		23,038,928.88
Noncurrent:		
Restricted Cash and Cash Equivalents		76,567,121.43
Total Deposits		293,264,655.12
Investments		
Noncurrent:		
Endowment Investments		45,087,380.19
Restricted Investments		1,604,615.45
Total Investments		46,691,995.64
Total Deposits and Investments	\$	339,956,650.76

NOTE 3 - 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. 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's endowment funds are based on an adopted spending policy which

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

provides a distribution of four (4%) of its calendar year end endowment fund's twelve month weighted average balance prior to the addition of the current year investment return. To the extent that the total return for the current year exceeds the payout and a 1.1 percent administrative fee, the excess is added to accumulated earnings unless donor restrictions require that it be added to principal. If current year earnings do not meet the payout requirements, the University uses accumulated income and appreciation from restricted, expendable net asset endowment balances to make up the difference. At June 30, 2014, endowment net assets of \$14,995,086.37 were available to be spent, all of which was restricted to specific purposes.

NOTE 4 - RECEIVABLES

Receivables at June 30, 2014, were as follows:

	<u>Gross Receivables</u>	<u>Less Allowance for Doubtful Accounts</u>	<u>Net Receivables</u>
Current Receivables:			
Students	\$ 2,277,275.07	\$ 950,000.00	\$ 1,327,275.07
Student Sponsors	239,764.40		239,764.40
Patients	54,093,882.97	6,930,501.40	47,163,381.57
Accounts	2,530,296.82	9,329.00	2,520,967.82
Intergovernmental	2,905,258.06		2,905,258.06
Grant Sponsors	1,188,529.02		1,188,529.02
Investment Earnings	0.03		0.03
Interest on Loans	410,411.42		410,411.42
Federal Interest Subsidy on Debt	113,997.46		113,997.46
Other	942,375.87	39,166.82	903,209.05
	<u>\$ 64,701,791.12</u>	<u>\$ 7,928,997.22</u>	<u>\$ 56,772,793.90</u>
Noncurrent Receivables:			
Patients	<u>\$ 3,834,432.24</u>	<u>\$ 0.00</u>	<u>\$ 3,834,432.24</u>
Notes Receivable:			
Notes Receivable - Current:			
Federal Loan Programs	\$ 2,222,883.24	\$ 1,147,604.47	\$ 1,075,278.77
Institutional Student Loan Programs	8,814.54	8,279.06	535.48
	<u>\$ 2,231,697.78</u>	<u>\$ 1,155,883.53</u>	<u>\$ 1,075,814.25</u>
Notes Receivable - Noncurrent:			
Federal Loan Programs	\$ 10,523,022.55	\$ 761,122.67	\$ 9,761,899.88
Institutional Student Loan Programs	300.00		300.00
	<u>\$ 10,523,322.55</u>	<u>\$ 761,122.67</u>	<u>\$ 9,762,199.88</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 5 - CAPITAL ASSETS

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

	Balance July 1, 2013	Increases	Decreases	Balance June 30, 2014
Capital Assets, Nondepreciable:				
Land and Permanent Easements	\$ 44,519,927.24	\$ 1,482,179.07	\$ 0.00	\$ 46,002,106.31
Construction in Progress	29,875,393.10	39,233,797.29	37,979,304.78	31,129,885.61
Computer Software in Development	966,479.00	63,568.38	356,479.00	673,568.38
Total Capital Assets, Nondepreciable	75,361,799.34	40,779,544.74	38,335,783.78	77,805,560.30
Capital Assets, Depreciable:				
Buildings	837,474,895.36	37,422,792.67	1,932,513.47	872,965,174.56
Machinery and Equipment	126,771,069.31	9,792,037.45	4,870,221.38	131,692,885.38
General Infrastructure	100,573,801.18	927,057.00	339,200.08	101,161,658.10
Computer Software	13,925,130.54	128,000.00	160,000.00	13,893,130.54
Total Capital Assets, Depreciable	1,078,744,896.39	48,269,887.12	7,301,934.93	1,119,712,848.58
Less Accumulated Depreciation/Amortization for:				
Buildings	195,744,236.60	13,485,805.64	1,788,284.48	207,441,757.76
Machinery and Equipment	61,038,283.68	8,841,290.17	3,799,202.16	66,080,371.69
General Infrastructure	17,634,361.04	2,808,351.64	81,559.68	20,361,153.00
Computer Software	4,917,860.76	803,149.73	128,000.00	5,593,010.49
Total Accumulated Depreciation/Amortization	279,334,742.08	25,938,597.18	5,797,046.32	299,476,292.94
Total Capital Assets, Depreciable, Net	799,410,154.31	22,331,289.94	1,504,888.61	820,236,555.64
Capital Assets, Net	\$ 874,771,953.65	\$ 63,110,834.68	\$ 39,840,672.39	\$ 898,042,115.94

