

**NORTH CAROLINA  
TOBACCO FOUNDATION, INC.**

**FINANCIAL REPORT**

**JUNE 30, 2012 and 2011**

**North Carolina Tobacco Foundation, Inc.**

**Financial Statements**

**For the years ended June 30, 2012 and 2011**

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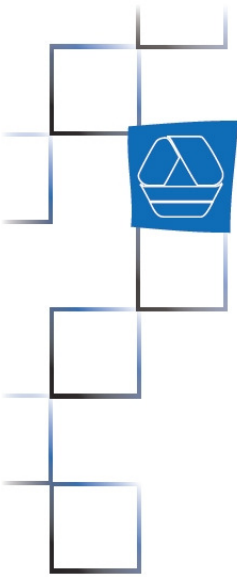
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**Williams Overman Pierce, LLP**  
Certified Public Accountants and Consultants

## **INDEPENDENT AUDITORS' REPORT**

To the Board of Directors  
North Carolina Tobacco Foundation, Inc.  
Raleigh, North Carolina

We have audited the accompanying statements of assets, liabilities, and net assets – modified cash basis of North Carolina Tobacco Foundation, Inc. (the “Foundation”), a nonprofit organization, as of June 30, 2012 and 2011, and the related statements of revenues, gains, and other income and support and changes in net assets – modified cash basis, and cash flows – modified cash basis for the years then ended. These financial statements are the responsibility of the Foundation’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 1 to the financial statements, these financial statements were prepared on the modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of North Carolina Tobacco Foundation, Inc. as of June 30, 2012 and 2011, and the changes in its net assets and its cash flows for the year then ended in conformity with the modified cash basis of accounting as described in Note 1.

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information on pages 16 through 18 is presented for purposes of additional analysis and is not a required part of the 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 financial statements. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentations of the supplementary information. However, we did not audit the information and express no opinion on it.

*Williams Overman Pierce, LLP*

Raleigh, North Carolina  
October 26, 2012

North Carolina Tobacco Foundation, Inc.

Statements of Assets, Liabilities, and Net Assets - Modified Cash Basis  
June 30, 2012 and 2011

	2012	2011
<b>ASSETS</b>		
Cash and cash equivalents (Note 1)	\$ 2,418,707	\$ 2,531,205
Intermediate investments (Note 1)	740,041	730,629
Marketable securities (Notes 1 and 3)	2,043,352	2,165,705
<b>Total assets</b>	<b>\$ 5,202,100</b>	<b>\$ 5,427,539</b>
<b>LIABILITIES AND NET ASSETS</b>		
Liabilities:		
Agency funds held in custody for others (Note 5)	\$ 728,546	\$ 837,513
Due to others (Note 1)	109	1,029
<b>Total liabilities</b>	<b>728,655</b>	<b>838,542</b>
Net assets:		
Unrestricted	588,763	621,474
Temporarily restricted (Note 7)	2,539,034	2,621,875
Permanently restricted (Note 8)	1,345,648	1,345,648
<b>Total net assets</b>	<b>4,473,445</b>	<b>4,588,997</b>
<b>Total liabilities and net assets</b>	<b>\$ 5,202,100</b>	<b>\$ 5,427,539</b>

North Carolina Tobacco Foundation, Inc.

Statements of Revenues, Gains, and Other Income and Support  
and Changes in Net Assets - Modified Cash Basis

Year Ended June 30, 2012

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains, and other income:				
Contributions (Note 1)	\$ 52,000	\$ 971,784	-	\$ 1,023,784
Donated services and facilities (Note 6)	18,800	-	-	18,800
Net investment income	9,894	46,826	-	56,720
Interest and dividends	15,905	4,246	-	20,151
Other income	-	12,336	-	12,336
Net assets released from restrictions (Note 9)	1,123,130	(1,123,130)	-	-
<b>Total revenues, gains, and other income</b>	<b>1,219,729</b>	<b>(87,938)</b>	<b>-</b>	<b>1,131,791</b>
Grants to support the University:				
Program:				
Scholarships and fellowships	259,230	-	-	259,230
Faculty support and professorships	473,175	-	-	473,175
Agricultural research support	54,092	-	-	54,092
Cooperative extension support	17,039	-	-	17,039
Departmental support	250,789	-	-	250,789
Other current services	142,435	-	-	142,435
<b>Total program support</b>	<b>1,196,760</b>	<b>-</b>	<b>-</b>	<b>1,196,760</b>
Administrative	33,800	-	-	33,800
Fundraising	16,783	-	-	16,783
<b>Total other support</b>	<b>50,583</b>	<b>-</b>	<b>-</b>	<b>50,583</b>
<b>Total support</b>	<b>1,247,343</b>	<b>-</b>	<b>-</b>	<b>1,247,343</b>
<b>Excess of revenues, gains, and other income over total support</b>	<b>(27,614)</b>	<b>(87,938)</b>	<b>-</b>	<b>(115,552)</b>
Net transfers:				
Among funds	(5,097)	5,097	-	-
<b>Total net transfers</b>	<b>(5,097)</b>	<b>5,097</b>	<b>-</b>	<b>-</b>
<b>Change in net assets</b>	<b>(32,711)</b>	<b>(82,841)</b>	<b>-</b>	<b>(115,552)</b>
Net assets:				
Beginning	621,474	2,621,875	1,345,648	4,588,997
Ending	\$ 588,763	\$ 2,539,034	\$ 1,345,648	\$ 4,473,445

North Carolina Tobacco Foundation, Inc.

