



**WAKE FOREST UNIVERSITY**

Consolidated Financial Statements

June 30, 2015

(With Independent Auditors' Report Thereon)



**KPMG LLP**  
Suite 400  
300 North Greene Street  
Greensboro, NC 27401

## **Independent Auditors' Report**

The Board of Trustees  
Wake Forest University:

We have audited the accompanying consolidated financial statements of Wake Forest University (the University), which comprise the consolidated balance sheet as of June 30, 2015, and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditors' Responsibility***

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal controls relevant to the University's preparation and fair presentation of the consolidated 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 consolidated financial statements.

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

### ***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Wake Forest University as of June 30, 2015, and the changes in its net assets and its cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.



***Report on Summarized Comparative Information***

We have previously audited the 2014 consolidated financial statements, and we expressed an unmodified audit opinion on those audited consolidated financial statements in our report dated October 28, 2014. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2014 is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

***Other Matter***

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information included in the consolidated balance sheet, statement of activities, statement of cash flows, and the accompanying notes related to the College of Arts and Sciences, Schools of Law, Business, and Divinity, and Reynolda House, Inc. (collectively, Reynolda Campus); and Wake Forest University Health Sciences (WFUHS) is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

**KPMG LLP**

Greensboro, North Carolina  
October 30, 2015

**WAKE FOREST UNIVERSITY**

Consolidated Balance Sheet

June 30, 2015

(with summarized comparative financial information as of June 30, 2014)

(Dollars in thousands)

<b>Assets</b>	<b>Supplementary information</b>			
	<b>Reynolda Campus</b>	<b>WFUHS</b>	<b>2015</b>	<b>2014</b>
Cash and cash equivalents	\$ 50,574	159,960	210,534	51,439
Accounts receivable, net	8,618	103,766	112,384	355,823
Patient receivables, net	—	38,083	38,083	49,294
Contributions receivable, net	114,307	23,193	137,500	107,579
Notes receivable, net	22,313	832	23,145	24,224
Investments	936,827	691,438	1,628,265	1,593,247
Investments in real estate	22,800	—	22,800	23,731
Other assets	6,740	19,684	26,424	27,359
Land, buildings, and equipment, net	455,947	296,795	752,742	756,439
Total assets	<u>\$ 1,618,126</u>	<u>1,333,751</u>	<u>2,951,877</u>	<u>2,989,135</u>
<b>Liabilities and Net Assets</b>				
Liabilities:				
Accounts payable and accruals	\$ 30,012	238,281	268,293	280,661
Other liabilities and deferrals	78,983	164,818	243,801	355,321
Annuities payable	24,661	3,312	27,973	26,187
Notes payable and capital leases	16,408	29,832	46,240	25,012
Bonds payable	269,417	173,695	443,112	457,700
Postretirement benefits	15,862	38,996	54,858	59,222
Government grants refundable	9,582	—	9,582	9,688
Total liabilities	<u>444,925</u>	<u>648,934</u>	<u>1,093,859</u>	<u>1,213,791</u>
Net assets:				
Unrestricted	511,185	458,273	969,458	941,441
Temporarily restricted	377,246	69,239	446,485	422,400
Permanently restricted	284,770	157,305	442,075	411,503
Total net assets	<u>1,173,201</u>	<u>684,817</u>	<u>1,858,018</u>	<u>1,775,344</u>
Total liabilities and net assets	<u>\$ 1,618,126</u>	<u>1,333,751</u>	<u>2,951,877</u>	<u>2,989,135</u>

See accompanying notes to consolidated financial statements.

**WAKE FOREST UNIVERSITY**

Consolidated Statement of Activities

Year ended June 30, 2015

(with summarized comparative financial information for the year ended June 30, 2014)

(Dollars in thousands)

	2015			Total	2014 Total
	Unrestricted	Temporarily restricted	Permanently restricted		
Operating revenues:					
Student tuition and fees	\$ 332,495	—	—	332,495	317,607
Less student aid	(97,256)	—	—	(97,256)	(92,867)
Net student tuition and fees	235,239	—	—	235,239	224,740
Government grants and contracts	176,373	—	—	176,373	180,075
Private grants and contracts	2,951	16,812	—	19,763	17,922
Contributions	27,226	33,587	—	60,813	40,542
Investment return designated for current operations	38,189	26,399	—	64,588	63,103
Patient revenue, net	428,744	—	—	428,744	367,451
Other	138,447	—	—	138,447	242,826
Sales and services of auxiliary enterprises	90,196	—	—	90,196	80,284
Net assets released from restrictions	53,028	(53,028)	—	—	—
Total operating revenues	1,190,393	23,770	—	1,214,163	1,216,943
Operating expenses:					
Salaries and wages	613,262	—	—	613,262	581,163
Employee benefits	123,908	—	—	123,908	111,109
Student aid	3,409	—	—	3,409	9,083
Services	195,096	—	—	195,096	210,051
Clinical and laboratory supplies	47,909	—	—	47,909	50,050
Other operating expenses	98,932	—	—	98,932	204,176
Integration and restructuring costs	—	—	—	—	6,149
Depreciation and amortization	65,350	—	—	65,350	62,233
Interest on debt	18,213	—	—	18,213	17,813
Total operating expenses	1,166,079	—	—	1,166,079	1,251,827
Operating excess (deficit)	24,314	23,770	—	48,084	(34,884)
Nonoperating activities:					
Restricted contributions	—	20,464	33,088	53,552	60,366
Net assets released from restriction	4,759	(4,759)	—	—	—
Investment return in excess of (less than)					
amounts designated for current operations	(20,134)	(18,127)	(256)	(38,517)	70,713
Actuarial (loss) gain on annuity obligations	—	—	(1,291)	(1,291)	(821)
Unrealized gain (loss) on interest rate swaps	(2,084)	—	—	(2,084)	18
Postretirement related changes other than net					
periodic cost	9,431	—	—	9,431	(11,286)
Gain from affiliates, equity method	10,749	—	—	10,749	3,167
Donor designation changes	—	35	(35)	—	(727)
Other, net	982	2,702	(934)	2,750	(4,905)
Change from nonoperating activities	3,703	315	30,572	34,590	116,525
Change in net assets	28,017	24,085	30,572	82,674	81,641
Net assets at beginning of year	941,441	422,400	411,503	1,775,344	1,693,703
Net assets at end of year	\$ 969,458	446,485	442,075	1,858,018	1,775,344

See accompanying notes to consolidated financial statements.

**WAKE FOREST UNIVERSITY**

Statement of Activities

College of Arts and Sciences, Schools of Law, Business, and Divinity, and Reynolda House, Inc.  
(Supplementary Information)

Year ended June 30, 2015

(Dollars in thousands)

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Operating revenues:				
Student tuition and fees	\$ 293,431	—	—	293,431
Less student aid	(86,770)	—	—	(86,770)
Net student tuition and fees	206,661	—	—	206,661
Government grants and contracts	8,623	—	—	8,623
Private grants and contracts	2,040	—	—	2,040
Contributions	21,416	15,493	—	36,909
Investment return designated for current operations	16,210	20,341	—	36,551
Patient revenue, net	—	—	—	—
Other	7,536	—	—	7,536
Sales and services of auxiliary enterprises	90,196	—	—	90,196
Net assets released from restrictions	26,468	(26,468)	—	—
Total operating revenues	<u>379,150</u>	<u>9,366</u>	<u>—</u>	<u>388,516</u>
Operating expenses:				
Salaries and wages	177,471	—	—	177,471
Employee benefits	46,618	—	—	46,618
Student aid	3,409	—	—	3,409
Services	41,228	—	—	41,228
Clinical and laboratory supplies	—	—	—	—
Other operating expenses	53,281	—	—	53,281
Integration and restructuring costs	—	—	—	—
Depreciation and amortization	32,051	—	—	32,051
Interest on debt	12,294	—	—	12,294
Total operating expenses	<u>366,352</u>	<u>—</u>	<u>—</u>	<u>366,352</u>
Operating excess (deficit)	<u>12,798</u>	<u>9,366</u>	<u>—</u>	<u>22,164</u>
Nonoperating activities:				
Restricted contributions	—	20,464	22,577	43,041
Net assets released from restriction	4,759	(4,759)	—	—
Investment return in excess of (less than) amounts designated for current operations	(8,361)	(12,915)	386	(20,890)
Actuarial (loss) gain on annuity obligations	—	—	(1,402)	(1,402)
Unrealized gain (loss) on interest rate swaps	(1,835)	—	—	(1,835)
Postretirement related changes other than net periodic cost	207	—	—	207
Gain from affiliates, equity method	—	—	—	—
Donor designation changes	—	35	(35)	—
Other, net	2,930	505	(326)	3,109
Change from nonoperating activities	<u>(2,300)</u>	<u>3,330</u>	<u>21,200</u>	<u>22,230</u>
Change in net assets	10,498	12,696	21,200	44,394
Net assets at beginning of year	500,687	364,550	263,570	1,128,807
Net assets at end of year	\$ <u>511,185</u>	<u>377,246</u>	<u>284,770</u>	<u>1,173,201</u>

See accompanying notes to consolidated financial statements.

**WAKE FOREST UNIVERSITY**  
Statement of Activities  
Wake Forest University Health Sciences  
(Supplementary Information)  
Year ended June 30, 2015  
(Dollars in thousands)

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Operating revenues:				
Student tuition and fees	\$ 39,064	—	—	39,064
Less student aid	(10,486)	—	—	(10,486)
Net student tuition and fees	28,578	—	—	28,578
Government grants and contracts	167,750	—	—	167,750
Private grants and contracts	911	16,812	—	17,723
Contributions	5,810	18,094	—	23,904
Investment return designated for current operations	21,979	6,058	—	28,037
Patient revenue, net	428,744	—	—	428,744
Other	130,911	—	—	130,911
Sales and services of auxiliary enterprises	—	—	—	—
Net assets released from restrictions	26,560	(26,560)	—	—
Total operating revenues	811,243	14,404	—	825,647
Operating expenses:				
Salaries and wages	435,791	—	—	435,791
Employee benefits	77,290	—	—	77,290
Student aid	—	—	—	—
Services	153,868	—	—	153,868
Clinical and laboratory supplies	47,909	—	—	47,909
Other operating expenses	45,651	—	—	45,651
Integration and restructuring costs	—	—	—	—
Depreciation and amortization	33,299	—	—	33,299
Interest on debt	5,919	—	—	5,919
Total operating expenses	799,727	—	—	799,727
Operating excess (deficit)	11,516	14,404	—	25,920
Nonoperating activities:				
Restricted contributions	—	—	10,511	10,511
Net assets released from restriction	—	—	—	—
Investment return in excess of (less than) amounts designated for current operations	(11,773)	(5,212)	(642)	(17,627)
Actuarial (loss) gain on annuity obligations	—	—	111	111
Unrealized gain (loss) on interest rate swaps	(249)	—	—	(249)
Postretirement related changes other than net periodic cost	9,224	—	—	9,224
Gain from affiliates, equity method	10,749	—	—	10,749
Donor designation changes	—	—	—	—
Other, net	(1,948)	2,197	(608)	(359)
Change from nonoperating activities	6,003	(3,015)	9,372	12,360
Change in net assets	17,519	11,389	9,372	38,280
Net assets at beginning of year	440,754	57,850	147,933	646,537
Net assets at end of year	\$ 458,273	69,239	157,305	684,817

See accompanying notes to consolidated financial statements.

