



WAKE FOREST UNIVERSITY

Consolidated Financial Statements

June 30, 2016

(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, 2016, 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, 2016, 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 2015 consolidated financial statements, and we expressed an unmodified audit opinion on those audited consolidated financial statements in our report dated October 30, 2015. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2015 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 25, 2016

WAKE FOREST UNIVERSITY

Consolidated Balance Sheet

June 30, 2016

(with summarized comparative financial information as of June 30, 2015)

(Dollars in thousands)

Assets	Supplementary information			
	Reynolda Campus	WFUHS	2016	2015
Cash and cash equivalents	\$ 63,530	32,338	95,868	210,534
Accounts receivable, net	8,882	77,108	85,990	112,384
Patient receivables, net	—	57,250	57,250	38,083
Contributions receivable, net	118,095	18,002	136,097	137,500
Notes receivable, net	22,998	716	23,714	23,145
Investments	911,432	788,576	1,700,008	1,628,265
Direct investments in real estate	19,763	—	19,763	22,800
Other assets	7,029	15,146	22,175	26,424
Land, buildings, and equipment, net	513,074	303,973	817,047	752,742
Total assets	\$ 1,664,803	1,293,109	2,957,912	2,951,877
Liabilities and Net Assets				
Liabilities:				
Accounts payable and accruals	\$ 49,668	204,139	253,807	268,293
Other liabilities and deferrals	74,908	163,578	238,486	243,801
Annuities payable	24,476	2,875	27,351	27,973
Notes payable and capital leases	53,966	25,244	79,210	46,240
Bonds payable	263,026	167,192	430,218	443,112
Postretirement benefits	15,983	40,018	56,001	54,858
Government grants refundable	9,447	—	9,447	9,582
Total liabilities	491,474	603,046	1,094,520	1,093,859
Net assets:				
Unrestricted	541,160	466,836	1,007,996	969,458
Temporarily restricted	339,437	60,736	400,173	446,485
Permanently restricted	292,732	162,491	455,223	442,075
Total net assets	1,173,329	690,063	1,863,392	1,858,018
Total liabilities and net assets	\$ 1,664,803	1,293,109	2,957,912	2,951,877

See accompanying notes to consolidated financial statements.

WAKE FOREST UNIVERSITY

Consolidated Statement of Activities

Year ended June 30, 2016

(with summarized comparative financial information for the year ended June 30, 2015)

(Dollars in thousands)

	2016			2015 Total
	Unrestricted	Temporarily restricted	Permanently restricted	
Operating revenues:				
Student tuition and fees	\$ 349,467	—	—	349,467
Less student aid	(103,841)	—	—	(103,841)
Net student tuition and fees	245,626	—	—	245,626
Government grants and contracts	167,966	—	—	167,966
Private grants and contracts	2,845	21,253	—	24,098
Contributions	24,903	13,461	—	38,364
Investment return designated for current operations	39,605	28,438	—	68,043
Patient revenue, net	473,959	—	—	473,959
Other	234,613	—	—	234,613
Sales and services of auxiliary enterprises	87,319	—	—	87,319
Net assets released from restrictions	61,812	(61,812)	—	—
Total operating revenues	1,338,648	1,340	—	1,339,988
Operating expenses:				
Salaries and wages	697,815	—	—	697,815
Employee benefits	162,565	—	—	162,565
Student aid	8,001	—	—	8,001
Services	197,403	—	—	197,403
Clinical and laboratory supplies	48,821	—	—	48,821
Other operating expenses	110,716	—	—	110,716
Depreciation and amortization	64,648	—	—	64,648
Interest on debt	17,489	—	—	17,489
Total operating expenses	1,307,458	—	—	1,307,458
Operating excess	31,190	1,340	—	32,530
Nonoperating activities:				
Restricted contributions	—	19,810	18,917	38,727
Net assets released from restriction	40,304	(40,304)	—	—
Investment return less than amounts designated for current operations	(30,077)	(27,271)	(3,695)	(61,043)
Actuarial loss on annuity obligations	—	—	(1,839)	(1,839)
Unrealized loss on interest rate swaps	(8,824)	—	—	(8,824)
Postretirement related changes other than net periodic cost	2,988	—	—	2,988
Gain from affiliates, equity method	3,706	—	—	3,706
Other, net	(749)	113	(235)	(871)
Change from nonoperating activities	7,348	(47,652)	13,148	(27,156)
Change in net assets	38,538	(46,312)	13,148	5,374
Net assets at beginning of year	969,458	446,485	442,075	1,858,018
Net assets at end of year	\$ 1,007,996	400,173	455,223	1,863,392

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, 2016

(Dollars in thousands)

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Operating revenues:				
Student tuition and fees	\$ 304,218	—	—	304,218
Less student aid	(92,392)	—	—	(92,392)
Net student tuition and fees	211,826	—	—	211,826
Government grants and contracts	8,066	—	—	8,066
Private grants and contracts	2,589	—	—	2,589
Contributions	19,108	12,177	—	31,285
Investment return designated for current operations	16,617	21,024	—	37,641
Other	8,324	—	—	8,324
Sales and services of auxiliary enterprises	87,319	—	—	87,319
Net assets released from restrictions	31,390	(31,390)	—	—
Total operating revenues	385,239	1,811	—	387,050
Operating expenses:				
Salaries and wages	186,010	—	—	186,010
Employee benefits	49,456	—	—	49,456
Student aid	3,306	—	—	3,306
Services	42,409	—	—	42,409
Other operating expenses	54,312	—	—	54,312
Depreciation and amortization	33,798	—	—	33,798
Interest on debt	12,168	—	—	12,168
Total operating expenses	381,459	—	—	381,459
Operating excess	3,780	1,811	—	5,591
Nonoperating activities:				
Restricted contributions	—	19,810	11,001	30,811
Net assets released from restriction	40,304	(40,304)	—	—
Investment return less than amounts designated for current operations	(6,501)	(19,265)	(824)	(26,590)
Actuarial (loss) gain on annuity obligations	—	—	(2,276)	(2,276)
Unrealized loss on interest rate swaps	(7,356)	—	—	(7,356)
Postretirement related changes other than net periodic cost	882	—	—	882
Other, net	(1,134)	139	61	(934)
Change from nonoperating activities	26,195	(39,620)	7,962	(5,463)
Change in net assets	29,975	(37,809)	7,962	128
Net assets at beginning of year	511,185	377,246	284,770	1,173,201
Net assets at end of year	\$ 541,160	339,437	292,732	1,173,329