Statements of Revenues, Gains, and Other Income and Support  
and Changes in Net Assets - Modified Cash Basis

Year Ended June 30, 2011

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains, and other income:				
Contributions (Note 1)	\$ 112,998	\$ 1,446,300	-	\$ 1,559,298
Donated services and facilities (Note 6)	13,800	-	-	13,800
Net asset reclassification - underwater endowments	1,364	(1,364)	-	-
Net investment income	9,095	272,153	-	281,248
Interest and dividends	22,958	7,967	-	30,925
Other income	13,258	-	-	13,258
Net assets released from restrictions (Note 9)	1,409,539	(1,409,539)	-	-
<b>Total revenues, gains, and other income</b>	<b>1,583,012</b>	<b>315,517</b>	<b>-</b>	<b>1,898,529</b>
Grants to support the University:				
Program:				
Scholarships and fellowships	420,363	-	-	420,363
Faculty support and professorships	595,625	-	-	595,625
Agricultural research support	47,663	-	-	47,663
Cooperative extension support	11,356	-	-	11,356
Departmental support	233,004	-	-	233,004
Other current services	172,975	-	-	172,975
<b>Total program support</b>	<b>1,480,986</b>	<b>-</b>	<b>-</b>	<b>1,480,986</b>
Administrative	27,995	-	-	27,995
Fundraising	22,897	-	-	22,897
<b>Total other support</b>	<b>50,892</b>	<b>-</b>	<b>-</b>	<b>50,892</b>
<b>Total support</b>	<b>1,531,878</b>	<b>-</b>	<b>-</b>	<b>1,531,878</b>
<b>Excess of revenues, gains, and other income over total support</b>	<b>51,134</b>	<b>315,517</b>	<b>-</b>	<b>366,651</b>
Net transfers:				
To other University-affiliated entity	-	(14,815)	(11,961)	(26,776)
Among funds	336	(336)	-	-
<b>Total net transfers</b>	<b>336</b>	<b>(15,151)</b>	<b>(11,961)</b>	<b>(26,776)</b>
<b>Change in net assets</b>	<b>51,470</b>	<b>300,366</b>	<b>(11,961)</b>	<b>339,875</b>
Net assets:				
Beginning	570,004	2,321,509	1,357,609	4,249,122
Ending	\$ 621,474	\$ 2,621,875	\$ 1,345,648	\$ 4,588,997

North Carolina Tobacco Foundation, Inc.

Statements of Cash Flows - Modified Cash Basis  
Years Ended June 30, 2012 and 2011

	2012	2011
Cash Flows From Operating Activities:		
Change in net assets	\$ (115,552)	\$ 339,875
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Net investment gains	(56,720)	(281,248)
Increase (decrease) in:		
Agency funds held in custody for others	(108,967)	(276,355)
Due to others	(920)	(123,054)
<b>Net cash used in operating activities</b>	<b>(282,159)</b>	<b>(340,782)</b>
Cash Flows From Investing Activities:		
Net proceeds from sales of investments	186,139	26,806
Net purchases of investments	(16,478)	55,831
<b>Net cash provided by investing activities</b>	<b>169,661</b>	<b>82,637</b>
<b>Net decrease in cash and cash equivalents</b>	<b>(112,498)</b>	<b>(258,145)</b>
Cash and cash equivalents:		
Beginning	2,531,205	2,789,350
Ending	<b>\$ 2,418,707</b>	<b>\$ 2,531,205</b>
Supplemental Disclosures of Noncash Activities:		
Donated services	\$ 18,800	\$ 13,800
Transfers among funds	<b>\$ 5,097</b>	<b>\$ 336</b>

## North Carolina Tobacco Foundation, Inc.

### Notes to Financial Statements For the years ended June 30, 2012 and 2011

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#### Note 1. Nature of Activities and Significant Accounting Policies

Nature of activities: The North Carolina Tobacco Foundation, Inc., ("Foundation") is one of a group of foundations which provides financial support exclusively to one or more of the colleges at North Carolina State University ("University"). The Foundation, established in 1975, provides aid and support for all types of extension and research pertaining to the production, manufacturing, and use of tobacco and tobacco products.