During the year ended June 30, 2014, the University incurred \$7,651,478.59 in interest costs related to the acquisition and construction of capital assets. Of this total, \$7,317,368.10 was charged in interest expense, and \$334,110.49 was capitalized.

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

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

	Amount
Accounts Payable and Accrued Liabilities	
Accounts Payable	\$ 14,675,611.02
Accrued Payroll	15,206,091.64
Contract Retainage	1,420,903.21
Other	288,241.30
Total Accounts Payable and Accrued Liabilities	\$ 31,590,847.17

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 7 - LONG-TERM LIABILITIES

UNIVERSITY

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

	Balance July 1, 2013 (As Restated)	Additions	Reductions	Balance June 30, 2014	Current Portion
Revenue Bonds Payable	\$ 140,965,000.00	\$ 53,685,000.00	\$ 7,235,000.00	\$ 187,415,000.00	\$ 7,215,000.00
Certificates of Participation	1,095,000.00		1,095,000.00		
Plus: Unamortized Premium	4,267,290.01	4,093,631.70	454,734.26	7,906,187.45	
Less: Unamortized Discount	(229,639.94)	(301,077.40)	(16,162.87)	(514,554.47)	
Total Revenue Bonds and Certificates of Participation Payable, Net	<u>146,097,650.07</u>	<u>57,477,554.30</u>	<u>8,768,571.39</u>	<u>194,806,632.98</u>	<u>7,215,000.00</u>
Notes Payable	13,602,640.67		2,281,093.66	11,321,547.01	1,968,450.46
Capital Leases Payable	349,999.49		130,426.36	219,573.13	110,850.88
Compensated Absences	21,551,715.49	15,465,609.02	14,987,042.48	22,030,282.03	1,371,866.70
Total Long-Term Liabilities	<u>\$ 181,602,005.72</u>	<u>\$ 72,943,163.32</u>	<u>\$ 26,167,133.89</u>	<u>\$ 228,378,035.15</u>	<u>\$ 10,666,168.04</u>