See accompanying notes to consolidated financial statements.

WAKE FOREST UNIVERSITY

Statement of Activities

Wake Forest University Health Sciences
(Supplementary Information)

Year ended June 30, 2016

(Dollars in thousands)

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Operating revenues:				
Student tuition and fees	\$ 45,249	—	—	45,249
Less student aid	(11,449)	—	—	(11,449)
Net student tuition and fees	33,800	—	—	33,800
Government grants and contracts	159,900	—	—	159,900
Private grants and contracts	256	21,253	—	21,509
Contributions	5,795	1,284	—	7,079
Investment return designated for current operations	22,988	7,414	—	30,402
Patient revenue, net	473,959	—	—	473,959
Other	226,289	—	—	226,289
Net assets released from restrictions	30,422	(30,422)	—	—
Total operating revenues	<u>953,409</u>	<u>(471)</u>	<u>—</u>	<u>952,938</u>
Operating expenses:				
Salaries and wages	511,805	—	—	511,805
Employee benefits	113,109	—	—	113,109
Student aid	4,695	—	—	4,695
Services	154,994	—	—	154,994
Clinical and laboratory supplies	48,821	—	—	48,821
Other operating expenses	56,404	—	—	56,404
Depreciation and amortization	30,850	—	—	30,850
Interest on debt	5,321	—	—	5,321
Total operating expenses	<u>925,999</u>	<u>—</u>	<u>—</u>	<u>925,999</u>
Operating excess (deficit)	<u>27,410</u>	<u>(471)</u>	<u>—</u>	<u>26,939</u>
Nonoperating activities:				
Restricted contributions	—	—	7,916	7,916
Investment return less than amounts designated for current operations	(23,576)	(8,006)	(2,871)	(34,453)
Actuarial gain on annuity obligations	—	—	437	437
Unrealized loss on interest rate swaps	(1,468)	—	—	(1,468)
Postretirement related changes other than net periodic cost	2,106	—	—	2,106
Gain from affiliates, equity method	3,706	—	—	3,706
Other, net	385	(26)	(296)	63
Change from nonoperating activities	<u>(18,847)</u>	<u>(8,032)</u>	<u>5,186</u>	<u>(21,693)</u>
Change in net assets	8,563	(8,503)	5,186	5,246
Net assets at beginning of year	458,273	69,239	157,305	684,817
Net assets at end of year	\$ <u>466,836</u>	<u>60,736</u>	<u>162,491</u>	<u>690,063</u>

See accompanying notes to consolidated financial statements.

WAKE FOREST UNIVERSITY
Consolidated Statement of Cash Flows
Year ended June 30, 2016
(with summarized comparative financial information for the year ended June 30, 2015)
(Dollars in thousands)

	Supplementary information		2016	2015
	Reynolda Campus	WFUHS		
Cash flows from operating activities:				
Change in net assets	\$ 128	5,246	5,374	82,674
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:				
Depreciation and amortization	33,798	30,068	63,866	65,350
Net (gains) losses on investments	(3,028)	4,051	1,023	5,643
Noncash gifts	(98)	—	(98)	(625)
Private gifts restricted for capital and long-term investment	(30,913)	(7,916)	(38,829)	(53,552)
Other revenue restricted for long-term investment	(810)	(308)	(1,118)	(573)
Loss (gain) on disposals of property and equipment	236	(144)	92	1,143
Gain from equity method affiliates	—	(3,706)	(3,706)	(10,749)
Unrealized loss on interest rate swaps	7,694	1,468	9,162	2,084
Bad debt expense	586	15,295	15,881	17,164
Changes in due from affiliates	—	4,293	4,293	—
Changes in operating assets and liabilities:				
Accounts and patient receivables	(572)	(7,804)	(8,376)	275,695
Contributions receivable	427	5,191	5,618	(28,175)
Notes receivable	—	116	116	(258)
Other assets and other liabilities and deferrals	(11,436)	(3,374)	(14,810)	(90,911)
Accounts payable and accruals	3,162	(35,822)	(32,660)	(4,409)
Postretirement benefits	121	1,051	1,172	(2,163)
Annuities payable	(185)	437	252	2,007
Net cash (used in) provided by operating activities	(890)	8,142	7,252	260,345
Cash flows from investing activities:				
Purchases of land, buildings, and equipment	(75,629)	(36,262)	(111,891)	(73,830)
Proceeds from sale of land, buildings, and equipment	3,392	66	3,458	3,331
Repayments of notes receivable	—	632	632	1,447
Disbursements of loans to students and other	(4,017)	(78)	(4,095)	(3,442)
Repayments of loans to students and other	3,297	138	3,435	3,184
Purchases of investments	(545,984)	(539,585)	(1,085,569)	(674,047)
Net proceeds from sales and maturities of investments	576,853	441,258	1,018,111	606,539
Decrease in deposits with bond trustee	—	—	—	25
Net cash used in investing activities	(42,088)	(133,831)	(175,919)	(136,793)
Cash flows from financing activities:				
Change in government grants refundable	(135)	—	(135)	(106)
Proceeds from notes payable	39,511	5,000	44,511	23,767
Principal payments on notes payable	(1,953)	(6,483)	(8,436)	(8,154)
Proceeds from borrowings from WFUBMC	—	—	—	9,684
Payments on borrowings from WFUBMC	—	(3,037)	(3,037)	(35,367)
Principal payments on bonds payable	(6,405)	(5,789)	(12,194)	(6,195)
Proceeds from private gifts restricted for capital and long-term investment	26,455	7,916	34,371	50,683
Net realized (gains) losses restricted for long-term investment	(2,349)	308	(2,041)	573
Other revenue restricted for long-term investment	810	152	962	658
Net cash provided by (used in) financing activities	55,934	(1,933)	54,001	35,543
Net increase (decrease) in cash and cash equivalents	12,956	(127,622)	(114,666)	159,095
Cash and cash equivalents at beginning of year	50,574	159,960	210,534	51,439
Cash and cash equivalents at end of year	\$ 63,530	32,338	95,868	210,534
Supplemental disclosures of cash flow information:				
Cash paid for interest, net of amounts capitalized	\$ 12,190	6,987	19,177	18,659
Assets acquired under capital leases	—	—	—	11,762
Transfer of assets to due to/from WFUBMC	—	—	—	36,938
Capital expenditures included in account payable	30,144	2,428	32,572	14,367