A summary of the Foundation's significant accounting policies follows:

Basis of accounting: The Foundation's policy is to prepare its financial statements on a modified cash basis of accounting which includes the recording of unrealized appreciation and depreciation in the value of its investments. The Foundation also recognizes a liability for future amounts due to grantors and/or beneficiaries of life income funds and a liability for amounts received by the Foundation on behalf of the University. Additionally, the Foundation recognizes donated services provided by the University Treasurer's Division. Under the modified cash basis of accounting, contributions and other revenues are recognized when collected, rather than when rights to receive transfer to the Foundation. Expenses are recognized when paid rather than when incurred. Pledges receivable are not included in the financial statements. Therefore, the accompanying financial statements are not intended to present financial position or changes in net assets in conformity with accounting principles generally accepted in the United States of America.

Basis of presentation: In preparing its financial statements, the Foundation's net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Foundation 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 may or will be met either by actions of the Foundation and/or by the passage of time.

Permanently restricted net assets - Net assets subject to donor-imposed stipulations that they be maintained permanently by the Foundation. Generally, the donors of these assets permit the Foundation to use all or part of the earnings on related investments for the donor-restricted purpose.

Cash and cash equivalents: For purposes of reporting cash flows, the Foundation considers all highly liquid debt instruments to be cash equivalents. Cash designated or restricted for long-term purposes is included with marketable securities. At times the Foundation places deposits with a high quality financial institution that may be in excess of federal insurance limits.

Cash and cash equivalents consist of accounts with BNY Mellon's Liquidity DIRECT, the State Treasurer's Short-Term Investment Fund ("STIF"), and an operating checking account with Wells Fargo Bank, N.A. The STIF account maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.



**North Carolina Tobacco Foundation, Inc.**

**Notes to Financial Statements  
For the years ended June 30, 2012 and 2011**

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**Note 1. Nature of Activities and Significant Accounting Policies (continued)**

Intermediate investments: Intermediate investments consist of an account with the commonfund Intermediate Term Fund for funds that can be invested for longer periods, but which are available in the event of short-term needs.

These investments are reported at readily determinable fair values of \$740,041 and \$730,629 at June 30, 2012 and 2011 respectively. The cost of these investments was \$826,718 as of June 30, 2012 and 2011.

Marketable securities: Long-term investments and marketable securities are stated at fair value based on readily determinable fair values, when available. Investments for which readily determinable fair values are not available are carried at estimated fair values as provided by the respective fund managers of the investments. The Foundation, in accordance with investment policies promulgated by its Board of Directors, utilizes services of the NC State Investment Fund, Inc. ("NCSIF").

Contributions: Restricted contributions are segregated for income and expense reporting purposes; however, the assets are commingled. When a donor or grantor restriction expires because the stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported as net assets released from restrictions in the statement of revenues, gains, and other income and support and changes in net assets - modified cash basis.

In fiscal year 2011, the University instituted a gift assessment program in support of Central Development and college-level fund-raising efforts. Beginning October 1, 2010, a one-time fee of 5% is assessed on gifts that support current operations and facilities, with 3% designated for Central Development and 2% designated to the fund-raising entity receiving the gift.

Investment income: Investment income is allocated on the basis of average fund balances for unrestricted and temporarily restricted net assets. For endowments, investment income is allocated on the "unit value" method of valuing interest in an investment portfolio and the investment earnings are recorded as unrestricted, temporarily restricted, or permanently restricted, as appropriate. Earnings from investments are net of investment fees of approximately \$8,575 and \$8,500 for the years ended June 30, 2012 and 2011, respectively. Gains and losses on sales of investments are allocated on the unit value method. Investment income on investments owned individually by one fund is directly allocated to the owning fund.

As part of the University's gift assessment program, beginning October 1, 2010, an annual fee of 0.50% is assessed on the average twenty-quarter average market value of assets held in the investment portfolio, with 0.25% designated for Central Development and 0.25% designated to college-level fund-raising efforts. In addition, an assessment of 0.50% is charged by the Foundation on the average twenty-quarter average market value of the assets held in the investment portfolio, for the support of Foundation fund-raising activities.

Due to others: Due to others at June 30, 2012 and 2011 consisted of \$109 and \$1,029, respectively, primarily due to North Carolina State University.

**North Carolina Tobacco Foundation, Inc.**

**Notes to Financial Statements  
For the years ended June 30, 2012 and 2011**

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**Note 1. Nature of Activities and Significant Accounting Policies (continued)**

Estimates: The preparation of financial statements in conformity with the modified cash basis of accounting requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Income taxes and uncertain tax positions: The Foundation is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and is classified as other than a private foundation. The Foundation had no significant unrelated trade or business income for 2012 and 2011. Therefore, no provision for income taxes has been reflected in the accompanying financial statements.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the organization and recognize a tax liability (or asset) if the organization has taken an uncertain position that more likely than not would be sustained upon examination by the IRS. Management has analyzed the tax positions taken by the Foundation, and has concluded that as of June 30, 2012, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements. The Foundation is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. Management believes it is no longer subject to income tax examinations for years prior to 2008.