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

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

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through June 30, 2014	Principal Outstanding June 30, 2014	See Table Below
Revenue Bonds Payable							
Housing and Dining Services							
Housing and Dining Revenue Refunding Bonds	2001B	5.75	11/01/2015	\$ 11,985,000.00	\$ 11,095,000.00	\$ 890,000.00	(1)
General Revenue Bonds Payable							
Tyler Dorm Project (BAB)	2010B	2.791-5.825**	10/01/2030	10,045,000.00		10,045,000.00	
Wright Place Renovations (BAB)	2010B	2.791-4.581**	10/01/2020	1,990,000.00		1,990,000.00	
Olympic Sports Facility(BAB)	2010B	2.791-5.875**	10/01/2035	15,935,000.00		15,935,000.00	
Refunding of 2003A West End Dining Project	2012	2.984	04/01/2024	4,650,000.00	620,000.00	4,030,000.00	
Refunding of 2004C College Hill Dormitory Construction	2012	2.984	04/01/2027	5,770,000.00	100,000.00	5,670,000.00	
Refunding of 2004C College Hill Dormitory Construction	2013A	2.5-4.0	10/01/2033	10,905,000.00		10,905,000.00	
Gateway East and West Housing Project	2014A	2.0-5.0	10/01/2043	53,685,000.00		53,685,000.00	
Total General Revenue Bonds Payable				<u>102,980,000.00</u>	<u>720,000.00</u>	<u>102,260,000.00</u>	
The University of North Carolina System Pool Revenue Bonds							
College Hill Dormitory Supplemental Funds	2006A	4.0-5.0	10/01/2033	3,805,000.00	585,000.00	3,220,000.00	
Refunding of Series 1999 (Student Health)	2006A	4.0-5.0	10/01/2018	2,110,000.00	950,000.00	1,160,000.00	
Refunding of Series 2001A (Jones and Galley)	2006A	4.0-5.0	10/01/2021	8,775,000.00	1,590,000.00	7,185,000.00	
Dining Project Croatan	2009A	3.0-5.25	10/01/2029	8,050,000.00	1,100,000.00	6,950,000.00	
Scott Residence Hall	2009A	3.0-5.25	10/01/2034	29,360,000.00	2,165,000.00	27,195,000.00	
Softball Field Project	2009A	3.0-5.25	10/01/2034	4,885,000.00	465,000.00	4,420,000.00	
Refunding of 1998 Housing and Dining Bonds	2009A	3.0-5.0	10/01/2018	2,820,000.00	1,110,000.00	1,710,000.00	
East End Zone Project	2010A	3.0-5.0	10/01/2029	17,400,000.00	1,565,000.00	15,835,000.00	
Refunding of 2004C College Hill Dormitory Construction	2010A	3.0-5.0	10/01/2021	4,370,000.00	30,000.00	4,340,000.00	
Refunding of 2001C Student Fee Revenue Refunding Bonds	2011A	4.0-5.0	05/01/2019	7,125,000.00	2,505,000.00	4,620,000.00	
Refunding of 2003A West End Dining Project	2011A	4.0-5.0	05/01/2021	5,215,000.00	120,000.00	5,095,000.00	
Refunding of 2004C College Hill Dormitory Construction	2011A	4.0-5.0	05/01/2023	2,545,000.00	10,000.00	2,535,000.00	
Total The University of North Carolina System Pool Revenue Bonds				<u>96,460,000.00</u>	<u>12,195,000.00</u>	<u>84,265,000.00</u>	
Total Revenue Bonds Payable (principal only)				<u>\$ 211,425,000.00</u>	<u>\$ 24,010,000.00</u>	<u>187,415,000.00</u>	
Less: Unamortized Discount						(514,554.47)	
Plus: Unamortized Premium						7,906,187.45	
Total Revenue Bonds Payable, Net						<u>\$ 194,806,632.98</u>	

** 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

Ref	Revenue Source	Total Future Revenues Pledged	Current Year		Estimate of % of Revenues Pledged	
			Revenues Net of Expenses	Principal		Interest
(1)	Housing & Dining Revenues	\$ 941,750.00	\$ 11,078,901.48	\$ 410,000.00	\$ 62,962.50	4.27%

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

Fiscal Year	Annual Requirements			
	Revenue Bonds Payable		Notes Payable	
	Principal	Interest	Principal	Interest
2015	\$ 7,215,000.00	\$ 8,354,289.20	\$ 1,968,450.46	\$ 214,037.42
2016	7,510,000.00	8,093,195.29	2,007,539.19	174,948.69
2017	8,280,000.00	7,787,576.38	2,047,404.13	135,083.76
2018	8,615,000.00	7,434,717.78	2,088,060.69	94,427.19
2019	9,100,000.00	7,037,177.12	2,129,524.59	52,963.29
2020-2024	39,105,000.00	29,628,552.10	1,080,567.95	10,676.01
2025-2029	38,655,000.00	20,840,662.89		
2030-2034	37,015,000.00	11,608,816.27		
2035-2039	16,520,000.00	5,252,803.13		
2040-2044	15,400,000.00	1,799,475.00		
Total Requirements	\$ 187,415,000.00	\$ 107,837,265.16	\$ 11,321,547.01	\$ 682,136.36

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

Purpose	Financial Institution	Interest Rate/Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through June 30, 2014	Principal Outstanding June 30, 2014
Auxiliary Gym	US Bank NA	1.976%	11/01/2019	\$ 13,251,669.83	\$ 1,930,122.82	\$ 11,321,547.01

COMPONENT UNITS

In December 2008, the East Carolina University Real Estate Foundation Inc., which is an affiliate of the East Carolina University Foundation, Inc., purchased real estate located at 2325 Stantonsburg Road in Greenville, North Carolina for \$3,300,000. This acquisition was financed for 100% of the purchase price, less associated costs, based on a twenty-year amortization with a final payment of all remaining principal and accrued interest due on January 5, 2019. As of June 30, 2014, the balance on the principal was \$2,773,442. The note has a variable interest rate of LIBOR plus 1.05%.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The Affiliate entered into an interest rate swap agreement which effectively converts the variable rate note to a fixed rate note at an annual interest rate of 3.85%.