**WAKE FOREST UNIVERSITY**  
Consolidated Statement of Cash Flows  
Year ended June 30, 2015  
(with summarized comparative financial information for the year ended June 30, 2014)  
(Dollars in thousands)

	<b>Supplementary information</b>			
	<b>Reynolda Campus</b>	<b>WFUHS</b>	<b>2015</b>	<b>2014</b>
Cash flows from operating activities:				
Change in net assets	\$ 44,394	38,280	82,674	81,641
Adjustments to reconcile change in net assets to net cash provided by operating activities:				
Depreciation and amortization	32,051	33,299	65,350	62,233
Net (gains) losses on investments	(12,557)	18,200	5,643	(86,019)
Noncash gifts	(625)	—	(625)	(1,962)
Private gifts restricted for capital and long-term investment	(43,041)	(10,511)	(53,552)	(62,024)
Other revenue restricted for long-term investment	—	(573)	(573)	(11)
Loss on disposals of property and equipment	487	656	1,143	1,792
Gain from equity method affiliates	—	(10,749)	(10,749)	(3,167)
Unrealized (gain) loss on interest rate swaps	1,835	249	2,084	(18)
Bad debt expense	1,345	15,819	17,164	52,261
Changes in operating assets and liabilities:				
Accounts and patient receivables	(15)	275,710	275,695	(214,402)
Contributions receivable	(10,033)	(18,142)	(28,175)	(3,544)
Notes receivable	—	(258)	(258)	(8)
Other assets and other liabilities and deferrals	3,219	(94,130)	(90,911)	69,306
Accounts payable and accruals	16,280	(20,689)	(4,409)	124,615
Postretirement benefits	604	(2,767)	(2,163)	11,388
Annuities payable	1,896	111	2,007	(164)
Net cash provided by operating activities	<u>35,840</u>	<u>224,505</u>	<u>260,345</u>	<u>31,917</u>
Cash flows from investing activities:				
Purchases of land, buildings, and equipment	(56,007)	(17,823)	(73,830)	(79,422)
Proceeds from sale of land, buildings, and equipment	—	3,331	3,331	1,323
Repayments of notes receivable	—	1,447	1,447	1,132
Disbursements of loans to students and other	(3,421)	(21)	(3,442)	(2,577)
Repayments of loans to students and other	3,084	100	3,184	3,267
Purchases of investments	(393,237)	(280,810)	(674,047)	(542,820)
Net proceeds from sales and maturities of investments	377,778	228,761	606,539	512,844
Decrease in deposits with bond trustee	25	—	25	71,159
Net cash used in investing activities	<u>(71,778)</u>	<u>(65,015)</u>	<u>(136,793)</u>	<u>(35,094)</u>
Cash flows from financing activities:				
Change in government grants refundable	(106)	—	(106)	(139)
Proceeds from notes payable	10,728	13,039	23,767	3,857
Principal payments on notes payable	(225)	(7,929)	(8,154)	(33,530)
Proceeds from borrowings from WFUBMC	—	9,684	9,684	(2,158)
Payments on borrowings from WFUBMC	—	(35,367)	(35,367)	—
Principal payments on bonds payable	(6,195)	—	(6,195)	(10,520)
Proceeds from private gifts restricted for capital and long-term investment	40,172	10,511	50,683	48,370
Net realized gains restricted for long-term investment	—	573	573	724
Other revenue restricted for long-term investment	—	658	658	11
Net cash provided by (used in) financing activities	<u>44,374</u>	<u>(8,831)</u>	<u>35,543</u>	<u>6,615</u>
Net increase in cash and cash equivalents	8,436	150,659	159,095	3,438
Cash and cash equivalents at beginning of year	42,138	9,301	51,439	48,001
Cash and cash equivalents at end of year	<u>\$ 50,574</u>	<u>159,960</u>	<u>210,534</u>	<u>51,439</u>
Supplemental disclosures of cash flow information:				
Cash paid for interest, net of amounts capitalized	\$ 12,171	6,488	18,659	18,833
Assets acquired under capital leases	11,762	—	11,762	1,729
Transfer of plan assets to investments	—	—	—	34,812
Transfer of assets to due to/from WFUBMC	—	36,938	36,938	—
Capital expenditures included in account payable	10,900	740	11,640	—

See accompanying notes to consolidated financial statements.



# WAKE FOREST UNIVERSITY

## Notes to Consolidated Financial Statements

June 30, 2015

(Dollars in thousands)

### (1) Organization and Summary of Significant Accounting Policies

#### (a) *Description of Wake Forest University*

Wake Forest University (the University) is a private, coeducational, not-for-profit institution of higher education and research located in Winston-Salem, North Carolina. The consolidated financial statements of the University include the College of Arts and Sciences, Schools of Law, Business, and Divinity, and consolidating subsidiaries including: Verger Capital Fund (Master Fund), Verger Fund I, and Reynolda House, Inc. (collectively, Reynolda Campus), and Wake Forest University Health Sciences (WFUHS), and all entities over which the University has control, including all of the subsidiaries of Reynolda Campus and WFUHS, including Verger Fund II, which is controlled by the Master Fund. All significant intercompany balances and transactions have been eliminated in consolidation.

On October 18, 2013, the University's Board of Trustees created an asset management company and related investment funds. These entities included Verger Capital Management LLC (VCM), Verger Capital Fund (Master Fund), Verger Fund I LLC and Verger Fund II LLC. VCM provides investment management services for the University's long-term pool. The Master Fund provides investment services for Verger Fund I and Verger Fund II LLC. The Master Fund is controlled and consolidated by the University. Verger Fund I LLC was created to hold the Reynolda Campus long-term endowment pool. Verger Fund II LLC was created to hold the WFUHS and Reynolda House long-term endowment pools. As of June 30, 2015, VCM, Verger Capital Fund LLC, Verger Fund I LLC, and Verger Fund II LLC are consolidated entities.

Effective July 1, 2010, the Boards of WFUHS, North Carolina Baptist Hospital (NCBH), Wake Forest University Baptist Medical Center (WFUBMC) and the University approved the Medical Center Integration Agreement (the Integration Agreement or MCIA). The Integration Agreement allows for the leveraging of the combined resources of WFUHS and NCBH to fulfill a single mission, improve health and optimize performance of the combined organizations, while balancing patient care, education and research. The University and NCBH are the members of WFUBMC.

The Integration Agreement created an integrated academic medical center that combines clinical care, education and research under a single management and debt structure referred to as Wake Forest Baptist (WFB), which is governed by WFUBMC. One of the nation's preeminent academic medical centers, WFB is an integrated healthcare system that operates over 40 subsidiaries. It provides a continuum of care that includes primary care centers, outpatient rehabilitation, and dialysis centers. To ensure alignment across the organization, WFUHS and NCBH unrestricted operating income (deficit) are shared equally between the entities. Although the entities will be operated to maximize the value at the total WFB level, revenues, expenses, existing and new assets and debt will continue to be accounted for generally at the individual entity levels.

The WFUBMC Board is comprised of seven directors elected by NCBH from among its Board members, seven directors elected by the University's Board of Trustees and two nonvoting directors elected by the WFUBMC Board from among the faculty of WFUHS. Subject to the reserved powers of the members, the WFB operates WFUHS (including all subsidiaries and affiliates) and NCBH

# WAKE FOREST UNIVERSITY

## Notes to Consolidated Financial Statements

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(Dollars in thousands)

(including all subsidiaries and affiliates), including day-to-day management, strategic direction, managed care contracting and other business activities conferred on WFUBMC.

### **(b) Recently Adopted Accounting Standards**

In May 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-07, *Disclosures for Investments in Certain Entities That Calculate Net Assets Value per Share (or Its Equivalent)*. This ASU removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share as a practical expedient. The University adopted ASU 2015-07 in fiscal year 2015 and removed these investments from the summary of levels within the fair value hierarchy footnote disclosure.

In April 2015, the FASB issued ASU 2015-03, *Interest-Imputation of Interest (Subtopic 835-30) Simplifying the Presentation of Debt Issuance Costs*. This ASU requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts and that the amortization of debt issuance costs be reported as interest expense. The University adopted ASU 2015-03 in fiscal year 2015 and reclassified the June 30, 2014 bond issuance costs for the University and WFUHS are \$2,092 and \$1,328, respectively.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This ASU establishes principles for reporting useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. Particularly, that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 is effective for fiscal year 2019. WFUHS expects to record a decrease in net patient service revenue related to self-pay patients and a corresponding decrease in bad debt expense upon adoption of the standard.

### **(c) Basis of Presentation**

The consolidated financial statements have been prepared on the accrual basis in conformity with U.S. generally accepted accounting principles (GAAP).

Net assets, revenues, and gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the University and changes therein are classified and reported as follows:

- *Unrestricted net assets* – net assets that are not subject to donor-imposed stipulations.
- *Temporarily restricted net assets* – net assets subject to donor-imposed stipulations that will be met either by actions of the University and/or the passage of time.
- *Permanently restricted net assets* – net assets subject to donor-imposed stipulations that they be maintained permanently by the University. Generally, the donors of these assets permit the

## WAKE FOREST UNIVERSITY

### Notes to Consolidated Financial Statements

June 30, 2015

(Dollars in thousands)

University to use all, or part of, the income earned on related investments for general or specific purposes.

Revenues are reported as increases in unrestricted net assets unless their use is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulations or by law. Expirations of restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets.

Income and realized and unrealized gains on investments of permanently restricted net assets are reported as follows:

- As increases in permanently restricted net assets if the terms of the gift require that they be added to the principal of a permanent endowment fund.
- As increases in temporarily restricted net assets until appropriated for expenditure by the University and donor restrictions for their use are met.

Revenues earned, expenses incurred, and returns made available for the University's operating purposes of teaching, research, patient care, and other programs and services are components of the operating excess or deficit presented in the consolidated statement of activities. The University considers the following items to be nonoperating activities: restricted contributions for capital and long-term investment and the related net assets released from restriction, investment return in excess of or less than amounts designated for current operations, actuarial gain or loss on annuity obligations, unrealized gain or loss on interest rate swaps, postretirement related changes other than net periodic cost, gain or loss from affiliates (equity method), donor designation changes, and other, net.

#### *(d) Cash Equivalents*

Cash equivalents include highly liquid investments with original maturities at date of purchase of three months or less. Such assets, reported at fair value, primarily consist of depository account balances, money market funds and accounts. The University maintains bank accounts at various financial institutions covered by the Federal Depository Insurance Corporation (FDIC). At various times throughout the year, the University may maintain bank accounts in excess of the FDIC-insured limit. Management believes that the risk associated with these bank accounts is minimal.