**Note 2. Endowment**

The Foundation's endowment consists of seven individual funds established for a variety of purposes related to the mission of the University. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions. The majority of the Foundation's signed endowment gift agreements with donors have donor-imposed restrictions which stipulate that principal shall not be used to fund spending.

Interpretation of relevant law:

The Uniform Prudent Management of Institutional Funds Act ("UPMIFA") was adopted in North Carolina as NC General Statute 36E effective March 17, 2009. UPMIFA defines a prudence standard for management and investment of institutional funds. As a result of the Foundation's interpretation of UPMIFA, the Foundation classifies 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 that are required by the applicable donor gift instrument. The remaining 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 foundation's endowment spending policy.

Funds with deficiencies:

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the original gift value. These deficiencies generally result from unfavorable market fluctuations which produce unrealized losses to the fund. Deficiencies of this nature are reported in unrestricted net assets, and were \$0 as of June 30, 2012 and 2011.

**North Carolina Tobacco Foundation, Inc.**

**Notes to Financial Statements  
For the years ended June 30, 2012 and 2011**

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**Note 2. Endowment (continued)**

Investment return objectives and risk parameters:

The Foundation has adopted investment and spending policies for endowment assets that attempt to provide a stable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity or for donor-specified periods as well as board-designated funds. The endowment assets are invested through the NCSIF in a manner that is intended to produce results that exceed a 70% S&P 500 Index/30% Barclays Aggregate Bond Index benchmark over rolling five and ten year periods while assuming a moderate level of investment risk.

Spending policy:

The Foundation has a policy of appropriating for programmatic spending each year 4% of its endowment fund's average market value over the prior twenty quarters through the fiscal year-end preceding the fiscal year in which the spending is planned. This is consistent with the Foundation's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return. However, in declining market conditions, many endowments are not able to fund spending at the 4% level. Unless the gift instrument specifies otherwise, up to 15% of the corpus of an endowment may be expended if reserves are not sufficient to fund the programmatic spending amount, subject to the guidelines provided by UPMIFA. However, if the gift instrument does not allow spending of corpus, the Foundation does not initiate or renew spending for the individual endowments affected by declining market conditions until their market value has been recovered and exceeds their original gift value. In establishing the spending policy, the Foundation considered the long-term expected return on its endowment. Spending budgets were calculated at \$81,295 and \$77,655 for fiscal years 2012 and 2013, respectively.

Strategies employed for achieving investment objectives:

For the long term, the primary investment objective for the NCSIF is to earn a total return (net of investment and custodial fees), within prudent levels of risk, which is sufficient to maintain in real terms the purchasing power of the NCSIF and to meet the spending needs of the University. To meet this investment objective, the NCSIF invests in various asset classes to offer diversification. The purpose of diversification is to provide reasonable assurance that no single security or class of securities or manager will have a disproportionate impact on the performance of the total fund.

NCSIF's investments are diversified both by asset class (e.g. common stocks and fixed income securities) and within asset classes (e.g., within common stocks by economic sector, geographic area, industry, quality, and size). In addition, the NCSIF seeks to diversify exposure to all asset classes through the use of multiple managers that use a variety of investment approaches.

North Carolina Tobacco Foundation, Inc.

Notes to Financial Statements  
For the years ended June 30, 2012 and 2011

**Note 2. Endowment (continued)**

The following represents changes in endowment net assets for the fiscal year ended June 30, 2012:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Endowment net assets, beginning of year</b>	<b>\$ 13,450</b>	<b>\$ 769,972</b>	<b>\$ 1,345,648</b>	<b>\$ 2,129,070</b>
Net asset reclassification - underwater endowments	-	-	-	-
Endowment net assets after reclassification	13,450	769,972	1,345,648	2,129,070
Total investment return	(169)	45,979	-	45,810
Appropriations of endowment assets for expenditure	(820)	(130,708)	-	(131,528)
Other changes:				
Transfers	-	-	-	-
<b>Endowment net assets, end of year</b>	<b>\$ 12,461</b>	<b>\$ 685,243</b>	<b>\$ 1,345,648</b>	<b>\$ 2,043,352</b>

The following represents endowment net asset composition by type of fund, as of June 30, 2012:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor restricted endowment funds	<b>\$ 12,461</b>	<b>\$ 685,243</b>	<b>\$ 1,345,648</b>	<b>\$ 2,043,352</b>
<b>Total funds</b>	<b>\$ 12,461</b>	<b>\$ 685,243</b>	<b>\$ 1,345,648</b>	<b>\$ 2,043,352</b>

The following represents changes in endowment net assets for the fiscal year ended June 30, 2011:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ 12,687	\$ 607,743	\$ 1,357,609	\$ 1,978,039
Net asset reclassification - underwater endowments	1,364	(1,364)	-	-
Endowment net assets after reclassification	14,051	606,379	1,357,609	1,978,039
Total investment return	299	257,161	-	257,460
Appropriations of endowment assets for expenditure	(900)	(93,568)	-	(94,468)
Other changes:				
Transfers	-	-	(11,961)	(11,961)
Endowment net assets, end of year	\$ 13,450	\$ 769,972	\$ 1,345,648	\$ 2,129,070