In July 2013, Green Town Properties, Inc. and the East Carolina University Foundation, Inc. purchased real estate located at 402 Bowman Gray Drive in Greenville, North Carolina for \$775,000. This acquisition was financed for 100% of the purchase price, less associated costs, based on a twenty-year amortization with a final payment of all remaining principal and accrued interest due on July 31, 2023. As of June 30, 2014, the balance on the principal was \$749,331. The note has a fixed interest rate of 3.64% and is collateralized by the purchased property.

In July 2013, Green Town Properties, Inc. and the East Carolina University Foundation, Inc. purchased real estate located at 2280 Hemby Lane in Greenville, North Carolina for \$4,125,000. This acquisition was financed for 100% of the purchase price, less associated costs, based on a twenty-year amortization with a final payment of all remaining principal and accrued interest due on July 31, 2023. As of June 30, 2014, the balance on the principal was \$3,988,308. The note has a fixed interest rate of 3.64% and is collateralized by the purchased property.

Maturities of the long-term portion of notes payable as of June 30, 2014 were as follows:

Fiscal Year	Amount
2015	\$ 307,143.00
2016	317,921.00
2017	345,267.00
2018	358,228.00
2019	371,673.00
Thereafter	5,810,849.00
Total	7,511,081.00
Less Current Portion	307,143.00
Noncurrent portion of long-term debt	\$ 7,203,938.00

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 8 - LEASE OBLIGATIONS

- A. Capital Lease Obligations** - Capital lease obligations relating to medical equipment are recorded at the present value of the minimum lease payments. Future minimum lease payments under capital lease obligations consist of the following at June 30, 2014:

<u>Fiscal Year</u>	<u>Amount</u>
2015	\$ 119,099.02
2016	86,297.84
2017	<u>27,188.88</u>
Total Minimum Lease Payments	232,585.74
Amount Representing Interest (0 - 10.123% Rate of Interest)	<u>13,012.61</u>
Present Value of Future Lease Payments	<u><u>\$ 219,573.13</u></u>

Machinery and equipment acquired under capital lease amounted to \$641,713.07 at June 30, 2014.

Depreciation for the capital assets associated with capital leases is included in depreciation expense, and accumulated depreciation for assets acquired under capital lease totaled \$274,696.99 at June 30, 2014.

- B. Operating Lease Obligations** - The University entered into operating leases for equipment and buildings. Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2014:

<u>Fiscal Year</u>	<u>Amount</u>
2015	\$ 4,852,132.67
2016	4,027,996.68
2017	3,290,385.63
2018	2,351,955.41
2019	1,900,879.73
2020-2024	<u>4,413,967.56</u>
Total Minimum Lease Payments	<u><u>\$ 20,837,317.68</u></u>

Rental expense for all operating leases during the year was \$5,980,484.17.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 9 - REVENUES

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

	Gross Revenues	Internal Sales Eliminations	Less Scholarship Discounts	Less Allowance for Uncollectibles*	Less Indigent Care and Contractual Adjustments	Net Revenues
Operating Revenues:						
Student Tuition and Fees	\$ 207,003,893.24	\$ 0.00	\$ 37,479,035.51	\$ (150,000.00)	\$ 0.00	\$ 169,674,857.73
Patient Services	\$ 468,236,112.60	\$ 0.00	\$ 0.00	\$ 38,588,244.01	\$ 222,332,361.16	\$ 207,315,507.43
Sales and Services:						
Sales and Services of Auxiliary Enterprises:						
Residential Life	\$ 29,134,179.09	\$ 1,580,492.80	\$ 4,934,139.34	\$ 0.00	\$ 0.00	\$ 22,619,546.95
Dining	27,370,006.19	1,017,665.12	3,782,476.04			22,569,865.03
Student Union Services	42,052.63					42,052.63
Health, Physical Education, and Recreation Services	1,961,383.37	381,967.70				1,579,415.67
Bookstore	12,892,434.70	115,180.28	1,245,806.81			11,531,447.61
Parking	2,729,026.81	57,473.50		(154,362.49)		2,825,915.80
Athletic	16,017,760.61					16,017,760.61
Other	1,586,755.06	379,432.62		30,251.77		1,177,070.67
Sales and Services of Education and Related Activities	8,277,913.46	1,211,230.20				7,066,683.26
Total Sales and Services	\$ 100,011,511.92	\$ 4,743,442.22	\$ 9,962,422.19	\$ (124,110.72)	\$ 0.00	\$ 85,429,758.23