#### *(e) Revenue Recognition*

The University's revenue recognition policies are as follows:

**Student tuition and fees** – Student tuition and fees are recorded as revenue during the year that the related services are rendered. Student tuition and fees received in advance of services to be rendered are recorded as deferred revenue. Student aid provided by the University is reflected as a reduction of gross student tuition and fee revenue. Student aid does not include payments made to students for services rendered to the University.

# WAKE FOREST UNIVERSITY

## Notes to Consolidated Financial Statements

June 30, 2015

(Dollars in thousands)

**Grants and contracts** – Revenues under grants and contracts with private and governmental sponsoring organizations are deferred until related expenses are incurred. The revenues include recoveries of direct and indirect costs, which are generally determined as a negotiated or agreed-upon percentage of direct costs with certain exclusions.

**Patient revenue, net** – WFUHS records patient revenue at the estimated net realizable amounts due from patients, third-party payers, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers and contractual adjustments. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and will be adjusted in future periods as interim or final settlements are determined.

**Charity care** – WFUHS provides care for patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. WFUHS does not pursue collection of amounts determined to qualify as charity care; accordingly, such amounts are not reported in net patient revenue.

WFUHS maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone and estimated costs incurred for services and supplies furnished under its charity care policy and equivalent service statistics. Costs incurred are estimated based on the ratio of total operating expenses to gross charges applied to charity care charges. The amounts of direct and indirect costs incurred for services and supplies furnished under WFUHS' charity care policy totaled approximately \$24,891 and \$14,918 in 2015 and 2014, respectively.

**HITECH Incentive Funding for Meaningful Use of Electronic Health Records (EHR)** – The American Recovery and Reinvestment Act of 2009 (ARRA) established incentive payments under the Medicare and Medicaid programs for certain healthcare providers that use certified EHR technology. The program is commonly referred to as the Health Information Technology for Economic and Clinical Health (HITECH) Act. To qualify for incentives under the HITECH Act, healthcare providers must meet designated EHR meaningful use criteria as defined by the Centers for Medicare and Medicaid Services (CMS). Incentive payments are awarded to healthcare providers who have attested to CMS that applicable meaningful use criteria have been met. Compliance with meaningful use criteria is subject to audit by the federal government or its designee and incentive payments are subject to adjustment in a future period. WFUHS recognizes revenue for EHR incentive payments in the period in which it has obtained reasonable assurance that it is in compliance with the applicable EHR meaningful use requirements. Accordingly, for the years ended June 30, 2015 and 2014, WFUHS recognized EHR incentives of approximately \$3,197 and \$4,988, respectively, which are included in other revenue (separate from net patient service revenue) in the consolidated statement of activities.

*(f) Contributions*

Contributions, including unconditional promises to give, are recognized as revenues in the period received. Contributions restricted for capital projects or permanent endowment funds and contributions under split-interest agreements or perpetual trusts are reported as nonoperating activities. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their

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estimated fair value. Contributions to be received after one year, net of an allowance for uncollectible contributions receivable, are discounted to their present value at a risk-adjusted rate. Amortization of discounts is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions. An allowance for uncollectible contributions receivable is provided based upon management's judgment, considering such factors as prior collection history, type of contribution, relationship with donor, and nature of fund-raising activity.

**(g) *Investments***

Investments in readily marketable debt and equity securities are stated at their fair values, which are determined based on quoted market prices. Investments in private equity and absolute return funds are reported at estimated fair value, utilizing their net asset values. Those net asset values are determined by the investment managers and are reviewed and evaluated by the University's investment management company. These estimated fair values may differ from the values that would have been used had a ready market existed for these investments. Investments in equity method affiliates are accounted for using the equity method.

**(h) *Investments in Real Estate***

Investments in real estate are primarily comprised of rental properties of the University and are valued at the lower of net book value or market. Accordingly, if there is a decline in market value the carrying amount of the investment is reduced to market value. The University records depreciation on rental properties over 40 years. Depreciation is calculated using the straight-line method. Real estate gifts held for sale are recorded at fair value, based on periodic external appraisals.

**(i) *Split-Interest Agreements***

The University's split-interest agreements with donors consist primarily of irrevocable charitable remainder trusts for which the University serves as trustee and charitable gift annuities. Assets held in these trusts are stated at fair value and are included in investments. Contribution revenue is recognized at the dates the trusts are established. The University recognizes the change in value of split-interest agreements according to the fair value of assets that are associated with each trust and recalculates the liability for the present value of annuity obligations. Any change in fair value is recognized in the consolidated statement of activities.

The University is also the beneficiary of certain trusts and other assets held and administered by others. The University's share of these assets is recognized in investments at fair value.

**(j) *Fair Value Measurements***

The fair value hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving

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significant unobservable inputs (Level 3 measurements). The hierarchy requires the use of observable market data when available. The three levels of the fair value hierarchy are as follows:

Level 1 – Valuations for assets and liabilities traded in active exchange markets as of the reporting date. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 – Valuations for assets and liabilities are determined through direct or indirect observations other than quoted market prices.

Level 3 – Valuations for assets and liabilities that are derived from other valuation methodologies including discounted cash flow models and similar techniques, and not based on market exchange, dealer or broker traded transactions.

Assets Valued at Net Asset Value (NAV) – As previously noted, the University has retrospectively adopted ASU 2015-07. As a result, the University removed investments valued using NAV under the practical expedient from the leveling table and identifies these investments as assets valued at NAV in note 8 in order to reconcile in note 8 to the consolidated balance sheet.

The carrying amounts of cash and cash equivalents (Level 1), patient receivables (Level 2), and accounts receivable (Level 2) approximate fair value because of the terms and relatively short maturity of these financial instruments. The carrying amounts of contributions receivable represent the present value of estimated future cash flows, which approximates fair value (Level 3). Investments (Levels 1–3, see note 8) and deposits with bond trustee (Level 1) are reported at fair value as of the date of the consolidated financial statements. A reasonable estimate of the fair value of notes receivable from students under government loan programs cannot be made because such loans are not sellable and can only be assigned to the U.S. government or its designees. The fair value of receivables from students under University loan programs (Level 2) approximates carrying value.

The carrying amounts of accounts payable and other accruals (Level 2) approximate fair value because of the relatively short maturity of these financial instruments. Annuities payable (Level 2) are recorded at fair value using a single discount rate equivalent to the University's nonexempt borrowing rate. The carrying amounts of notes and bonds payable (Level 2) with variable interest rates approximate their fair value because substantially all of these financial instruments bear interest at rates that approximate current market rates for borrowings with similar maturities and credit quality. The disclosure of fair value of fixed-rate debt maturities is determined using a relative price approach, by discounting future principal and interest payments at the market yield to maturity, and at the market yield to each call date. The fair value of Reynolda Campus Series 2009 fixed-rate tax-exempt bonds (Level 2) was \$115,751 and \$116,956 at June 30, 2015 and 2014, respectively. The fair value of WFUHS Series 2012B and Series 2012C fixed-rate bonds (Level 2) was \$116,319 and \$54,810, at June 30, 2015, respectively, and \$119,181 and \$56,955, at June 30, 2014, respectively.

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**(k) Bond Issuance Costs**

Costs related to the registration and issuance of bonds are carried at cost less accumulated amortization and are amortized over the life of the bonds on a method that approximates the effective-interest method and are included in bonds payable on the 2015 consolidated balance sheet.

**(l) Land, Buildings, and Equipment**

Land, buildings, and equipment are recorded at cost at date of acquisition or estimated fair market value on the date received for donated items. Depreciation is calculated using the straight-line method over the estimated useful life of each class or component of depreciable asset. Estimated lives range from 3 to 60 years. Depreciation is not calculated on land and construction in progress. Gains or losses on the disposal of land, buildings, and equipment are included in the consolidated statement of activities. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of constructing these assets.

**(m) Impairment of Long-Lived Assets**

The University periodically assesses the realizability of its long-lived assets and evaluates such assets for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. For assets to be held, impairment is determined to exist if estimated future cash flows, undiscounted and without interest charges, are less than the carrying amount. The University recognizes an impairment charge when the fair value of the asset or group of assets is less than the carrying value.

**(n) Asset Retirement Obligations**

The University has asset retirement obligations (AROs) arising from regulatory requirements to perform certain asset retirement activities at the time that certain buildings and equipment are disposed of or renovated. The liability was initially measured at fair value and subsequently is adjusted for accretion expense and changes in the amount or timing of the estimated cash flows. The corresponding asset retirement costs are capitalized as part of the carrying amount of the related long-lived asset and depreciated over the asset's useful life. The University revalues asset retirement obligations as remediation costs are incurred or as additional cost information becomes available.

**(o) Government Grants Refundable**

Funds provided by the U.S. government under the Federal Perkins Loan Program is loaned to qualified students and may be reloaned after collections. These funds are ultimately refundable to the U.S. government and are reported as liabilities.

**(p) Derivative Instruments**

The University holds certain interest rate swap agreements to manage the fixed/variable mix of its debt portfolio. The notional amounts of the agreements dictate the payments between the counterparties based on agreed-upon rates as determined in the agreements. The University records all derivative instruments on the consolidated balance sheet at their respective fair values. All changes in fair value

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are reflected in the consolidated statement of activities. Cash payments and receipts are included in interest on debt.

**(q) Postretirement Plans**

The University records annual amounts relating to its postretirement plans based on calculations that incorporate various actuarial and other assumptions including discount rates, mortality, assumed rates of return, turnover rates, and healthcare cost trend rates. The University reviews its assumptions on an annual basis and makes modifications to the assumptions based on current rates and trends when it is appropriate to do so. The effect of modifications to those assumptions is recorded as a change in unrestricted net assets and amortized to net periodic benefit cost over future periods using the corridor method. The University believes that the assumptions utilized in recording its obligations under its plans are reasonable based on its experience and market conditions. The net periodic benefit costs are recognized as employees render the services necessary to earn the postretirement benefits.

WFUHS sponsors a defined benefit postretirement medical and dental plan that covers all WFUHS full-time employees who elect coverage and satisfy the plan eligibility requirements when they retire. On June 2, 2011, the Board of WFUHS approved that effective as of January 1, 2012, the defined benefit postretirement plan would be discontinued for most future retirees. The minimum age required for postretirement benefits will increase from 60 to 62. However, the additional requirement of the rule of 75 (age and service) remains unchanged. All current retirees and currently eligible employees previously grandfathered will continue to be eligible for benefits under this plan. Any WFUHS employee who is within 5 years of meeting the new retirement eligibility of age 62 with combined age and years of service equal to at least 75 as of January 1, 2012 will be grandfathered into this benefit.

During fiscal year 2014, WFUHS signed a declaration to terminate the voluntary employees' beneficiary association (VEBA) and amended the terms of the trust to allow the assets to be drawn down to pay eligible plan participants' health and dental claims. As a result of the amendment, the assets are no longer considered restricted as plan assets and are included in investments in the consolidated balance sheet. Upon complete liquidation of the VEBA, future health and dental claims will be paid from WFUHS' general assets (see note 17).