**North Carolina Tobacco Foundation, Inc.**

**Notes to Financial Statements  
For the years ended June 30, 2012 and 2011**

**Note 2. Endowment (continued)**

The following represents endowment net asset composition by type of fund, as of June 30, 2011:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor restricted endowment funds	13,450	769,972	1,345,648	2,129,070
Total funds	<u>\$ 13,450</u>	<u>\$ 769,972</u>	<u>\$ 1,345,648</u>	<u>\$ 2,129,070</u>

**Note 3. Long-Term Investments**

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

Investments at June 30, 2012 and 2011 consisted of:

	2012		2011	
	Cost	Fair Value	Cost	Fair Value
STIF	\$ 8,389	\$ 8,389	\$ -	\$ -
NC State Investment Fund, Inc.	1,959,983	2,034,963	2,131,302	2,165,705
	<u>\$ 1,968,372</u>	<u>\$ 2,043,352</u>	<u>\$ 2,131,302</u>	<u>\$ 2,165,705</u>

Investments held by the NCSIF at June 30, 2012 were made up of limited partnerships and the State Treasurer's Short Term Investment Fund ("STIF"). As of June 30, 2012, approximately 87% of these limited partnerships were with the UNC Management Company ("UNCMC"), 7% were committed to or in other private equity investments with JP Morgan, Blackrock, and SEI, and 6% invested in the STIF. NCSIF's net assets were valued at approximately \$397,192,000 and \$378,260,000 at June 30, 2012 and 2011, respectively. The Foundation's investment in NCSIF represents approximately 0.5% and 1.0% of the member's equity of NCSIF at June 30, 2012 and 2011, respectively.

North Carolina Tobacco Foundation, Inc.

Notes to Financial Statements  
For the years ended June 30, 2012 and 2011

**Note 4. Fair Value Measurement**

The Fair Value Measurements and Disclosures Topic of the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 820 provides a framework for measuring fair value under generally accepted accounting principles. ASC 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC 820 requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs. ASC 820 also establishes a fair value hierarchy, which prioritizes the valuation inputs into three broad levels.

The fair value hierarchy of inputs is summarized in the three broad levels listed below:

Level 1 – quoted prices in active markets for identical investments

Level 2 – other significant observable inputs (including quoted prices for similar investments, interest rates, credit risks, etc.)

Level 3 – significant unobservable inputs (including the fund’s own assumptions in determining the fair value of investments)

To measure fair value, there are three general valuation techniques that may be used, as described below:

A) Market approach – Uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. Prices may be indicated by pricing guides, sales transactions, market trades, or other sources

B) Cost approach – Based on the amount that currently would be required to replace the service capacity of an asset (replacement cost); and

C) Income approach – Uses valuation techniques to convert future amounts to a single present value amount based on current market expectations about the future amounts (includes present value techniques and option-pricing models). Net present value is an income approach where a stream of expected cash flows is discounted at an appropriate market interest rate.

Assets itemized below are measured at fair value on a recurring basis using both market and income approaches. The market approach was used for level 2 and the income approach was used for level 3. While the NCSIF is categorized below as a Level 3 investment, as a member of the UNCMC, the NCSIF has full redemption privileges with a 60 day notice requirement.

	2012			
	Level 1	Level 2	Level 3	Total Fair Value
commonfund Intermediate Term Fund	\$ -	\$ 740,041	\$ -	\$ 740,041
STIF	8,389	-	-	8,389
NC State Investment Fund, Inc.	-	-	2,034,963	2,034,963
	<b>\$ 8,389</b>	<b>\$ 740,041</b>	<b>\$ 2,034,963</b>	<b>\$ 2,783,393</b>

	2011			
	Level 1	Level 2	Level 3	Total Fair Value
commonfund Intermediate Term Fund	\$ -	\$ 730,629	\$ -	\$ 730,629
NC State Investment Fund, Inc.	-	-	2,165,705	2,165,705
	<b>\$ -</b>	<b>\$ 730,629</b>	<b>\$ 2,165,705</b>	<b>\$ 2,896,334</b>

**North Carolina Tobacco Foundation, Inc.**

**Notes to Financial Statements  
For the years ended June 30, 2012 and 2011**

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**Note 4. Fair Value Measurement (continued)**

The following is a reconciliation of the assets measured at fair value on a recurring basis in which significant unobservable inputs (Level 3) were used in determining value:

	<u>2012</u>	<u>2011</u>
	<u>NC State Investment Fund, Inc.</u>	<u>NC State Investment Fund, Inc.</u>
Beginning Balance	\$ 2,165,705	\$ 1,764,846
Unrealized gain on investments	40,577	276,347
Realized gain on investments	15,283	2,297
Net investment income	(186,602)	122,215
Ending balance	<u>\$ 2,034,963</u>	<u>\$ 2,165,705</u>

**Note 5. Agency Funds**

The Foundation has a directed fund agreement with the Tobacco Education and Research Council, Inc. ("TERC") to maintain proceeds of a settlement agreement with Philip Morris USA. Under this agreement, the funds are held by the Foundation and used for land grant university tobacco programs, continuing support of tobacco farmer projects to improve the quality of leaf tobacco, and to reduce Tobacco Specific Nitrosamines and/or suspected harmful substances in the tobacco leaf. For the years ended June 30, 2012 and 2011, agency funds were \$728,546 and \$837,513, respectively.