NOTE 10 - 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	Other Operating Expenses	Total
Instruction	\$ 237,278,535.02	\$ 9,703,811.72	\$ 16,878,416.26	\$ 0.00	\$ 58,364.93	\$ 0.00	\$ 0.00	\$ 263,919,127.93
Research	12,642,436.79	2,301,025.84	4,783,023.35		433.44			19,726,919.42
Public Service	13,817,273.59	172,509.93	3,250,894.33		1,155.84			17,241,833.69
Academic Support	18,899,768.35	11,897,033.22	3,107,280.54		14,796.30			33,918,878.41
Student Services	10,010,952.66	430,188.17	1,272,984.11					11,714,124.94
Institutional Support	35,680,361.09	4,029,512.27	9,238,036.44		28,374.04			48,976,283.84
Operations and Maintenance of Plant	23,820,125.33	16,507,735.40	6,723,717.75		18,735,866.30			65,787,444.78
Student Financial Aid				39,879,568.01				39,879,568.01
Auxiliary Enterprises	188,764,131.81	36,658,386.89	66,636,265.84		682,927.35			292,741,711.89
Depreciation/ Amortization						25,938,597.18		25,938,597.18
Other Operating Expenses							422,279.26	422,279.26
Total Operating Expenses	\$ 540,913,584.64	\$ 81,700,203.44	\$ 111,890,618.62	\$ 39,879,568.01	\$ 19,521,918.20	\$ 25,938,597.18	\$ 422,279.26	\$ 820,266,769.35

NOTE 11 - PENSION PLANS

Retirement Plans - Each permanent full-time employee, as a condition of employment, is a member of either the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Eligible employees can elect to participate in the Optional Retirement Program at the time of

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

employment; otherwise they are automatically enrolled in the Teachers' and State Employees' Retirement System.

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

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

For the current fiscal year, the University had a total payroll of \$425,302,702.24, of which \$191,033,860.52 was covered under the TSERS. Total employer and employee contributions for pension benefits for the year were \$16,600,842.48 and \$11,462,031.63, respectively.

Required employer contribution rates for the years ended June 30, 2013, and 2012, were 8.33% and 7.44%, respectively, while employee contributions were 6% each year. The University made 100% of its annual required contributions for the years ended June 30, 2014, 2013, and 2012, which were \$16,600,842.48, \$15,542,359.08 and \$13,443,660.78, respectively.

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

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

participation in the Program. Participants become eligible to receive distributions when they terminate employment or retire.

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

For the current fiscal year, the University had a total payroll of \$425,302,702.24, of which \$184,351,080.56 was covered under the Optional Retirement Program. Total employer and employee contributions for pension benefits for the year were \$12,609,613.91 and \$11,061,064.83 respectively.

NOTE 12 - OTHER POSTEMPLOYMENT BENEFITS

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

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

By General Statute, a Retiree Health Benefit Fund (the Fund) has been established as a fund in which accumulated contributions from employers and any earnings on those contributions shall be used to provide health benefits to retired and disabled employees and applicable beneficiaries. By statute, the Fund is administered by the Board of Trustees of the Teachers' and State Employees' Retirement System and contributions to the Fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and applicable 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

For the current fiscal year the University contributed 5.40% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the Fund. Required contribution rates for the years ended June 30, 2013, and 2012, were 5.30% and 5.0%, respectively. The University made 100% of its annual required contributions to the Plan for the years ended June 30, 2014, 2013, and 2012, which were \$20,270,786.82, \$19,231,505.09, and \$17,761,628.38, respectively. The University assumes no liability for retiree health care benefits provided by the programs other than its required contribution.