**(r) Integration and Restructuring Costs**

As a result of the Integration Agreement and management's continued efforts toward the creation of an integrated academic medical center, WFUHS has recognized \$0 and \$6,149 for the years ended June 30, 2015 and 2014, respectively, in associated integration and restructuring costs, which include payments to third parties for assistance with the integration agreement and establishment of an integrated clinical documentation and billing system as well as the recognition of termination benefits related to a reduction in force. Given the nature of these costs, the integration and restructuring costs have been reported as a nonoperating expense in the consolidated statement of activities.



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**(t) Use of Estimates**

The University prepares its consolidated financial statements in accordance with GAAP that requires management to make estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying amount of land, buildings, and equipment, and the valuation of nonreadily marketable investments, investments in real estate, allowances for receivables, third-party payer settlements, AROs, professional liabilities, interest rate swap obligations and obligations related to employee benefits. Actual results could differ from those estimates.

**(u) Income Taxes**

The University is a tax-exempt organization as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and is generally exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. Accordingly, no provision for income taxes is made in the consolidated financial statements. If applicable, unrelated business income is reported by all member and subsidiary organizations on IRS Form 990-T. Fiscal years ending on or after June 30, 2012 remain subject to examination by federal and state tax authorities. The University has evaluated uncertain tax positions for the years ended June 30, 2015 and 2014, including a quantification of tax risks in areas such as unrelated business income and taxation of its for-profit subsidiaries. This evaluation did not identify any material items that effect the consolidated financial statements for the years ended June 30, 2015 and 2014.

**(v) Reclassifications**

Certain amounts previously reported in the 2014 consolidated financial statements have been reclassified to conform to the 2015 presentation. Such reclassifications have no effect on total assets, liabilities or net assets or operating, investing or financing cash flows as previously reported.

**(w) Comparative Financial Information**

The consolidated financial statements include certain prior year information for comparative purposes, which does not include sufficient detail to constitute a presentation in conformity with GAAP. Accordingly, such information should be read in conjunction with the University's consolidated financial statements for the year ended June 30, 2014 from which this information was derived.

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**(2) Accounts Receivable**

The following is an analysis of accounts receivable at June 30, 2015 and 2014:

	2015			2014 Total
	Reynolda Campus	WFUHS	Total	
Accounts receivable	\$ 6,376	69,593	75,969	44,575
Grants receivable	2,790	34,980	37,770	36,995
Royalties receivable	—	—	—	275,465
Total accounts receivable	9,166	104,573	113,739	357,035
Less allowance for bad debts	(548)	(807)	(1,355)	(1,212)
Accounts receivable, net	\$ 8,618	103,766	112,384	355,823

In fiscal year 2014, WFUHS reached a settlement agreement with Kinetic Concepts, Inc. (KCI) that resolves a patent dispute between the two organizations over the Negative Pressure Wound Therapy technology. Under the terms of the settlement, KCI agreed to pay retrospective U.S. patent royalties over a four-year period of \$280 million to WFUHS to resolve all disputes between WFUHS and KCI. This settlement amount is included in accounts receivable net of the estimated present value of future cash flows and in other sources in the consolidated statement of activities at June 30, 2014. The receivable balance includes the inventor's share, which represents 50% of the settlement amount. The corresponding liability for amounts due to the inventors is included in other liabilities in the consolidated balance sheet and in other operating expenses in the consolidated statement of activities at June 30, 2014. During the current fiscal year, WFUHS sold the 2016 and 2017 prospective settlement payments to a third party. Pursuant to the agreement, WFUHS received \$102.4 million (net of fees), which is reflected in the reduction of the royalty received in the consolidated balance sheet.

**(3) Patient Revenue and Patient Receivables**

Net patient service revenue is recorded when patient services are performed at the estimated net realizable amounts from patients, third-party payers, and others for services rendered. WFUHS recognizes patient service revenue associated with services provided to patients who have third-party coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, WFUHS recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated or provided by policy). On the basis of historical experience, a significant portion of WFUHS' uninsured patients will be unable or unwilling to pay for the services provided. Thus, WFUHS records a significant provision for bad debts related to uninsured patients in the period the services

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are provided. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the period from these major payer sources, is as follows:

	WFUHS	
	2015	2014
Third-party payers	\$ 429,156	348,977
Self-pay	15,414	70,694
Provision for bad debts	(15,826)	(52,220)
Patient revenue, net	\$ 428,744	367,451

WFUHS has agreements with third-party payers that provide for payments to WFUHS at amounts different from its established rates. Payment arrangements with nongovernmental payers are a negotiated percentage increase to the Medicare fee schedule allowable. Under the Medicare and Medicaid programs, WFUHS is entitled to reimbursement for billed current procedural terminology (CPT) codes at fee schedule rates determined by federal and state governments. Differences between established billing rates and reimbursements from these programs are recorded as contractual adjustments to arrive at net patient service revenue.

Patient receivables are reduced by an allowance for doubtful accounts. In evaluating the collectibility of patient receivables, WFUHS analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, WFUHS analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (e.g., for expected uncollectible deductibles and copayments on accounts for which the third-party payer has not yet paid, or for payers who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), WFUHS records a provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Subsequent to the implementation of a new patient accounting system, WFUHS experienced revenue cycle and billing disruptions that led to growing patient receivable balances along with corresponding cash collections not being realized. As a result of this experience, WFUHS recognized an unfavorable \$21,000 change in its allowance estimates to accurately reflect the realization of the outstanding patient receivables. This change in estimate was reflected as a reduction to patient service revenue in the accompanying consolidated statement of activities for the year ended June 30, 2014.

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Patient receivables are recorded net of allowance for contractual adjustments and uncollectible accounts of \$71,693 and \$76,771, respectively, at June 30, 2015 and \$123,761 and \$49,294, respectively, at June 30, 2014.

WFUHS' allowance for doubtful accounts for self-pay patients increased from 86 percent of self-pay accounts receivable at June 30, 2014 to 91 percent of self-pay accounts receivable at June 30, 2015. In addition, WFUHS' self-pay allowances and expenses (which include charity care charges foregone and bad debt expense) decreased \$69,367 from \$95,796 for fiscal year 2014 to \$26,429 for fiscal year 2015. WFUHS maintains an allowance for doubtful accounts for patient residuals associated with third-party payors. The allowance was \$24,322 and \$26,158 at June 30, 2015 and 2014, respectively.

#### Concentration of Credit Risk

WFUHS grants credit without collateral to its patients, most of whom are insured under third-party payer agreements. The mix of receivables from patients and third-party payers was as follows as of June 30:

	2015	2014
Medicare	11%	11%
Medicaid	17	20
Self-pay	29	38
Other	43	31
	100%	100%

#### (4) Contributions Receivable

The following is an analysis of the maturities of the University's contributions receivable at June 30, 2015 and 2014:

	2015			2014
	Reynolda Campus	WFUHS	Total	
One year or less	\$ 27,131	7,692	34,823	26,684
Between one and five years	50,594	17,278	67,872	51,045
More than five years	104,542	799	105,341	96,107
Gross contributions receivable	182,267	25,769	208,036	173,836
Less estimated uncollectible amounts	(6,562)	(1,228)	(7,790)	(6,171)
Less discount to present value	(61,398)	(1,348)	(62,746)	(60,086)
Contributions receivable, net	\$ 114,307	23,193	137,500	107,579

Contributions receivable are discounted at a rate commensurate with the scheduled timing of receipt. Such amounts outstanding as of June 30, 2015, and 2014, were discounted at rates ranging from 2.62% to 2.88% for WFU, respectively, and 1.91% to 2.26% for WFUHS, respectively.

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Contributions receivable, net for Reynolda Campus included perpetual commitments from a foundation with a long-standing history of support to the University. These long-term unconditional promises to give represented 31% and 34% of Reynolda Campus' net contributions receivable as of June 30, 2015 and 2014, respectively.

#### (5) Notes Receivable

The following is an analysis of notes receivable at June 30, 2015 and 2014:

	2015			2014 Total
	Reynolda Campus	WFUHS	Total	
Student loans receivable	\$ 19,026	862	19,888	20,214
Other notes receivable	3,637	928	4,565	6,006
Total notes receivable	22,663	1,790	24,453	26,220
Less estimated uncollectible amounts	(350)	(958)	(1,308)	(1,996)
Notes receivable, net	\$ 22,313	832	23,145	24,224

The University makes uncollateralized loans to students based on financial need. Student loans are funded through Federal government loan programs or institutional resources. At June 30, 2015 and 2014, student loans receivable consisted of Federal loan programs of \$18,205 and \$18,467, respectively, and institutional loan programs of \$1,683 and \$1,747, respectively. The University participates in the Perkins federal revolving loan program. The availability of funds for loans under the program is dependent on reimbursements to the pool from repayments on outstanding loans. Funds advanced by the Federal government of \$9,582 and \$9,688 at June 30, 2015 and 2014, respectively, are ultimately refundable to the federal government and are reported as government grants refundable on the consolidated balance sheet. Outstanding loans canceled under the program result in a reduction of the funds available for loan and a decrease in the liability to the federal government. Amounts due under the Perkins loan program are guaranteed by the federal government and, therefore, no allowance for uncollectible amounts is reported under the program. Allowances for uncollectible institutional student loans are based on prior collection experience and current economic factors, which, in management's judgment, could influence the ability of loan recipients to repay the amounts per the loan terms. Institutional student loan balances are written off only when they are deemed to be permanently uncollectible. At June 30, 2015 and 2014, the allowance for uncollectible institutional student loan amounts was \$350 and \$423, respectively.

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#### (6) Investments

Investments at June 30, 2015 and 2014 consist of the following:

	<b>2015</b>	<b>2014</b>
Short-term investments <sup>(a)</sup>	\$ 129,882	57,983
Absolute return <sup>(b)</sup>	273,061	300,657
Commodities: <sup>(c)</sup>	135,804	90,034
Fixed income: <sup>(d)</sup>		
Domestic	277,821	381,155
International	88,185	80,531
Private equity <sup>(e)</sup>	106,125	106,233
Public equity: <sup>(f)</sup>		
Domestic	261,143	190,591
International	157,025	164,883
Real estate: <sup>(g)</sup>	56,587	108,608
Beneficial interest in perpetual trusts and assets held by others <sup>(h)</sup>	25,837	27,269
Other	116,795	85,303
<b>Total investments</b>	<b>\$ 1,628,265</b>	<b>1,593,247</b>

- (a) Includes short duration U.S. Treasury debt securities and other short-term, higher quality debt securities, cash and money market mutual funds.
- (b) Includes investments in hedge funds and hedge fund-of-funds that invest both long and short on a global basis primarily in: equity securities (common stocks), credit securities (both investment grade and noninvestment grade), commodities, and currencies. In aggregate, the expectation is that the returns of this segment should not be highly correlated to the broad equity market.
- (c) Includes primarily illiquid investments in timberland, oil and gas properties, and water rights and entitlements held through limited partnership interests. While many of the investments are U.S. focused, some are more global. The category also includes more liquid allocations made to commodity (precious metals, industrial materials, and energy) mutual funds.
- (d) Includes long only, hedge strategies, and illiquid investments in various fixed income strategies (both U.S. and non-U.S.) including: investment grade securities, noninvestment grade securities, mortgage backed securities, asset backed securities, Treasury Inflation Protected Securities (TIPS), distressed debt, senior loans, and bank loans. The long only position also includes mutual funds that have daily liquidity in U.S. and non-U.S. fixed income markets.
- (e) Includes illiquid investments primarily in buyout, growth equity, and venture capital (both U.S. and non-U.S.) held through limited partnership interests.