See accompanying notes to consolidated financial statements.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 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, LLC (Master Fund), Verger Fund I, LLC (Verger Fund I), Verger Fund II, LLC (Verger Fund II) 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. 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), Master Fund, Verger Fund I and Verger Fund II. 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. The Master Fund is controlled and consolidated by the University. Verger Fund I was created to hold the Reynolda Campus long-term endowment pool. Verger Fund II was created to hold the WFUHS and Reynolda House long-term endowment pools. The Master Fund, Verger Capital Fund, Verger Fund I, and Verger Fund II 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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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, WFB operates WFUHS (including all subsidiaries and affiliates) and NCBH (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 January 2016, the FASB issued ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*. This ASU removes the requirement to disclose the fair value of financial instruments measured at amortized costs. The University adopted ASU 2016-01 in 2016 and removed the fair value disclosure for its fixed rate debt.

(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 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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

- 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) 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 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.

(f) Notes Receivable

Notes receivable, which are recorded at face value, principally represent amounts due from students under Perkins and other U.S. government sponsored loan programs. A general allowance is made for uncollectible student loans after considering long-term collection experience and current trends. Other notes receivable are evaluated individually for impairment, with allowances based on management's expectations given facts and circumstances related to each note.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(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 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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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.

Net asset value (NAV) – Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy.

In the event that changes in the inputs used in the fair value measurement of an asset or liability result in a transfer of the fair value measurement to a different categorization (e.g., from Level 3 to Level 2), such transfers between fair value categories are recognized at the end of the reporting period.

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.

(k) 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.

(l) 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

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

University recognizes an impairment charge when the fair value of the asset or group of assets is less than the carrying value.

(m) *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.

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

(o) *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.

(p) *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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(q) *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.

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. Indirect costs 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 \$24,179 and \$24,891 in 2016 and 2015, 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

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

meaningful use requirements. Accordingly, for the years ended June 30, 2016 and 2015, WFUHS recognized EHR incentives of approximately \$1,571 and \$3,197, respectively, which are included in other revenue (separate from net patient service revenue) in the consolidated statement of activities.

(r) 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.

(s) 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, 2013 remain subject to examination by federal and state tax authorities. The University has evaluated uncertain tax positions for the years ended June 30, 2016 and 2015, 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, 2016 and 2015.

(t) Reclassifications

Certain amounts previously reported in the 2015 consolidated financial statements have been reclassified to conform to the 2016 presentation. Such reclassifications have no effect on total assets, liabilities or net assets or operating, investing or financing cash flows as previously reported.

(u) 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, 2015 from which this information was derived.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(2) Accounts Receivable

The following is an analysis of accounts receivable at June 30, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Accounts receivable	\$ 6,538	42,695	49,233	75,969
Grants receivable	3,122	35,818	38,940	37,770
Total accounts receivable	9,660	78,513	88,173	113,739
Less allowance for bad debts	(778)	(1,405)	(2,183)	(1,355)
Accounts receivable, net	\$ 8,882	77,108	85,990	112,384

(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 who 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 are provided. The following is an analysis of net patient service revenue at June 30, 2016 and 2015:

	WFUHS	
	2016	2015
Third-party payers	\$ 475,552	429,156
Self-pay	13,702	15,414
Provision for bad debts	(15,295)	(15,826)
Net patient service revenue	\$ 473,959	428,744

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

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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 collectability 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.

Patient receivables are recorded net of allowance for contractual adjustments and uncollectible accounts of \$105,309 and \$63,748, respectively, at June 30, 2016 and \$71,693 and \$76,771, respectively, at June 30, 2015.