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

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

Disability income benefits are funded by actuarially determined employer contributions that are established by the General Assembly. For the fiscal year ended June 30, 2014, the University made a statutory contribution of .44% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. Required contribution rates for the years ended June 30, 2013, and 2012, were .44% and .52%, respectively. The University made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2014, 2013, and 2012, which were \$1,651,693.74, \$1,596,577.78, and \$1,836,809.35, 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*.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 13 - 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.

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.

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 for primary extended coverage for buildings and contents. Coverage may be purchased through the Fund for sprinkler leakage, theft, vandalism, or all-risk perils. Flood insurance may be purchased for qualifying assets. University departments also have the option to purchase all-risk coverage for computers and miscellaneous equipment on a scheduled basis.

The University has the option to purchase through the Fund different levels of coverage for the University's buildings and contents. The optional levels of coverage are decided upon and paid for by the departments occupying the University's buildings.

The types of optional coverage are: Sprinkler Leakage Coverage for buildings with fire sprinklers; Flood Coverage for buildings prone to flood; Extended Coverage for windstorm, hail, explosion, aircraft or vehicles, riot or civil commotion and smoke; Broad Form Coverage for windstorm, hail, explosion, aircraft or vehicles, riot or civil commotion, smoke, vandalism, sprinkler leakage, sinkhole collapse, volcanic action, falling objects, weight of snow, ice or sleet, and water damage; All Risk Special Form Coverage for windstorm, hail, explosion, aircraft or vehicles, riot or civil commotion, smoke, vandalism, sprinkler leakage, sinkhole collapse, volcanic action, falling objects, weight of snow, ice or sleet, water damage, theft, any other loss not specifically

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

excluded. The coverage rates are determined by the Department of Insurance State Property Fire Insurance Fund. Losses covered by the Fund are subject to a \$5,000 per occurrence deductible at the insured replacement value of the building at the time of the loss.

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.

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

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: professional liability, medical malpractice, accident health, athletic accident, postal contract bond, surety bond, student internship liability, oceanographic equipment, leased equipment, boiler and machinery, inland marine property, watercraft, fine arts, musical instruments, modular units, international students, study abroad students, business travel and policies as the need for additional coverage arises.

The University provides medical malpractice insurance for Brody School of Medicine faculty physicians and independently licensed allied health providers (Nurse Practitioners, Certified Registered Nurse Anesthetists, Certified Nurse Midwives, and Physician Assistants). There is a shared blanket policy for all other employees of the ECU Physicians. The medical malpractice is with a private insurance company with coverage of \$3,000,000 per occurrence, \$5,000,000 annual aggregate, and a \$200,000 deductible; as well as an excess policy in the amount of \$ 10,000,000.

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

The North Carolina Workers' Compensation Program provides benefits to workers injured on the job. All employees of the State and its component units are included in the program. When an employee is injured, the University's primary responsibility is to arrange for and provide the necessary treatment for

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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.

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.

Hurricane Irene struck East Carolina University on August 27, 2011. The resulting damage to the campus was significant at a reported \$2,063,357. Major and immediate repairs were needed to repair roof damage, to repair and/or replace equipment damaged by wind or flooding, to remove trees down or causing a hazard to the campus, to restore parking and roadways and to otherwise restore the campus to a safe and effective operating condition. The University administration addressed the emergency situation and then a detailed scope of work continued to evolve as the assessment continued. As of 06/30/2014, all repairs/replacements have been completed and claims with FEMA and NCDOI have been closed.

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

NOTE 14 - COMMITMENTS AND CONTINGENCIES

- A. **Commitments** - The University has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were \$55,794,581.58 and on other purchases were \$13,579,685.39 at June 30, 2014.
- B. **Pending Litigation and Claims** - The University is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. University management 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 15 - INVESTMENT IN JOINT VENTURES

- A. **Moye Medical Endoscopy Center, LLC** - The University participates in a joint venture with Vidant Medical Center, to operate Moye Medical Endoscopy Center, LLC, d/b/a East Carolina Endoscopy Center. The

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

University has an equity interest of \$849,765.84 which has been reflected in the financial statements. The University has an ongoing financial responsibility for the joint venture because of its 50% ownership stake in the company. Complete financial statements for Moye Medical Endoscopy Center, LLC can be obtained from 3800 East Tenth Street, Second Floor, Greenville, NC 27858.