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- (f) Includes investments primarily in U.S. and non-U.S. common stocks (including emerging markets) as well as funds that invest in U.S. and non-U.S. common stocks (including emerging markets), mutual funds, and exchange traded funds. While most of the assets are invested long only, some assets are invested on a hedged basis (both long and short).
- (g) Includes illiquid investments in commercial real estate, residential real estate, and farmland held through limited partnership interests. While many of the investments are U.S. focused, some are more global.
- (h) Includes trusts and certain other assets held and administered by others which the University has an unconditional right to receive all or a portion of the specified cash flows.

In addition to the long-term pool, the University also manages other investment portfolios. Generally, these portfolios are invested in mutual funds, U.S. Treasury debt securities, and fixed income securities with daily liquidity. Each portfolio's asset allocation is customized based upon the return and risk objectives and distribution requirements of the portfolio.

The components of total investment return as reflected in the consolidated statement of activities are as follows:

	<b>2015</b>	<b>2014</b>
Investment income, net	\$ 39,666	37,426
Realized gains, net	41,248	33,705
Changes in unrealized appreciation (depreciation)	(54,843)	62,685
Total investment return	26,071	133,816
Endowment appropriation designated for current operations	(62,258)	(63,103)
Other investment returns designated for current operations	(2,330)	—
Investment return in excess of (less than) amounts designated for current operations	\$ (38,517)	70,713

Investment income has been reduced by investment fees of \$7,884 and \$12,846 in 2015 and 2014, respectively.

#### **(7) Endowment**

The University's pooled endowment consists of approximately 1,500 individual funds established for a variety of purposes including both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions. Gift annuities, beneficial interest in perpetual trusts and assets held by others, and contributions receivable are not considered components of the endowment.

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The Board of Trustees has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as allowing the University to appropriate for expenditure or accumulate so much of an endowment fund as the University determines is prudent for the uses, benefits, purposes, and duration for which the endowment fund is established, subject to the intent of the donor as expressed in the gift instrument. As a result of this interpretation, the University's policy is to report as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

The portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the University in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Board of Trustees considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purposes of the University and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the University
7. The investment policies of the University

The University has adopted investment and spending policies for endowment assets that support the objectives of optimizing long-term returns and providing a sustainable level of endowment income distribution to support the University's activities through the annual operating budget while preserving the real (inflation adjusted) purchasing power of the endowment. The University's primary investment objective is to maximize total return within reasonable and prudent levels of risk while maintaining sufficient liquidity to meet disbursement needs. The endowment spending rate for the years ended June 30, 2015 and 2014 was 5.3%, calculated as a percentage of the average of the previous three-year semiannual moving market value per unit and subject to a 10% maximum annual growth or decline in per-unit spending.

The portfolio is constructed on a foundation of modern portfolio theory and strategic asset allocation. The University diversifies its investments among various asset classes incorporating multiple strategies and investment advisors to help manage risk. Major investment decisions are approved by the Board's Investment Policy Committee, which oversees the University's investments in accordance with established guidelines. Management and investment decisions are not made in isolation, but in the context of the portfolio of investments as a whole and as part of the overall investment strategy.



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The University invests a substantial portion of these assets (97%) in Verger Capital Fund, compared to 39.4% in 2014. The University has established three individual unitized endowment pools for WFU, Reynolda House, and WFUHS. The internal long-term pools are reported on a fair value basis, with each individual fund subscribing to or disposing of units on the basis of the fair value per unit at the beginning of each quarter within which the transaction took place. At June 30, 2015, Reynolda Campus held units of 14,241,100, WFUHS held 10,508,099 units and Reynolda House held units of 628,863 in these long-term pools with a fair value of \$49.55, \$49.35 and \$49.51 per unit, respectively. At June 30, 2014, the University maintained one unitized long-term pool holding a total of 23,249,587 units with a fair value of \$51.11 per unit.

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the value of the original gift. Deficiencies of this nature are reported in unrestricted net assets as follows: Reynolda Campus and WFUHS, respectively, were \$6,551 and \$1,083 as of June 30, 2015; and \$5,394 and \$756 as of June 30, 2014.

Endowment net assets consist of the following at June 30, 2015 and 2014:

	2015			Total	2014 Total
	Unrestricted	Temporarily restricted	Permanently restricted		
Reynolda Campus:					
Donor-restricted endowment funds	\$ (6,551)	233,847	248,439	475,735	469,124
Board-designated endowment funds	237,253	—	—	237,253	244,610
Endowment net assets	230,702	233,847	248,439	712,988	713,734
WFUHS:					
Donor-restricted endowment funds	(1,083)	36,357	129,503	164,777	162,003
Board-designated endowment funds	274,006	13,985	1,644	289,635	272,289
Endowment net assets	272,923	50,342	131,147	454,412	434,292
Total endowment net assets	\$ 503,625	284,189	379,586	1,167,400	1,148,026

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Changes in endowment net assets for the years ended June 30, 2015 and 2014 are as follows:

	2015			Total	2014 Total
	Unrestricted	Temporarily restricted	Permanently restricted		
<b>Reynolda Campus:</b>					
Beginning balance	\$ 239,216	245,140	229,378	713,734	660,363
Investment return:					
Investment income net of fees	806	1,666	23	2,495	4,589
Net appreciation	1,223	5,497	424	7,144	58,317
Total investment return	2,029	7,163	447	9,639	62,906
Contributions	35	112	17,881	18,028	18,754
Appropriation for expenditure	(11,178)	(18,568)	—	(29,746)	(28,198)
Transfers due to donor redesignations	—	—	(35)	(35)	—
Transfers to (from) Board-designated funds	600	—	768	1,368	(91)
Ending balance	\$ 230,702	233,847	248,439	712,988	713,734
<b>WFUHS:</b>					
Beginning balance	\$ 257,858	53,241	123,193	434,292	401,275
Investment return:					
Investment income net of fees	4,077	2,353	206	6,636	13,828
Net appreciation	301	301	9	611	22,683
Total investment return	4,378	2,654	215	7,247	36,511
Contributions	3,102	—	7,739	10,841	8,172
Appropriation for expenditure	(12,852)	(5,406)	—	(18,258)	(14,166)
Transfers to (from) Board-designated funds	20,437	—	—	20,437	2,500
Ending balance	\$ 272,923	50,489	131,147	454,559	434,292

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#### (8) Fair Values of Assets and Liabilities

The following table summarizes the valuation of the University's assets and liabilities within the fair value hierarchy levels as of June 30, 2015:

	2015				2014
	Level 1	Level 2	Level 3	Total	Total
Financial assets:					
Cash and cash equivalents	\$ 210,534	—	—	210,534	51,439
Investments:					
Short-term investments	129,882	—	—	129,882	57,983
Absolute return	2,260	430	—	2,690	137,163
Commodities	30,052	—	—	30,052	19,047
Fixed income:					
Domestic	221,906	27,101	16,118	265,125	350,121
International	12,876	27,503	—	40,379	50,177
Public equity:					
Domestic	208,890	3,525	295	212,710	126,451
International	86,815	817	—	87,632	131,160
Real estate	5,133	—	—	5,133	48,867
Beneficial interest in perpetual trusts and assets held by others					
Other	—	—	25,837	25,837	27,269
Other	3,885	53,036	—	56,921	7,623
Deposits with bond trustee	—	—	—	—	25
Assets valued at NAV	—	—	—	771,904	637,386
Total assets	<u>\$ 912,233</u>	<u>112,412</u>	<u>42,250</u>	<u>1,838,799</u>	<u>1,644,711</u>
Financial liabilities:					
Other liabilities and deferrals:					
Interest rate swap agreements	\$ —	12,490	—	12,490	20,012
Annuities payable	—	27,973	—	27,973	26,187
Total liabilities	<u>\$ —</u>	<u>40,463</u>	<u>—</u>	<u>40,463</u>	<u>46,199</u>

The classification of investments in the fair value hierarchy is not necessarily an indication of the risks or liquidity of each investment's underlying assets and liabilities. In general, for Level 2 and Level 3 investments, the University utilizes the investment manager to provide a valuation estimate based on disclosed techniques and processes, which have been reviewed for propriety and consistency with consideration given to type and investment strategy.

As stated previously, the University adopted ASU 2015-07 and has excluded from the levels above the investments measured using net asset value per share under the practical expedient. These shares or units are generally reported at the net asset value reported by the fund managers.

The University's policy is to recognize transfers into and out of Levels 1, 2, and 3 as of the end of the year or when a change in level becomes known. There were no significant transfers between Level 1 and Level 2

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securities during the year ended June 30, 2015 other than the removal of investments at NAV from the hierarchy.

Fair value for LIBOR-based interest rate swaps is determined using a relative price approach, by discounting the future expected cash flows at the market discount rate. For the variable leg of a swap, the expected cash flows are based on implied market forward rates for the appropriate underlying index. A credit value adjustment is applied to the total market value of the swap and quantifies the default risk of a counterparty using a default probability assumption based on the counterparty's credit default swap pricing at year-end.

Obligations under split-interest agreements reported in annuities payable were discounted at a rate that is equivalent to the University's nonexempt borrowing rate of 3.71% and 3.87% at June 30, 2015 and 2014, respectively.

The following table presents the reconciliation of Level 3 assets measured at fair value for the year ended June 30, 2015. Both observable and unobservable inputs may be used to determine the fair value of positions that the University has classified as Level 3. The University has excluded the impact of retrospective application of ASU 2015-07 for the table below.

	<u>Balance as of June 30, 2014</u>	<u>Total realized and unrealized gains (losses)</u>	<u>Purchases</u>	<u>Sales</u>	<u>Net transfers out of Level 3</u>	<u>Balance as of June 30, 2015</u>
Investments:						
Fixed income:						
Domestic	\$ 12,334	(1,087)	8,120	(3,249)	—	16,118
Public equity:						
Domestic	70	(525)	750	—	—	295
Interests in perpetual trusts and assets held by others	<u>26,576</u>	<u>(497)</u>	<u>406</u>	<u>(648)</u>		<u>25,837</u>
Total assets	<u>\$ 38,980</u>	<u>(2,109)</u>	<u>9,276</u>	<u>(3,897)</u>	<u>—</u>	<u>42,250</u>

The University's aggregate unfunded private capital commitments are approximately \$138,300, or 8.50%, of total investments at June 30, 2015. Of these commitments, \$63,300 relates to private equity, \$5,000 relates to real estate, \$21,500 relates to commodities, \$22,500 relates to absolute return, \$1,200 relates to public equities and \$24,800 relates to fixed income. These commitments are expected to be called over a multiyear time frame. The University believes it has adequate liquidity and funding sources to meet these obligations.