WFUHS' allowance for doubtful accounts for self-pay patients decreased from 91% of self-pay accounts receivable at June 30, 2015 to 89% of self-pay accounts receivable at June 30, 2016. In addition, WFUHS' self-pay allowances and expenses (which include charity care charges foregone and bad debt expense) decreased \$11,254 from \$26,429 for fiscal year 2015 to \$15,175 for fiscal year 2016. WFUHS maintains an allowance for doubtful accounts for patient residuals associated with third-party payers. The allowance was \$21,611 and \$24,322 at June 30, 2016 and 2015, 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:

	<u>2016</u>	<u>2015</u>
Medicare	13%	11%
Medicaid	15	17
Self-pay	18	29
Other	54	43
	<u>100%</u>	<u>100%</u>

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(4) Contributions Receivable

The following is an analysis of the maturities of the University's contributions receivable at June 30, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
One year or less	\$ 31,882	8,544	40,426	34,823
Between one and five years	53,523	10,969	64,492	67,872
More than five years	100,000	494	100,494	105,341
Gross contributions receivable	185,405	20,007	205,412	208,036
Less estimated uncollectible amounts	(6,807)	(1,246)	(8,053)	(7,790)
Less discount to present value	(60,503)	(759)	(61,262)	(62,746)
Contributions receivable, net	\$ <u>118,095</u>	<u>18,002</u>	<u>136,097</u>	<u>137,500</u>

Contributions receivable are discounted at a rate commensurate with the scheduled timing of receipt. Such amounts outstanding as of June 30, 2016, and 2015, were discounted at rates ranging from 2.26% to 2.88% for WFU, respectively, and 1.91% to 2.26% for WFUHS, respectively.

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 30% and 31% of Reynolda Campus' net contributions receivable as of June 30, 2016 and 2015, respectively.

(5) Notes Receivable

The following is an analysis of notes receivable at June 30, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Student loans receivable	\$ 19,312	795	20,107	19,888
Other notes receivable	4,068	508	4,576	4,565
Total notes receivable	23,380	1,303	24,683	24,453
Less estimated uncollectible amounts	(382)	(587)	(969)	(1,308)
Notes receivable, net	\$ <u>22,998</u>	<u>716</u>	<u>23,714</u>	<u>23,145</u>

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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, 2016 and 2015, student loans receivable consisted of Federal loan programs of \$18,542 and \$18,205, respectively, and institutional loan programs of \$1,566 and \$1,683, 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 \$9,447 and \$9,582 at June 30, 2016 and 2015, 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, 2016 and 2015, the allowance for uncollectible institutional student loan amounts was \$382 and \$350, respectively.

(6) Investments

Investments at June 30, 2016 and 2015 consist of the following:

	2016	2015
Short-term investments ^(a)	\$ 157,072	129,882
Absolute return ^(b)	279,231	273,061
Commodities: ^(c)	136,639	135,804
Fixed income: ^(d)		
Domestic	341,893	277,821
International	74,245	88,185
Private equity ^(e)	118,777	106,125
Public equity: ^(f)		
Domestic	247,682	261,143
International	160,356	157,025
Real estate: ^(g)	53,177	56,587
Beneficial interest in perpetual trusts and assets held by others ^(h)	23,909	25,837
Other	107,027	116,795
Total investments	\$ 1,700,008	1,628,265

(a) Includes short duration U.S. Treasury debt securities and other short-term, higher quality debt securities, cash and money market mutual funds.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

- (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.
- (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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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

	<u>2016</u>	<u>2015</u>
Investment income, net	\$ 25,817	39,666
Realized (losses) gains, net	(14,415)	41,248
Changes in unrealized depreciation	(4,402)	(54,843)
Total investment return	7,000	26,071
Endowment appropriation designated for current operations	(65,202)	(62,258)
Other investment returns designated for current operations	(2,841)	(2,330)
Investment return less than amounts designated for current operations	\$ <u>(61,043)</u>	<u>(38,517)</u>

The University incurred internal investment management costs of \$8,741 and \$7,884 in 2016 and 2015, respectively. The University reports investment returns net of internal and external management fees.

(7) Endowment

The University's pooled endowment consists of approximately 1,775 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.

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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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, 2016 and 2015 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.

The University invests the majority of these assets in Verger Capital Fund. 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, 2016, Reynolda Campus held units of 14,601,539, WFUHS held 11,021,932 units and Reynolda House held units of 641,689 in these long-term pools with a fair value of \$46.76, \$46.52 and \$46.46 per unit, respectively. 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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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 \$10,591 and \$2,217 as of June 30, 2016; and \$6,551 and \$1,083 as of June 30, 2015.

Endowment net assets consist of the following at June 30, 2016 and 2015:

	2016			Total	2015 Total
	Unrestricted	Temporarily restricted	Permanently restricted		
Reynolda Campus:					
Donor-restricted endowment funds	\$ (10,591)	212,609	259,806	461,824	475,735
Board-designated endowment funds	224,498	—	—	224,498	237,253
Endowment net assets	<u>\$ 213,907</u>	<u>212,609</u>	<u>259,806</u>	<u>686,322</u>	<u>712,988</u>
WFUHS:					
Donor-restricted endowment funds	\$ (2,217)	45,683	138,995	182,461	180,406
Board-designated endowment funds	272,429	—	—	272,429	274,006
Total endowment net assets	<u>\$ 270,212</u>	<u>45,683</u>	<u>138,995</u>	<u>454,890</u>	<u>454,412</u>

Changes in endowment net assets for the years ended June 30, 2016 and 2015 are as follows:

	2016			Total	2015 Total
	Unrestricted	Temporarily restricted	Permanently restricted		
Reynolda Campus:					
Beginning balance	\$ 230,702	233,847	248,439	712,988	713,734
Investment return:					
Investment income net of fees	(1,448)	(3,456)	(56)	(4,960)	2,495
Net (depreciation) appreciation	(1,104)	3,126	(1,157)	865	7,144
Total investment return (loss)	(2,552)	(330)	(1,213)	(4,095)	9,639
Contributions	267	191	12,742	13,200	18,028
Appropriation for expenditure	(15,010)	(21,099)	(420)	(36,529)	(29,746)
Transfers due to donor redesignations	—	—	8	8	(35)
Transfers to Board-designated funds	500	—	250	750	1,368
Ending balance	<u>\$ 213,907</u>	<u>212,609</u>	<u>259,806</u>	<u>686,322</u>	<u>712,988</u>

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

	2016			Total	2015 Total
	Unrestricted	Temporarily restricted	Permanently restricted		
WFUHS:					
Beginning balance	\$ 272,923	50,342	131,147	454,412	434,292
Investment return:					
Investment income net of fees	2,746	1,572	133	4,451	6,636
Net (depreciation) appreciation	<u>(3,976)</u>	<u>(1,446)</u>	<u>(179)</u>	<u>(5,601)</u>	<u>464</u>
Total investment return (loss)	(1,230)	126	(46)	(1,150)	7,100
Contributions	996	—	7,894	8,890	10,841
Appropriation for expenditure	(14,771)	(4,785)	—	(19,556)	(18,258)
Transfers to Board-designated funds	<u>12,294</u>	<u>—</u>	<u>—</u>	<u>12,294</u>	<u>20,437</u>
Ending balance	\$ <u><u>270,212</u></u>	<u><u>45,683</u></u>	<u><u>138,995</u></u>	<u><u>454,890</u></u>	<u><u>454,412</u></u>

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(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:

	2016				Total
	Level 1	Level 2	Level 3	NAV	
Financial assets:					
Cash and cash equivalents	\$ 95,868	—	—	—	95,868
Investments:					
Short-term investments	157,072	—	—	—	157,072
Absolute return	16,088	—	—	263,143	279,231
Commodities	24,834	—	—	111,805	136,639
Fixed income:					
Domestic	230,494	75,971	11,912	23,516	341,893
International	2,987	28,265	5,842	37,151	74,245
Private equity	—	—	—	118,777	118,777
Public equity:					
Domestic	186,403	141	406	60,732	247,682
International	101,740	726	25	57,865	160,356
Real estate	12,179	—	—	40,998	53,177
Beneficial interest in perpetual trusts and assets held by others					
	—	—	23,909	—	23,909
Other	3,889	48,690	—	54,448	107,027
Total assets	<u>\$ 831,554</u>	<u>153,793</u>	<u>42,094</u>	<u>768,435</u>	<u>1,795,876</u>
Financial liabilities:					
Other liabilities and deferrals:					
Employee benefits	\$ —	48,690	—	—	48,690
Interest rate swap agreements	—	30,920	—	—	30,920
Annuities payable	—	27,351	—	—	27,351
Total liabilities	<u>\$ —</u>	<u>106,961</u>	<u>—</u>	<u>—</u>	<u>106,961</u>

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

	2015				
	Level 1	Level 2	Level 3	NAV	Total
Financial assets:					
Cash and cash equivalents	\$ 210,534	—	—	—	210,534
Investments:					
Short-term investments	129,882	—	—	—	129,882
Absolute return	2,260	430	—	270,371	273,061
Commodities	30,052	—	—	105,752	135,804
Fixed income:					
Domestic	221,906	27,101	16,118	12,696	277,821
International	12,876	27,503	—	47,806	88,185
Private equity	—	—	—	106,125	106,125
Public equity:					
Domestic	208,890	3,525	295	48,433	261,143
International	86,815	817	—	69,393	157,025
Real estate	5,133	—	—	51,454	56,587
Beneficial interest in perpetual trusts and assets held by others					
Other	—	—	25,837	—	25,837
Other	3,885	53,036	—	59,874	116,795
Total assets	<u>\$ 912,233</u>	<u>112,412</u>	<u>42,250</u>	<u>771,904</u>	<u>1,838,799</u>
Financial liabilities:					
Other liabilities and deferrals:					
Employee benefits	\$ —	44,186	—	—	44,186
Interest rate swap agreements	—	12,490	—	—	12,490
Annuities payable	—	27,973	—	—	27,973
Total liabilities	<u>\$ —</u>	<u>84,649</u>	<u>—</u>	<u>—</u>	<u>84,649</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 securities during the year ended June 30, 2016. Transfers into and out of Level 3 are typically the result of a change in observation of significant valuation inputs required by various models.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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 3.07% and 3.71% at June 30, 2016 and 2015, respectively.

The following table presents the reconciliation of Level 3 assets measured at fair value for the year ended June 30, 2016. Both observable and unobservable inputs may be used to determine the fair value of positions that the University has classified as Level 3.

	<u>Balance as of June 30, 2015</u>	<u>Total realized and unrealized losses</u>	<u>Purchases</u>	<u>Sales</u>	<u>Net transfers out of Level 3</u>	<u>Balance as of June 30, 2016</u>
Investments:						
Fixed income:						
Domestic	\$ 8,000	(531)	3,981	(829)	1,284	11,905
International	8,118	(261)	—	(2,008)	—	5,849
Public equity:						
Domestic	181	(99)	437	(113)	—	406
International	114	(4)	—	(85)	—	25
Interests in perpetual trusts and assets held by others	<u>25,837</u>	<u>(1,928)</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>23,909</u>
Total assets	<u>\$ 42,250</u>	<u>(2,823)</u>	<u>4,418</u>	<u>(3,035)</u>	<u>1,284</u>	<u>42,094</u>