**Note 6. Donated Services and Facilities**

Donated services in the amount of \$15,000 and \$10,000 for the years ended June 30, 2012 and 2011, respectively, have been reflected in the financial statements for services provided by the University Treasurer's Division. In addition, donated facilities provided by the University for college development in the amount of \$3,800 for the years ended June 30, 2012 and 2011, have been reflected in the financial statements.

**Note 7. Temporarily Restricted Net Assets**

Temporarily restricted net assets at June 30, 2012 and 2011 are available for the following purposes:

	<u>2012</u>	<u>2011</u>
Scholarships	\$ 57,058	\$ 48,626
Fellowships	67,969	75,547
Professorships	178,887	196,121
Research and related support	907,991	1,015,436
Endowment cumulative balance	685,243	769,972
Other	641,886	516,173
	<u>\$ 2,539,034</u>	<u>\$ 2,621,875</u>

Temporarily restricted net asset grouping "Other" includes amounts designated for general college support, research, and funds with multiple purposes.

North Carolina Tobacco Foundation, Inc.

Notes to Financial Statements  
For the years ended June 30, 2012 and 2011

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**Note 8. Permanently Restricted Net Assets**

Permanently restricted net assets at June 30, 2012 and 2011 are restricted to:

	<u>2012</u>	<u>2011</u>
Investment in perpetuity, the income from which is expendable to support:		
Scholarships	\$ 572,016	\$ 600,024
Professorships	1,428,329	1,484,554
Amounts reported as unrestricted or temporarily restricted net assets	(697,704)	(783,422)
Other	43,007	44,492
	<u>\$ 1,345,648</u>	<u>\$ 1,345,648</u>

Permanently restricted net asset grouping "Other" includes amounts designated for general college support, research, and funds with multiple purposes.

**Note 9. Net Assets Released From Donor Restrictions**

Net assets were released from donor restrictions as restrictions were met via the passage of time or by incurring expenses satisfying the restricted purposes specified by donors as follows:

	<u>2012</u>	<u>2011</u>
Scholarships	\$ 56,388	\$ 59,086
Fellowships	57,927	23,305
Professorships	76,431	67,822
Research and related support	799,623	846,303
Other	132,761	413,023
	<u>\$ 1,123,130</u>	<u>\$ 1,409,539</u>

The grouping "Other" includes amounts spent for general college support, research, and funds with multiple purposes.



**North Carolina Tobacco Foundation, Inc.**

**Notes to Financial Statements  
For the years ended June 30, 2012 and 2011**

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**Note 10. Prior Year Reclassifications and Restatement**

Certain amounts in the 2011 financial statements have been reclassified to conform to the 2012 presentation with no effect on previously reported total net assets.

During fiscal year 2012, the Foundation determined that the Foundation's donated services and salaries and fundraising were understated in the fiscal year 2011 by \$3,800 due to a prior year reporting error identified by management with no effect on previously reported total net assets.

For the year ended June 30, 2011, the ending net assets have been modified due to a prior year reporting error identified by management with no effect on previously reported total net assets. As a result unrestricted net assets and temporarily restricted net assets are \$1,484 lower and \$1,484 higher, respectively, than the amounts previously reported.

Statement of assets, liabilities, and net assets – modified cash basis at June 30, 2011 has been restated as follows:

	2011 as previously reported	Restatement	2011 as restated
Net Assets:			
Unrestricted	\$ 622,958	\$ (1,484)	\$ 621,474
Temporarily restricted	2,620,391	1,484	2,621,875
Permanently restricted	1,345,648	-	1,345,648
Total net assets	<u>\$ 4,588,997</u>	<u>\$ -</u>	<u>\$ 4,588,997</u>

Statement of revenues, gains, and other income and support and changes in net assets – modified cash basis for the year ended June 30, 2011 has been restated as follows:

	2011 as previously reported	Restatement	2011 as restated
Donated services and salaries	\$ 10,000	\$ 3,800	\$ 13,800
Fundraising	(24,195)	(3,800)	(27,995)
Change in net assets	<u>\$ (14,195)</u>	<u>\$ -</u>	<u>\$ (14,195)</u>

**Note 11. Subsequent Events**

The Foundation has evaluated subsequent events through October 26, 2012, the date which the financial statements were available to be issued, and there were none to report.

## **SUPPLEMENTARY INFORMATION**

North Carolina Tobacco Foundation, Inc.