Private investments are generally made through limited partnership agreements where the University is normally one of many limited partners. Under the terms of such agreements, the University is required to provide funding, up to the total amount committed by the University, when capital calls are made by fund managers. These partnerships have a stated maturity date, but can provide for annual extensions for the purpose of disposing remaining portfolio positions and returning capital to investors. Alternatively, the fund may dispose of all portfolio investments and return all capital to investors before the stated maturity date. While the timing and amount of future capital calls and distributions in any particular year are inherently

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uncertain, the University takes these factors into consideration when allocating to private investments and believes that it has adequate liquidity to meet its obligations.

Investment liquidity as of June 30, 2015 is aggregated below based on redemption or sale period:

Daily, with 1 – 5 days notice	\$	887,285
Monthly, with 5 – 15 days notice		124,455
Quarterly, with 5 – 95 days notice		63,510
Semi-annually, with 45 – 95 days notice		48,865
Yearly, with 60 – 180 days notice		86,071
Liquidity within 2 years, with 60 – 95 days notice		81,509
Illiquid		<u>336,570</u>
Total as of June 30, 2015	\$	<u><u>1,628,265</u></u>

#### (9) Land, Buildings, and Equipment

Land, buildings, and equipment are summarized as follows at June 30, 2015 and 2014:

	<u>Reynolda Campus</u>	<u>WFUHS</u>	<u>Total</u>	<u>2014 Total</u>
Land and improvements	\$ 26,862	95,730	122,592	122,601
Buildings and other improvements	622,560	387,406	1,009,966	1,005,564
Equipment and furnishings	105,559	185,736	291,295	279,619
Construction in progress	<u>38,387</u>	<u>16,267</u>	<u>54,654</u>	<u>23,011</u>
	793,368	685,139	1,478,507	1,430,795
Less accumulated depreciation	<u>(337,421)</u>	<u>(388,344)</u>	<u>(725,765)</u>	<u>(674,356)</u>
	<u>\$ 455,947</u>	<u>296,795</u>	<u>752,742</u>	<u>756,439</u>

Total depreciation expense on buildings, improvements, equipment, and furnishings was \$63,321 and \$61,187 for the years ended June 30, 2015 and 2014, respectively.

The University reviews property, plant and equipment for recoverability whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The University recognizes an impairment loss only if the carrying amount of a long-lived asset is not recoverable and exceeds its fair value. The carrying amount of a long-lived asset is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset. During 2015, WFUHS recorded an impairment loss of \$2,789 related to property, plant and equipment (Level 3).

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The University's policy is to capitalize interest cost incurred on debt during the construction of major projects exceeding one year. Interest cost of \$495 and \$1,350 was capitalized in the years ended June 30, 2015 and 2014, respectively.

The liabilities associated with AROs for the years ended June 30, 2015 and 2014, respectively, were \$9,282 and \$14,643 for Reynolda Campus, and \$2,695 and \$3,254 for WFUHS. These liabilities are reported in other liabilities and deferrals on the consolidated balance sheet.

#### (10) Notes, Capital Leases, and Bonds Payable

Notes, capital leases, and bonds payable at June 30, 2015 and 2014 consist of the following:

<u>Reynolda Campus</u>	<u>Years to nominal maturity</u>	<u>Interest rate at June 30, 2015</u>		<u>2015</u>	<u>2014</u>
Notes payable and capital leases:					
2013 Construction loan	2	0.64	variable	9,646	2,127
Promissory note	4	4.00	fixed	500	725
Capital leases	5	0.81 to 7.5	fixed	<u>6,262</u>	<u>3,053</u>
Total notes payable and capital leases				<u>16,408</u>	<u>5,905</u>
Bonds payable:					
2004 Series A tax-exempt	<1 to 5	0.06%	variable	23,475	26,290
2004 Series B tax-exempt	<1 to 5	0.06%	variable	10,830	14,210
2009 Series serial tax-exempt	25	4.00 to 5.00	fixed	49,430	49,430
2009 Series term tax-exempt	24	5.00	fixed	60,570	60,570
2012 Series serial taxable	29	2.6 to 3.1	fixed	20,425	20,425
2012 Series term taxable	29	3.45 to 3.7	fixed	104,575	104,575
Unamortized bond premium				2,090	2,177
Unamortized bond issuance costs				<u>(1,978)</u>	<u>(2,092)</u>
Total bonds payable				<u>269,417</u>	<u>275,585</u>
Total notes payable, capital leases, and bonds payable				<u>\$ 285,825</u>	<u>281,490</u>

Reynolda Campus has a two-year construction loan financing agreement with Branch Banking and Trust Company that permits the University to borrow up to \$100,000, bearing interest at LIBOR plus 0.45% to 0.60%. The loan agreement requires annual reviews on the December 31 anniversary date with interest payable quarterly.

Reynolda Campus has outstanding \$34,305 of tax-exempt North Carolina Facilities Finance Agency Revenue Bonds, Series 2004A and Series 2004B. The obligations of the University are evidenced by a loan agreement dated December 1, 2004, by and between the University and Branch Banking and Trust Company, as trustee. The Series 2004 tax-exempt bonds are due annually through 2020 in varying amounts from \$6,405 to \$7,340. The interest rate on the bonds is determined weekly, and at the option of the University may be

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converted to a fixed rate. The University's obligation under the loan agreement is an unsecured, unconditional obligation.

The North Carolina Facilities Finance Agency Revenue Bonds, Series 2009, are evidenced by a loan agreement dated May 1, 2009, by and between the University and Branch Banking and Trust Company, as trustee. The Series 2009 tax-exempt bonds have final maturities of January 1, 2039 for the serial bonds and January 1, 2038 for the term bonds. The 2009 bonds maturing on January 1, 2038 are subject to mandatory redemption through 2038 in increasing annual amounts of \$7,410 to \$10,005. Interest is payable each January 1 and July 1. The University's obligation under the loan agreement is an unsecured, unconditional obligation.

The Series 2012 taxable bonds are evidenced by a loan agreement dated August 2, 2012, by and between the University and Branch Banking and Trust Company, as trustee. The Series 2012 taxable bonds have final maturities of January 15, 2027 for the serial bonds and January 15, 2042 for the term bonds. The 2012 bonds maturing on January 15, 2032 and 2042 are subject to mandatory sinking fund redemptions through 2032 and 2042 in increasing annual amounts of \$5,445 to \$6,205 and \$6,405 to \$8,830, respectively. Interest is payable each January 15 and July 15. The University's obligation under the loan agreement is an unsecured, unconditional obligation.

WFUHS	Years to nominal maturity	Interest rate at June 30, 2015		2015	2014
Notes payable and capital leases:					
Line of credit	>1	Libor plus 0.6%	variable	\$ 13,039	—
Loan agreement	<1 to 10	Libor plus 0.65%	variable	15,678	17,679
Promissory note	2			160	240
Promissory note	7		fixed	955	1,081
Capital leases	3	4.07%–5.42%	fixed	—	107
Total notes payable and capital leases				<u>29,832</u>	<u>19,107</u>
Bonds payable:					
Series 2012 B	<1 to 20	2.00%–5.00%	fixed	105,750	109,220
Series 2012 C	<1 to 20	0.74%	variable	54,810	56,955
Unamortized bond premium				14,395	15,177
Unamortized bond issuance costs				<u>(1,260)</u>	<u>(1,328)</u>
Total bonds payable				<u>173,695</u>	<u>180,024</u>
Total notes payable, capital leases, and bonds payable				<u>\$ 203,527</u>	<u>199,131</u>

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Effective March 26, 2011, NCBH, WFUHS, and WFUBMC formed a single obligated group (Obligated Group) under the existing NCBH MTI. New obligations were issued to WFUHS obligation holders under the NCBH MTI. In addition, substantially all of the subsidiaries of NCBH, WFUHS, and WFUHS were included in the single credit group as Designated Members (Combined Group). Under the new credit structure, each member of the Obligated Group is jointly and severally liable for all debt and other obligations that are evidenced and secured under the MTI.

Bonds issued under the MTI are payable solely from the Obligated Group's revenues (as defined by the MTI). Additionally, the Combined Group must remain compliant with certain covenants and restrictions required by the MTI and loan agreements underlying the bonds. The Combined Group is subject to covenants under the MTI containing restrictions or limitations with respect to indebtedness, property encumbrance, consolidation or merger or transfer of assets. In addition, the Combined Group has agreed that it will not create any lien upon its property, accounts, or revenue now owned or hereafter acquired other than "permitted liens" as described in the MTI. WFUHS believes it is in compliance with such covenants and restrictions as of June 30, 2015. As of June 30, 2015, WFUHS is jointly and severally liable for \$499,980 of bonds payable borrowed by the other members of the Obligated Group and for \$89,000 under WFUBMC's line of credit. Because WFUHS does not expect to fund repayment of any of the amounts attributed to the other members of the Obligated Group under the MTI, no portion of these amounts meets the criteria for liability recognition in the accompanying consolidated financial statements.

The Series 2012 Revenue Bonds represent bonds issued by Wake Forest Baptist Obligated Group, representing funds borrowed by the entities pursuant to loan agreements with the North Carolina Medical Care Commission (NCMCC). As a conduit issuer, the NCMCC loans the debt proceeds to the borrower and the bonds are issued by the NCMCC under a MTI structure. The MTI provides the flexibility for multiple parties to participate in the debt issuances as part of an obligated group.

The Series 2012B bonds mature in full in fiscal year 2034. The fixed rate instruments bear interest at fixed coupon rates ranging from 2.00% to 5.00%. Per the bond agreements, the principal and sinking fund payments on the bonds are due on December 1 of each year beginning in 2015 and in increasing annual amounts of \$3,385 to \$7,000.

The Series 2012C bonds mature in full in fiscal year 2034. The bonds were issued in the Index Floating Rate Mode and bear interest at an Index Floating Rate based on the SIFMA Index plus a spread of 0.74%. At the option of WFUHS, the bonds may be converted to various interest rate modes. Per the bond agreements, the principal and sinking fund payments on the bonds are due on December 1 of each year beginning in 2015 and in increasing annual amounts of \$2,090 to \$4,825.

WFUHS entered into an unsecured, taxable line of credit agreement in the amount of \$125,000 to provide for the working capital needs of NCBH, WFUHS, and the Medical Center, all Borrowers under the credit facility. This line of credit refinanced the previously held \$160,000 line of credit. The line of credit is due on June 23, 2018 and bears interest at the one-month LIBOR plus 0.60%.



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WFUHS entered a loan agreement during fiscal year 2013, with a variable interest rate based upon the one-month LIBOR plus a premium of 0.65% for \$20,214 to refinance two previously outstanding fixed rate notes. Fixed principal payments and accrued interest are due monthly with a final maturity date of April 1, 2023. This taxable loan is guaranteed by both NCBH and WFUBMC.