The University's aggregate unfunded private capital commitments are approximately \$185,700, or 10.9%, of total investments at June 30, 2016. Of these commitments, \$92,200 relates to private equity, \$10,500 relates to real estate, \$55,300 relates to commodities, \$10,900 relates to absolute return, \$15,800 relates to fixed income and \$1,000 relates to emerging markets. 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 uncertain, the University takes these factors into consideration when allocating to private investments and believes that it has adequate liquidity to meet its obligations.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

As of June 30, 2016, redemption frequency and the corresponding notice period for all investments are as follows:

Category	Redemption frequency (in days) (if currently eligible)	Redemption notice period (in days)
Short-term investments	1 to 7 days	1 day
Absolute return	daily to >365	1 to 90 days
Commodities	1 to N/A	1 to N/A
Fixed income		
Domestic	1 to 180 days	daily to monthly
International	N/A	N/A
Private equity	N/A	N/A
Public equity		
Domestic	1 to 65 days	daily to quarterly
International	90 days	quarterly
Real estate	N/A	N/A
Perpetual trusts and assets held by others	N/A	N/A
Other	N/A	N/A

(9) Land, Buildings, and Equipment

Land, buildings, and equipment are summarized as follows at June 30, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Land and improvements	\$ 28,996	99,937	128,933	122,592
Buildings and other improvements	685,432	395,162	1,080,594	1,009,966
Equipment and furnishings	115,673	193,727	309,400	291,295
Construction in progress	50,832	22,341	73,173	54,654
	880,933	711,167	1,592,100	1,478,507
Less accumulated depreciation	(367,859)	(407,194)	(775,053)	(725,765)
	\$ 513,074	303,973	817,047	752,742

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

Total depreciation expense on buildings, improvements, equipment, and furnishings was \$64,584 and \$63,321 for the years ended June 30, 2016 and 2015, 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.

The University's policy is to capitalize interest cost incurred on debt during the construction of major projects exceeding one year. Interest cost of \$1,091 and \$495 was capitalized in the years ended June 30, 2016 and 2015, respectively.

The liabilities associated with AROs for the years ended June 30, 2016 and 2015, respectively, were \$8,414 and \$9,282 for Reynolda Campus, and \$2,756 and \$2,695 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, 2016 and 2015 consist of the following:

Reynolda Campus	Years to nominal maturity	Interest rate at June 30, 2016		2016	2015
Notes payable and capital leases:					
2013 Construction loan	2	0.64	Variable	\$ 48,973	9,646
Promissory note	4	4.00	Variable	275	500
Capital leases	5	0.81 to 7.5	Fixed	4,718	6,262
Total notes payable and capital leases				<u>53,966</u>	<u>16,408</u>
Bonds payable:					
2004 Series A tax-exempt	<1 to 5	0.06%	Fixed	20,560	23,475
2004 Series B tax-exempt	<1 to 5	0.06%	Variable	7,340	10,830
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 tax-exempt	29	2.6 to 3.1	Fixed	20,425	20,425
2012 Series term tax-exempt	29	3.45 to 3.7	Fixed	104,575	104,575
Unamortized bond premium				2,003	2,090
Unamortized bond issuance costs				(1,877)	(1,978)
Total bonds payable				<u>263,026</u>	<u>269,417</u>
Total notes payable, capital leases, and bonds payable				<u>\$ 316,992</u>	<u>285,825</u>

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

Reynolda Campus has a three 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 \$27,900 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 \$6,625 to \$7,340. The interest rate on the bonds is determined weekly, and at the option of the University may be 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, 2016		2016	2015
Notes payable and capital leases:					
Line of credit	>1	Libor plus 0.6%	Variable	\$ 11,489	13,039
Loan agreement	<1 to 10	Libor plus 0.65%	Variable	13,675	15,678
Promissory note	2			80	160
Promissory note	7		Fixed	—	955
Total notes payable				25,244	29,832

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

WFUHS	Years to nominal maturity	Interest rate at June 30, 2016		2016	2015
Bonds payable:					
Series 2012 B	<1 to 20	2.00%–5.00%	Fixed	\$ 102,155	105,750
Series 2012 C	<1 to 20	0.74%	Variable	52,615	54,810
Unamortized bond premium				13,614	14,395
Unamortized bond issuance costs				(1,192)	(1,260)
Total bonds payable				<u>167,192</u>	<u>173,695</u>
Total notes payable and bonds payable				<u>\$ 192,436</u>	<u>203,527</u>

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 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, 2016. As of June 30, 2016, WFUHS is jointly and severally liable for \$482,971 of bonds payable borrowed by the other members of the Obligated Group and for \$14,518 and \$54,000 under WFUBMC's line of credit and notes payable. 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 2016 and in increasing annual amounts of \$3,385 to \$7,000.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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 2016 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 0.70%.

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 \$20,014 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, 2016 and thereafter are as follows:

	<u>Reynolda Campus</u>	<u>WFUHS</u>	<u>Total</u>
2017	\$ 8,551	8,081	16,632
2018	57,116	18,992	76,108
2019	8,084	7,743	15,827
2020	8,058	8,013	16,071
2021	14	8,298	8,312
In total thereafter	<u>235,169</u>	<u>141,309</u>	<u>376,478</u>
	<u>\$ 316,992</u>	<u>192,436</u>	<u>509,428</u>

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 2016 consolidated balance sheet. Total amortization expense for issue costs and premium is included in interest expense in the consolidated statements of activities.

(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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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.