General Fund Budget vs. Actual - Unaudited  
Year Ended June 30, 2012

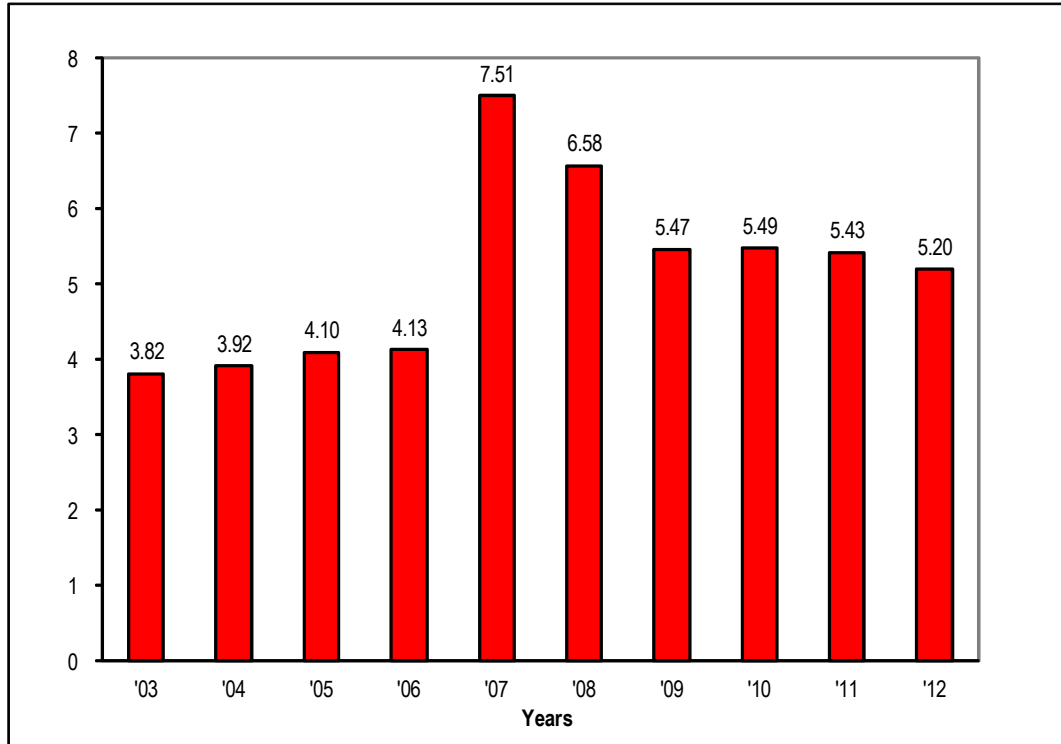
	Budget	Actual	Variance
Income:			
Contributions	\$ 130,000	\$ 49,400	\$ (80,600)
Interest and dividends	21,000	17,951	(3,049)
Endowment assessment	2,760	2,695	(65)
Grant administration fee	5,000	-	(5,000)
<b>Total income</b>	<b>158,760</b>	<b>70,046</b>	<b>(88,714)</b>
Support:			
Program support	113,001	71,130	(41,871)
Endowment fee transferred to University Advancement	2,760	2,695	(65)
Foundation administration	38,450	31,588	(6,862)
<b>Total support</b>	<b>154,211</b>	<b>105,413</b>	<b>(48,798)</b>
<b>Income less support</b>	<b>4,549</b>	<b>(35,367)</b>	<b>(39,916)</b>
General fund balance:			
Beginning	701,070	701,070	-
Ending	\$ 705,619	\$ 665,703	\$ (39,916)