Aggregate annual maturities of notes, capital leases, and bonds payable for each of the five fiscal years subsequent to June 30, 2015 and thereafter are as follows:

	<u>Reynolda Campus</u>	<u>WFUHS</u>	<u>Total</u>
2016	\$ 8,201	8,094	16,295
2017	18,172	21,239	39,411
2018	8,104	8,335	16,439
2019	8,134	8,575	16,709
2020	8,031	8,845	16,876
In total thereafter	<u>235,183</u>	<u>148,439</u>	<u>383,622</u>
	<u>\$ 285,825</u>	<u>203,527</u>	<u>489,352</u>

#### (11) Interest Rate Swap Agreements

To manage the fixed/variable allocation of its debt portfolio, including hedging exposure to increasing interest expense from variable rate debt, the University utilizes interest rate swap agreements. The University has only limited involvement with derivative instruments and does not use them for trading purposes.

Parties to interest rate swap agreements are subject to market risk for changes in interest rates as well as credit loss in the event of nonperformance by the counterparty. To minimize this exposure, the University verifies that the counterparties for these swap transactions are major financial institutions that meet the University's criteria for financial stability and creditworthiness. Additionally, the University is exposed to tax basis risk since a change in tax rate environments will change the level of correlation between the interest rate payments made on the variable rate bonds and the percentage of LIBOR payments being received from the counterparties.

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The following table summarizes the general terms for each of the University's swap agreements:

	<b>Reynolda Campus</b>		<b>WFUHS</b>
	<b>November 2006 interest rate swap</b>	<b>October 2008 interest rate swap</b>	<b>August 2002 interest rate swap</b>
Notional amount	\$ 23,475	50,000	24,042
Effective date	November 6, 2006	October 1, 2008	August 20, 2002
Maturity date	January 1, 2020	January 1, 2038	July 1, 2034
Rate received	67% of one-month LIBOR	67% of one-month LIBOR	67% of one-month LIBOR
Rate paid	3.38%	3.61%	3.67%
Collateral provisions	None	100% liability if > \$20,000	100% asset/liability – \$250 min
Settlement frequency	Monthly	Monthly	Weekly

The University records all interest rate swap agreements in other liabilities and deferrals on the consolidated balance sheet at their respective fair values. The fair value of the interest rate swap agreements is the estimated amount the University would pay to terminate the swap agreements at the reporting date, taking into account current forward interest rates and the current forward creditworthiness of the swap counterparties. All changes in fair value are reflected as a gain or loss in nonoperating activities in the consolidated statement of activities. Periodic net cash settlement amounts with counterparties are accounted for as adjustments to interest expense on the related debt and collateral to support the swaps is included in investments on the consolidated balance sheet. Collateral held by counterparties at June 30, 2015 and 2014, respectively, was \$0 and \$0 for Reynolda Campus, and \$4,890 and \$4,340 for WFUHS.

The related financial information on each of these instruments is as follows:

	<b>2015</b>		<b>2014</b>	
	<b>Fair value</b>	<b>Gain (Loss)</b>	<b>Fair value</b>	<b>Gain (Loss)</b>
<b>Reynolda Campus:</b>				
November 2006 interest rate swap	\$ (1,843)	495	(2,338)	545
October 2008 interest rate swap	(15,450)	(2,330)	(13,120)	(525)
Total	(17,293)	(1,835)	(15,458)	20
<b>WFUHS:</b>				
August 2002 interest rate swap	4,803	(249)	(4,554)	(2)
Total	4,803	(249)	(4,554)	(2)
Grand total	\$ (12,490)	(2,084)	(20,012)	18

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As of June 30, 2015, the University's adjusted debt portfolio, after taking into account the aforementioned swap agreements, was 100% fixed rate for Reynolda Campus, and approximately 69% fixed rate for WFUHS.

**(12) Net Assets**

Temporarily restricted net assets are composed of the following at June 30, 2015 and 2014:

	<b>2015</b>			<b>2014 Total</b>
	<b>Reynolda Campus</b>	<b>WFUHS</b>	<b>Total</b>	
Gifts and pledges	\$ 143,399	18,897	162,296	124,019
Donor-restricted endowments	233,847	50,342	284,189	298,381
	<u>\$ 377,246</u>	<u>69,239</u>	<u>446,485</u>	<u>422,400</u>

Such temporarily restricted net assets are available for the following purposes as of June 30, 2015 and 2014:

	<b>2015</b>			<b>2014 Total</b>
	<b>Reynolda Campus</b>	<b>WFUHS</b>	<b>Total</b>	
Student scholarships	\$ 199,671	4,998	204,669	172,343
Instruction and research	64,727	39,175	103,902	118,873
Academic support	40,585	8,614	49,199	59,548
Subsequent period operations, capital, and other	72,263	16,452	88,715	71,636
	<u>\$ 377,246</u>	<u>69,239</u>	<u>446,485</u>	<u>422,400</u>

Permanently restricted net assets are composed of the following at June 30, 2015 and 2014:

	<b>2015</b>			<b>2014 Total</b>
	<b>Reynolda Campus</b>	<b>WFUHS</b>	<b>Total</b>	
Donor-restricted endowments	\$ 248,439	131,147	379,586	352,571
Gifts and pledges	22,274	4,692	26,966	19,171
Student loan funds	—	4,874	4,874	5,988
Interests in perpetual trusts and assets held by others	4,907	14,349	19,256	20,064
Annuity and other split-interest agreements	9,150	2,243	11,393	13,709
	<u>\$ 284,770</u>	<u>157,305</u>	<u>442,075</u>	<u>411,503</u>

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The future return on the following donor-restricted endowments is restricted for the following purposes as of June 30, 2015 and 2014:

	2015			2014 Total
	Reynolda Campus	WFUHS	Total	
Student scholarships	\$ 166,139	37,127	203,266	180,402
Instruction and research	53,091	86,367	139,458	127,711
Academic support	22,129	7,653	29,782	37,648
Subsequent period operations and other	7,080	—	7,080	6,810
	\$ 248,439	131,147	379,586	352,571

### (13) Functional Expenses

Expenses are reported in the consolidated statement of activities in natural categories. Functional expenses for the years ended June 30, 2015 and 2014 are categorized as follows:

	2015			2014 Total
	Reynolda Campus	WFUHS	Total	
Instruction and departmental research	\$ 125,910	77,418	203,328	302,853
Patient services	—	495,052	495,052	482,191
Sponsored research, training, and other programs	9,174	188,081	197,255	191,560
Organized activities	2,332	—	2,332	2,094
Academic support	31,895	12,559	44,454	40,504
Libraries	14,133	3,486	17,619	15,680
Student services	27,976	2,166	30,142	31,622
Institutional support	78,190	20,965	99,155	102,248
Auxiliary enterprises	76,742	—	76,742	83,075
Total operating expenses	\$ 366,352	799,727	1,166,079	1,251,827

Functional expenses are reported in categories recommended by the National Association of College and University Business Officers. The expenses are reported in these functional categories after the allocation of plant operation and maintenance expense, depreciation expense, accretion expense, and interest expense. The University's primary program services are instruction, patient services, sponsored research, and organized activities. Expenses reported as academic support, libraries, student services, institutional support, and auxiliary enterprises are incurred in support of these primary program services.

# WAKE FOREST UNIVERSITY

## Notes to Consolidated Financial Statements

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(Dollars in thousands)

Plant operation and maintenance expense, depreciation expense, accretion expense, and interest expense are allocated to program and supporting activities based on a percentage allocation and periodic assessment of facilities usage, for Reynolda Campus and WFUHS, respectively.

### (14) Contingencies and Other Commitments

The University maintains rental properties and has entered into long-term operating lease agreements for this real estate providing for future rental income as follows:

	<u>Reynolda Campus</u>	<u>WFUHS</u>	<u>Total</u>
Year ending June 30:			
2016	\$ 10,060	693	10,753
2017	10,286	487	10,773
2018	10,489	466	10,955
2019	10,697	471	11,168
2020	10,908	—	10,908
	<u>\$ 52,440</u>	<u>2,117</u>	<u>54,557</u>

Total income from real estate was \$10,753 and \$10,123 for Reynolda Campus and \$1,775 and \$1,913 for WFUHS for the years ended June 30, 2015 and 2014, respectively.

The estimated cost to complete construction in progress at June 30, 2015 and 2014, respectively, were \$85,064 and \$21,035 for Reynolda Campus, and \$22,124 and \$2,146 for WFUHS.

Grant awards not yet funded and for which services have not yet been performed are not recorded until services have been performed. At June 30, 2015, such grant awards amounted to \$9,778 and \$212,381 for Reynolda Campus and WFUHS, respectively.

Expenditures and indirect costs related to federal and state grants and contracts are subject to adjustment based upon review by the granting agencies. The amounts, if any, of expenditures, which may be disallowed by the granting agencies cannot be determined at this time, although management expects they will not have a material effect on the University's consolidated financial statements.

The University is self-insured for dental benefits, self-insured or fully insured for retiree medical benefits (depending on retiree benefit elections), and self-insured for active employees receiving medical benefits. The University provides an accrual for actual claims reported but not paid and a provision for incurred but not reported claims based on historical trends. Accrued employee health and dental costs, including estimated claims incurred but not reported, amounted to approximately \$1,050 and \$1,135 at June 30, 2015 and 2014, respectively, for Reynolda Campus and \$5,575 and \$5,185 at June 30, 2015 and 2014, respectively, for WFUHS and are included in other liabilities in the accompanying consolidated balance sheet.

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The estimated liability for self-insurance claims will be significantly affected if current and future claims differ from historical trends. While management monitors reported claims closely and considers potential outcomes as estimated by its actuaries when determining its self-insurance liability accruals, the complexity of the claims, the extended period of time to settle the claims and the wide range of potential outcomes complicate the estimation. In the opinion of management, adequate provision has been made for this related risk.

The University self-insures workers' compensation liability with excess commercial insurance providing per loss and aggregate annual coverage. The University provides an accrual for actual claims reported but not paid and a provision for incurred but not reported claims based on historical trends.

The estimated liability for workers' compensation claims will be significantly affected if current and future claims differ from historical trends. While management monitors reported claims closely and considers potential outcomes as estimated by its actuaries when determining its self-insurance liability accruals, the complexity of the claims, the extended period of time to settle the claims and the wide range of potential outcomes complicate the estimation. In the opinion of management, adequate provision has been made for this related risk.

The University is involved in legal actions arising in the normal course of activities and is subject to periodic audits and inquiries by regulatory agencies. Although the ultimate outcome of such matters is not determinable at this time, management, after taking into consideration advice of legal counsel, believes that the resolutions of pending matters will not have a materially adverse effect, individually or in the aggregate, upon the University's consolidated financial statements.

#### **(15) Sale-Leaseback Agreement**

In 2006, WFUHS entered into a sale-leaseback agreement to sell and lease back certain assets. The initial lease term is 20 years with four renewal options of five years each and the lease is classified as an operating lease. Operating lease payments in each year from 2016 to 2020 are \$7,591, \$7,667, \$7,744, \$7,821 and \$7,899, respectively, and \$56,311 thereafter.