- B. Carolina Behavioral Health Alliance, LLC** - The University participates in a joint venture with The University of North Carolina at Chapel Hill and Wake Forest University to operate Carolina Behavioral Health Alliance, LLC. The University has an equity interest of \$202,173.00 which has been reflected in the financial statements. The University has an ongoing financial responsibility for the joint venture because of its 33.33% ownership stake in the company. Complete financial statements for Carolina Behavioral Health Alliance, LLC can be obtained from 3800 East Tenth Street, Second Floor, Greenville, NC 27858.
- C. NewCo Cancer Services, LLC** - The University participates in a joint venture with Vidant Medical Center, to operate NewCo Cancer Services, LLC, d/b/a the Leo Jenkins Cancer Center. The University has an equity interest of \$4,959,390.00 which has been reflected in the financial statements. The University has an ongoing financial responsibility for the joint venture because of its 50% ownership stake in the company. Complete financial statements for NewCo Cancer Services, LLC can be obtained from 3800 East Tenth Street, Second Floor, Greenville, NC 27858.

NOTE 16 - ACQUISITION

On July 31, 2013, East Carolina University acquired East Carolina Neurology, a specialty medical practice, for \$7,011,669.34. The payment was comprised of \$571,000 in capitalized equipment, \$406,340 in expensed equipment and supplies, and \$6,034,329.34 in intangibles. The intangibles included the certificate of need, non-compete agreements for physicians, a ready workforce and goodwill. The intangibles are reflected on the balance sheet as a prepaid asset. The prepaid asset will be amortized over 4 years, which is the life of the certificate of need.

NOTE 17 - RELATED PARTIES

Foundations - There are three separately incorporated nonprofit foundations associated with the University that are not included as component units. These foundations are the East Carolina University Educational Foundation, Inc., the

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

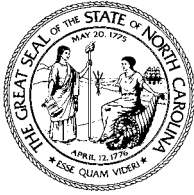
East Carolina University Medical and Health Sciences Foundation, Inc. and the East Carolina University Alumni Association, Inc. These organizations serve as the primary fundraising arm of the University through which individuals, corporations, and other organizations support University programs by providing scholarships, fellowships, faculty salary supplements, and unrestricted funds to specific colleges and the University's overall academic environment. The University's financial statements do not include the assets, liabilities, net position, or operational transactions of the foundations, except for support from each organization to the University. This support was \$11,816,644.22 for the year ended June 30, 2014. Indirect support from the foundations that was not included in the University's financial statements was \$997,263.33 for the year ended June 30, 2014.

NOTE 18 - NET POSITION RESTATEMENT

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

	<u>Amount</u>
July 1, 2013 Net Position as Previously Reported	\$ 992,076,429.77
Restatement:	
Expense previously amortized bond issuance costs pursuant to GASB 65 requirements	<u>(727,677.60)</u>
July 1, 2013 Net Position as Restated	<u><u>\$ 991,348,752.17</u></u>

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Beth A. Wood, CPA
State Auditor

STATE OF NORTH CAROLINA

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

Board of Trustees
East Carolina University
Greenville, 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 East Carolina 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 unit, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the University's basic financial statements, and have issued our report thereon dated November 11, 2014. Our report includes a reference to other auditors who audited the financial statements of East Carolina University Foundation, Inc. and Consolidated Affiliates, as described in our report on the University's financial statements. The financial statements of the discretely presented component unit were not audited in accordance with *Government Auditing Standards*, and accordingly, this report does not include reporting on internal control over financial reporting or instances of reportable noncompliance associated with the discretely presented component unit.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable

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

possibility that a material misstatement of the University's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Compliance and Other Matters

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

Purpose of this Report

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



Beth A. Wood, CPA
State Auditor

Raleigh, North Carolina

November 11, 2014

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