# North Carolina Tobacco Foundation, Inc.

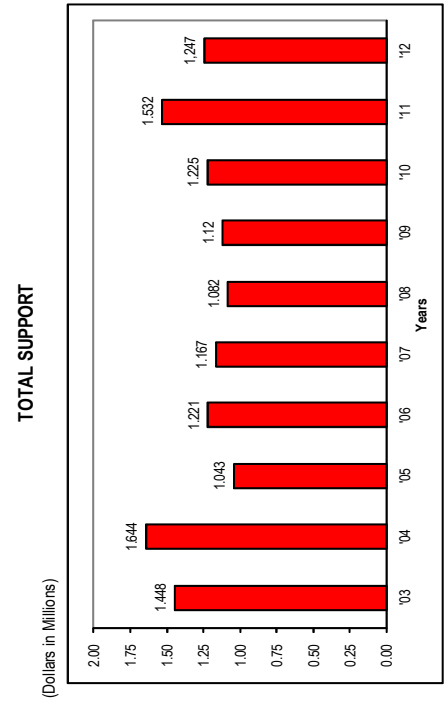
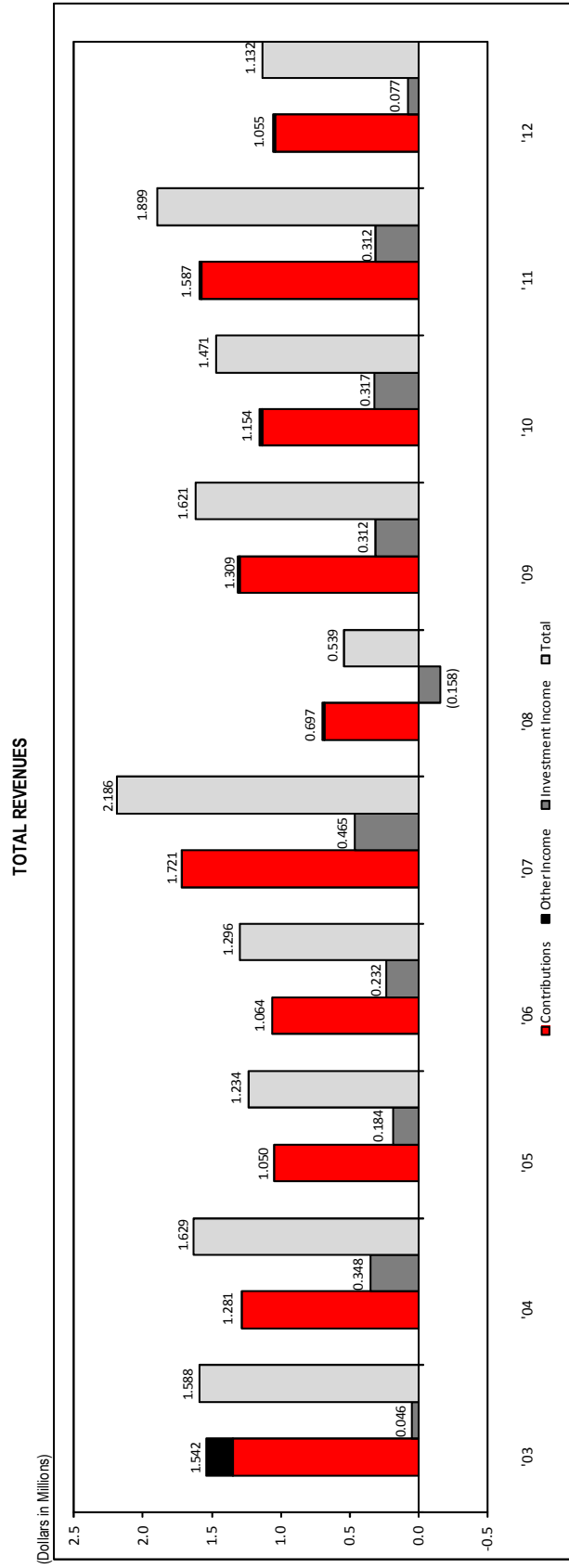
## Ten Year Summary of Assets - Unaudited Fiscal Years Ended June 30

### TOTAL ASSETS

(Dollars in Millions)



**North Carolina Tobacco Foundation, Inc.**  
**Ten Year Summary of Revenues and Support - Unaudited**  
**Fiscal Years Ended June 30**



## **OTHER INFORMATION**



**Williams Overman Pierce, LLP**  
Certified Public Accountants and Consultants

October 26, 2012

To the Board of Directors  
North Carolina Tobacco Foundation, Inc.  
Raleigh, North Carolina

We have audited the financial statements of North Carolina Tobacco Foundation, Inc. (the "Foundation"), a nonprofit organization, for the year ended June 30, 2012, and have issued our report thereon dated October 26, 2012. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our engagement letter to you dated June 13, 2012. Professional standards also require that we communicate to you the following information related to our audit.

**Significant Audit Findings**

*Qualitative Aspects of Accounting Practices*

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by North Carolina Tobacco Foundation, Inc. are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2012. We noted no transactions entered into by the Foundation during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected.

The financial statement disclosures are neutral, consistent, and clear.

*Difficulties Encountered in Performing the Audit*

We encountered no significant difficulties in dealing with management in performing and completing our audit.

*Corrected and Uncorrected Misstatements*

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. No material misstatements were identified as a result of audit procedures and as such, no adjustments were necessary.



### *Disagreements with Management*

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditors' report. We are pleased to report that no such disagreements arose during the course of our audit.

### *Management Representations*

We have requested certain representations from management that are included in the management representation letter dated October 26, 2012.

### *Management Consultations with Other Independent Accountants*

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the Foundation's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

### *Other Audit Findings or Issues*

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Foundation's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

### **Other Matters**

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles selected by the Foundation, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves. However, we did not audit the supplementary information and, therefore, do not express an opinion on it.

### **Closing**

We are happy to respond to any questions you may have concerning this communication. We appreciate the opportunity to continue to serve the North Carolina Tobacco Foundation, Inc.

This information is intended solely for the use of the Board of Directors and management of North Carolina Tobacco Foundation, Inc. and is not intended to be and should not be used by anyone other than these specified parties.

*Williams Dverman Pierce, LLP*