In 2010, WFUHS entered into another sale-leaseback agreement to sell and lease back certain assets. The initial lease term is 16 years with three 5-year renewal options. The lease is classified as an operating lease. Operating lease payments are due monthly and expected payments each year from 2016 to 2020 are \$5,366, \$5,501, \$5,638, \$5,779 and \$5,924, respectively, and \$45,825 thereafter.

WFUHS has a deferred gain related to the sale and leaseback of certain assets. The deferred gain was \$23,073 and \$25,019 for 2015 and 2014, respectively, and is included in other liabilities and deferrals on the consolidated balance sheet.

#### **(16) Retirement Plans**

Substantially all employees of the University are eligible to participate in defined contribution benefit plans. The University contributes a specified percentage of each employee's salary to the plans. Contributions for the years ended June 30, 2015 and 2014, respectively, were \$12,087 and \$11,496 for Reynolda Campus and \$14,603 and \$7,756 for WFUHS.

## WAKE FOREST UNIVERSITY

### Notes to Consolidated Financial Statements

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Reynolda Campus and WFUHS have accrued \$2,888 and \$5,090 at June 30, 2015, respectively, and \$2,493 and \$5,341, respectively, at June 30, 2014 for a liability associated with a defined benefit supplemental executive retirement plan. These liabilities are included in other liabilities and deferrals on the consolidated balance sheet.

#### **(17) Postretirement Benefits**

The University sponsors defined benefit postretirement medical and dental plans that cover all of its full-time employees who elect coverage and satisfy the plans' eligibility requirements when they retire. In addition, Reynolda Campus sponsors a death benefit plan which pays a \$2 benefit for each retiree. To be eligible, retired employees of Reynolda Campus must be at least 62 years of age with ten or more years of service or be at least 65 years of age with five or more years of service.

WFUHS sponsors a defined benefit postretirement medical and dental plan that covers all WFUHS full-time employees who elect coverage and satisfy the plan eligibility requirements when they retire. On June 2, 2011, the Board of WFUHS approved that effective as of January 1, 2012, the defined benefit postretirement plan would be discontinued for most future retirees. The minimum age required for postretirement benefits will increase from 60 to 62. However, the additional requirement of the rule of 75 (age and service) remains unchanged. All current retirees and currently eligible employees previously grandfathered will continue to be eligible for benefits under this plan. Any WFUHS employee who is within 5 years of meeting the new retirement eligibility of age 62 with combined age and years of service equal to at least 75 as of January 1, 2012 will be grandfathered into this benefit.

The measurement date for the defined postretirement benefit plan is June 30.

During fiscal year 2014, WFUHS signed a declaration to terminate the VEBA and amended the terms of the trust to allow the assets to be drawn down to pay eligible plan participants' health and dental claims. As a result of the amendment, the assets are no longer considered restricted as plan assets and are included in investments in the consolidated balance sheet. Upon complete liquidation of the VEBA, future health and dental claims will be paid from WFUHS' general assets.

**WAKE FOREST UNIVERSITY**

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The following table provides a reconciliation of the changes in each plan's benefit obligation, fair value of plan assets, and funded status for the years ended June 30, 2015 and 2014:

	2015			2014 Total
	Reynolda Campus	WFUHS	Total	
Change in benefit obligation:				
Benefit obligation at beginning of year	\$ 15,258	43,964	59,222	50,789
Service cost	808	278	1,086	1,056
Interest cost	665	1,869	2,534	2,434
Participants' contributions	801	1,992	2,793	2,577
Actuarial loss (gain)	(225)	(5,292)	(5,517)	7,558
Benefits paid	(1,445)	(3,845)	(5,290)	(5,192)
Benefit obligation at end of year	15,862	38,966	54,828	59,222
Change in plan assets:				
Fair value of plan assets at beginning of year	—	—	—	41,203
Actual return on plan assets	—	—	—	5,087
Employer contributions	644	1,853	2,497	(8,863)
Participants' contributions	801	1,992	2,793	2,577
Benefits paid	(1,445)	(3,845)	(5,290)	(5,192)
Transfer of plan assets	—	—	—	(34,812)
Fair value of plan assets at end of year	—	—	—	—
Total (liability) asset	\$ (15,862)	(38,966)	(54,828)	(59,222)
	2015			2014 Total
	Reynolds Campus	WFUHS	Total	
Amounts recognized in unrestricted net assets:				
Prior service credit	\$ —	227	227	5,261
Net actuarial gain (loss)	(1,976)	(9,546)	(11,522)	(16,122)
Total increase (decrease)	\$ (1,976)	(9,319)	(11,295)	(10,861)



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The following table provides the components of net periodic benefit cost for the years ended June 30, 2015 and 2014:

	2015			2014 Total
	Reynolda Campus	WFUHS	Total	
Service cost	\$ 808	278	1,086	1,056
Interest cost	665	1,869	2,534	2,434
Expected return on plan assets	—	—	—	(2,884)
Amortization of prior service cost (credit)	—	(5,034)	(5,034)	(6,059)
Amortization of net actuarial (gain) loss	(18)	3,053	3,035	2,337
Net periodic benefit cost	\$ 1,455	166	1,621	(3,116)

The prior service costs are amortized on a straight-line basis over the average remaining service period of active participants. Gains in excess of 10% of the greater of the benefit obligation and the market-related value of assets are amortized over the average remaining service period of active participants.

The actuarial net (gain) loss and prior service cost (credit) for the defined postretirement benefits plans that will be amortized from accumulated nonoperating income into net periodic benefit cost (credit) over the next fiscal year for Reynolda Campus and WFUHS are \$(18) and \$167, respectively.

The weighted average discount rate used to determine the accumulated postretirement benefit obligation at June 30, 2015 for Reynolda Campus and WFUHS, respectively, was 4.58% and 4.43%, and at June 30, 2014 was 4.45% and 4.36%, respectively. The discount rate reflects the current yield curve results as of June 30, 2015 and 2014. For management purposes, Reynolda Campus used 8.00% and 8.50%, and WFUHS used 7.20% and 8.00% for 2015 and 2014, respectively, for the annual rate of increase in the per capita cost of covered healthcare benefits for the first year, and a 4.50% rate was assumed in each year as the ultimate rate.

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Assumed healthcare cost trend rates have a significant effect on the amounts reported for the postretirement benefit plan. A 1% change in assumed healthcare cost trend rates would have the following effects:

	<u>One percentage increase</u>	<u>One percentage decrease</u>
Reynolda Campus:		
Effect on total service and interest cost components of net periodic benefit cost	\$ 293	(252)
Effect on postretirement benefit obligation	46	(39)
WFUHS:		
Effect on total service and interest cost components of net periodic benefit cost	\$ 6	(5)
Effect on postretirement benefit obligation	116	(110)

Aggregate benefits expected to be paid by the University in each of the next five fiscal years subsequent to June 30, 2015 and thereafter are as follows:

	<u>Reynolda Campus</u>	<u>WFUHS</u>	<u>Total</u>
2016	\$ 677	2,341	3,018
2017	678	2,509	3,187
2018	740	2,555	3,295
2019	812	2,457	3,269
2020	875	2,391	3,266
Five years thereafter	5,455	11,535	16,990
	<u>\$ 9,237</u>	<u>23,788</u>	<u>33,025</u>

The expected benefits to be paid are based on the same assumptions used to measure the University's benefit obligation at June 30, 2015 and include estimated future employee service.

Recent federal healthcare legislation includes several provisions that may affect the University's benefit plans, including imposing an excise tax on high cost coverage, eliminating lifetime and annual coverage limits, and imposing inflation-adjusted fees for each person covered by a health insurance policy for each policy plan year ending after September 30, 2012, through September 30, 2019. For the postretirement benefit plan, the changes due to recent federal healthcare legislation did not change the postretirement benefit obligation for Reynolda Campus and WFUHS.

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#### (18) Related-Party Transactions

WFUHS and NCBH each incur expenses in the course of managing WFB as an integrated academic medical center. These expenses are aggregated and allocated between WFUHS and NCBH such that each individual entity bears a share of the expenses that is proportionate to the benefit received by each entity. Additionally, WFUHS and NCBH share certain facilities, provide various services, and incur certain expenses on behalf of each other. These transactions are recorded at fair value and the costs associated with operating and maintaining jointly occupied facilities are ultimately paid by the party having beneficial occupancy.

These transactions are recorded as follows in the consolidated financial statements:

	<b>2015</b>	<b>2014</b>
(Expense) revenue from MCIA	\$ 107,946	(20,906)
Corporate service allocation, net	65,629	50,923
Other professional fees, net	62,352	42,005
Total net revenue from NCBH	\$ 235,927	72,022
Accounts receivable from (payable to) NCBH	\$ 21,625	(101,492)

In the prior fiscal year, WFUBMC entered into an unsecured line of credit in the amount of \$160,000 to provide for the working capital needs of NCBH, WFUHS, and their affiliates. This line of credit was guaranteed by both NCBH and WFUHS. The outstanding balance of this line of credit was \$124,367 as of June 30, 2014 of which WFUHS recorded a liability of \$35,367 due to WFUBMC in other liabilities that represented the portion of the line of credit utilized by WFUHS. In the current fiscal year, WFUBMC refinanced the previously held \$160,000 line of credit with a \$60,000 unsecured loan agreement that was guaranteed by both NCBH and WFUHS. The outstanding balance of this unsecured loan was \$60,000 as of June 30, 2015 of which WFUHS recorded a liability of \$9,684 due to WFUBMC in other liabilities that represented the portion of the unsecured loan utilized by WFUHS.

#### (19) Professional Liability Insurance

WFB maintains professional liability coverage, which included a \$4,000 per occurrence and a \$16,000 annual aggregate self-insurance retention for the year ended June 30, 2015. WFUHS estimates its professional liability on an actuarial basis. WFUHS' accrued professional liability costs, including estimated claims incurred but not reported, amounted to approximately \$42,145 and \$41,869 at June 30, 2015 and 2014, respectively, and are included in other liabilities and deferrals on the consolidated balance sheet. In the opinion of management, adequate provision has been made for the related risk.

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The estimated liability for self-insurance claims will be significantly affected if current and future claims differ from historical trends. While management monitors reported claims closely and considers potential outcomes as estimated by its actuaries when determining its self-insurance liability accruals, the complexity of the claims, the extended period of time to settle the claims and the wide range of potential outcomes complicate the estimation. In the opinion of management, adequate provision has been made for this related risk.

#### **(20) HIPPA Compliance**

Under the Health Insurance Portability and Accountability Act of 1996 (HIPPA), the federal government has authority to complete fraud and abuse investigations. HIPPA has established substantial fines and penalties for offenders. WFUHS maintains policies, procedures and requires regular training sessions to employers to monitor compliance with HIPPA, as well as other applicable local, state and federal statutes and regulations.

#### **(21) Subsequent Events**

The University has evaluated events occurring after June 30, 2015 through October 30, 2015, which represents the date the consolidated financial statements were issued and determined that all significant events and disclosures are included in the consolidated financial statements.