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

	<u>Reynolda Campus</u>		<u>WFUHS</u>
	<u>November 2006</u> interest rate swap	<u>October 2008</u> interest rate swap	<u>August 2002</u> interest rate swap
Notional amount	\$ 20,560	50,000	23,350
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, 2016 and 2015, respectively, was \$2,500 and \$0 for Reynolda Campus, and \$5,980 and \$4,890 for WFUHS.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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

	2016		2015	
	Fair value	Gain (loss)	Fair value	Gain (loss)
Reynolda Campus:				
November 2006 interest rate swap	\$ (1,505)	338	(1,843)	495
October 2008 interest rate swap	(23,144)	(7,694)	(15,450)	(2,330)
Total	(24,649)	(7,356)	(17,293)	(1,835)
WFUHS:				
August 2002 interest rate swap	(6,271)	(1,468)	(4,803)	(249)
Total	(6,271)	(1,468)	(4,803)	(249)
Grand total	\$ (30,920)	(8,824)	(22,096)	(2,084)

As of June 30, 2016, the University's adjusted debt portfolio, after taking into account the aforementioned swap agreements, was 100% fixed rate for Reynolda Campus, and approximately 70% fixed rate for WFUHS.

(12) Net Assets

Temporarily restricted net assets are composed of the following at June 30, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Gifts and pledges	\$ 126,828	15,053	141,881	162,296
Donor-restricted endowments	212,609	45,683	258,292	284,189
	\$ 339,437	60,736	400,173	446,485

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

Such temporarily restricted net assets are available for the following purposes as of June 30, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Student scholarships	\$ 201,810	1,756	203,566	204,669
Instruction and research	59,715	35,334	95,049	103,902
Academic support	36,299	12,902	49,201	49,199
Subsequent period operations, capital, and other	41,613	10,744	52,357	88,715
	\$ 339,437	60,736	400,173	446,485

Permanently restricted net assets are composed of the following at June 30, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Donor-restricted endowments	\$ 259,806	138,995	398,801	379,586
Gifts and pledges	21,228	3,532	24,760	26,966
Student loan funds	—	4,944	4,944	4,874
Interests in perpetual trusts and assets held by others	4,795	13,281	18,076	19,256
Annuity and other split-interest agreements	6,903	1,739	8,642	11,393
	\$ 292,732	162,491	455,223	442,075

The future return on the following donor-restricted endowments is restricted for the following purposes as of June 30, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Student scholarships	\$ 173,006	31,211	204,217	203,266
Instruction and research	56,297	93,983	150,280	139,458
Academic support	23,371	13,801	37,172	29,782
Subsequent period operations and other	7,132	—	7,132	7,080
	\$ 259,806	138,995	398,801	379,586

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(13) Functional Expenses

Expenses are reported in the consolidated statement of activities in natural categories. Functional expenses for the years ended June 30, 2016 and 2015 are categorized as follows:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Instruction and departmental research	\$ 134,855	80,405	215,260	203,328
Patient services	—	616,751	616,751	495,052
Sponsored research, training, and other programs	8,823	179,508	188,331	197,255
Organized activities	2,595	—	2,595	2,332
Academic support	27,330	13,068	40,398	44,454
Libraries	14,474	3,781	18,255	17,619
Student services	29,957	1,874	31,831	30,142
Institutional support	79,229	30,612	109,841	99,155
Auxiliary enterprises	84,196	—	84,196	76,742
	Total operating expenses	\$ 381,459	925,999	1,307,458
		381,459	925,999	1,307,458
		381,459	925,999	1,166,079

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.

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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(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:			
2017	\$ 10,575	1,260	11,835
2018	10,883	1,153	12,036
2019	11,096	749	11,845
2020	11,313	660	11,973
2021	11,535	691	12,226
	<u>\$ 55,402</u>	<u>4,513</u>	<u>59,915</u>

Total income from real estate was \$10,526 and \$10,753 for Reynolda Campus and \$1,789 and \$1,775 for WFUHS for the years ended June 30, 2016 and 2015, respectively.

The estimated cost to complete construction in progress at June 30, 2016 and 2015, respectively, were \$96,240 and \$85,064 for Reynolda Campus, and \$12,182 and \$22,124 for WFUHS.

Expenditures related to federal and state grants and contracts are subject to adjustment based upon review by the granting agencies. Amounts of expenditures that granting agencies might disallow cannot be determined at this time. These amounts affect government grants and contract revenue as well as facilities and administrative cost recovery. The University would not expect these costs to influence the consolidated financial position significantly.

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 \$1,473 and \$1,050 at June 30, 2016 and 2015, respectively, for Reynolda Campus and \$5,485 and \$5,575 at June 30, 2016 and 2015, respectively, for WFUHS and are included in other liabilities in the accompanying consolidated balance sheet.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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.

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

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 5-year renewal options. The lease is classified as an operating lease. Operating lease payments in each year from 2017 to 2021 are \$7,667, \$7,744, \$7,821, \$7,899 and \$7,978, respectively, and \$48,333 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 2017 to 2021 are \$5,501, \$5,638, \$5,779, \$5,924 and \$6,072, respectively, and \$39,754 thereafter.

WFUHS has a deferred gain related to the sale and leaseback of certain assets. The deferred gain was \$21,176 and \$23,073 for 2016 and 2015, respectively, and is included in other liabilities and deferrals in the accompanying consolidated balance sheets.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(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, 2016 and 2015, respectively, were \$12,558 and \$12,087 for Reynolda Campus and \$24,303 and \$14,603 for WFUHS.

Reynolda Campus and WFUHS have accrued \$334 and \$6,190 at June 30, 2016, respectively, and \$2,888 and \$5,090 at June 30, 2015, respectively, at June 30, 2015 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.

Effective January 1, 2016, retirees age 65 and over transitioned from the existing medical benefits plan to a Health Reimbursement Arrangement to provide fixed annual contributions for medical expenses. This change resulted in a prior service cost decrease of \$4,543 for the year ended June 30, 2016, which is included in the change in postretirement benefits obligation in the statements of activities.

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 years of 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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Change in benefit obligation:				
Benefit obligation at beginning of year	\$ 15,862	38,966	54,828	59,222
Service cost	795	136	931	1,086
Interest cost	711	1,675	2,386	2,534
Plan amendments	(4,543)	—	(4,543)	—
Participants' contributions	564	575	1,139	2,793
Actuarial loss (gain)	3,632	868	4,500	(5,517)
Benefits paid	(1,038)	(2,202)	(3,240)	(5,290)
Benefit obligation at end of year	15,983	40,018	56,001	54,828
Change in plan assets:				
Fair value of plan assets at beginning of year	—	—	—	—
Employer contributions	474	1,627	2,101	2,497
Participants' contributions	564	575	1,139	2,793
Benefits paid	(1,038)	(2,202)	(3,240)	(5,290)
Fair value of plan assets at end of year	—	—	—	—
Total liability	\$ (15,983)	(40,018)	(56,001)	(54,828)
Amounts recognized in unrestricted net assets:				
Prior service (cost) credit	\$ (4,543)	197	(4,346)	227
Net actuarial gain (loss)	1,685	(9,037)	(7,352)	(11,522)
Total decrease	\$ (2,858)	(8,840)	(11,698)	(11,295)

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

The following table provides the components of net periodic benefit cost for the years ended June 30, 2016 and 2015:

	2016			2015 Total
	Reynolda Campus	WFUHS	Total	
Service cost	\$ 795	135	930	1,086
Interest cost	711	1,675	2,386	2,534
Amortization of prior service credit	—	(30)	(30)	(5,034)
Amortization of net actuarial (gain) loss	(29)	1,378	1,349	3,035
Net periodic benefit cost	\$ 1,477	3,158	4,635	1,621

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 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 \$883 and \$1,362, respectively.

The weighted average discount rate used to determine the accumulated postretirement benefit obligation at June 30, 2016 for Reynolda Campus and WFUHS, respectively, was 3.85% and 3.70%, and at June 30, 2015 was 4.58% and 4.43%, respectively. The discount rate reflects the current yield curve results as of June 30, 2016 and 2015. For management purposes, Reynolda Campus used 7.0% and 8.00%, and WFUHS used 7.00% and 7.20% for 2016 and 2015, 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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

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:

	One percentage increase	One percentage decrease
Reynolda Campus:		
Effect on total service and interest cost components of net periodic benefit cost	\$ 355	(310)
Effect on postretirement benefit obligation	57	(49)
WFUHS:		
Effect on total service and interest cost components of net periodic benefit cost	\$ 8	(7)
Effect on postretirement benefit obligation	216	(174)

Aggregate benefits expected to be paid by the University, net of participant contributions, for the postretirement benefits plans are as follows:

	Reynolda Campus	WFUHS	Total
2017	\$ 668	2,379	3,047
2018	605	2,464	3,069
2019	697	2,362	3,059
2020	754	2,320	3,074
2021	841	2,296	3,137
Five years thereafter	5,242	11,070	16,312
	\$ 8,807	22,891	31,698

The expected benefits to be paid are based on the same assumptions used to measure the University's benefit obligation at June 30, 2016 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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(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:

	<u>2016</u>	<u>2015</u>
Revenue from MCIA	\$ 198,796	107,946
Corporate service allocation, net	34,477	65,629
Other professional fees, net	<u>(19,509)</u>	<u>62,352</u>
Total net revenue from NCBH	<u>\$ 213,764</u>	<u>235,927</u>
Accounts (payable to) receivable from NCBH	\$ (17,089)	21,625

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 unsecured loan was \$54,000 and \$60,000 as of June 30, 2016 and 2015, respectively, of which WFUHS recorded a liability of \$8,716 and \$9,684, respectively, 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 \$5,000 per occurrence and a \$25,000 annual aggregate self-insurance retention for the year ended June 30, 2016. WFUHS estimates its professional liability on an actuarial basis. WFUHS' accrued professional liability costs, including estimated claims incurred but not reported, amounted to approximately \$45,779 and \$42,145 at June 30, 2016 and 2015, 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.

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.

WAKE FOREST UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(With summarized information for 2015)

(Dollars in thousands)

(20) Subsequent Events

The University evaluated events subsequent to June 30, 2016, through October 25, 2016, the date of the issuance of the consolidated financial statements. During this period, the Reynolda Campus issued \$159,100 of tax-exempt North Carolina Capital Facilities Finance Agency Educational Facilities Revenue and Revenue Refunding Bonds, Series 2016. The 2016 Series bonds were issued for the purpose of the current refunding and defeasance of the Series 2009 tax-exempt bonds (\$110,000) and financing the costs of acquisition, construction, renovation and installation of capital assets of the Reynolda Campus. The Series 2016 tax exempt bonds are evidenced by a loan agreement dated July 27, 2016, by and between the University and Branch Banking and Trust Company, as trustee. The Series 2016 tax-exempt bonds have final maturities of January 1, 2039 for the Series bonds and January 1, 2041 and 2046 for the term bonds. The 2016 bonds maturing on January 1, 2040 and 2046 are subject to mandatory sinking fund redemptions through 2041 and 2046 with annual amounts of \$1,720 to \$2,930 and \$1,290 to \$3,485, respectively. Interest is payable each January 1 and July 1. The University's obligation under the loan agreement is an unsecured, unconditional obligation.

The University did not identify any other material subsequent events for recognition or disclosure.