

Cone Health Foundation

Financial Statements as of and for the Years Ended
September 30, 2014 and 2013, and
Independent Auditors' Report

CONE HEALTH FOUNDATION

TABLE OF CONTENTS

	Page
INDEPENDENT AUDITORS' REPORT	1-2
FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED SEPTEMBER 30, 2014 AND 2013:	
Statements of Financial Position	3
Statements of Activities and Changes in Net Assets	4
Statements of Cash Flows	5
Notes to Financial Statements	6-12

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Cone Health Foundation:

We have audited the accompanying financial statements of Cone Health Foundation (the "Foundation"), which comprise the statements of financial position as of September 30, 2014 and 2013, and the related statements of activities and changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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 audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Foundation's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Foundation's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Foundation as of September 30, 2014 and 2013, and the results of its activities and changes in net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

March 10, 2015

CONE HEALTH FOUNDATION

STATEMENTS OF FINANCIAL POSITION AS OF SEPTEMBER 30, 2014 AND 2013

	2014	2013
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 698,407	\$ 417,305
Investments—short term	129,281	424,760
Other current assets	<u>832</u>	<u>1,027</u>
Total current assets	828,520	843,092
INVESTMENTS—Long term	<u>113,826,179</u>	<u>112,269,367</u>
TOTAL	<u>\$ 114,654,699</u>	<u>\$ 113,112,459</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Grants payable—current	4,393,297	4,092,335
Accounts payable and accrued expenses	<u>132,430</u>	<u>131,725</u>
Total current liabilities	4,525,727	4,224,060
GRANTS PAYABLE—Net of current portion	<u>25,000</u>	<u>4,326,210</u>
Total liabilities	4,550,727	8,550,270
UNRESTRICTED NET ASSETS	<u>110,103,972</u>	<u>104,562,189</u>
TOTAL	<u>\$ 114,654,699</u>	<u>\$ 113,112,459</u>

See notes to financial statements.

CONE HEALTH FOUNDATION

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS FOR THE YEARS ENDED SEPTEMBER 30, 2014 and 2013

	2014	2013
REVENUES:		
Dividends and interest	\$ 1,477,948	\$ 1,876,256
Other operating revenue	5,872	17,404
Realized gains on investments	<u>2,723,079</u>	<u>3,448,993</u>
Total revenues	<u>4,206,899</u>	<u>5,342,653</u>
EXPENSES:		
Grants awarded	503,966	1,718,398
Wages and benefits	733,859	702,138
Investment management fees	326,947	380,248
General and administrative expenses	320,207	259,584
Consulting fees	<u>188,819</u>	<u>44,966</u>
Total expenses	<u>2,073,798</u>	<u>3,105,334</u>
EXCESS OF REVENUES OVER EXPENSES	2,133,101	2,237,319
CHANGE IN UNREALIZED GAINS ON INVESTMENTS—Net	<u>3,408,682</u>	<u>2,707,209</u>
CHANGE IN UNRESTRICTED NET ASSETS	5,541,783	4,944,528
NET ASSETS—Beginning of year	<u>104,562,189</u>	<u>99,617,661</u>
NET ASSETS—End of year	<u>\$ 110,103,972</u>	<u>\$ 104,562,189</u>

See notes to financial statements.

CONE HEALTH FOUNDATION

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED SEPTEMBER 30, 2014 AND 2013

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	\$ 5,541,783	\$ 4,944,528
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Change in unrealized gains on investments—net	(3,408,682)	(2,707,209)
Net realized gains on sale of investments	(2,723,079)	(3,448,993)
Purchase of trading securities	(1,489,964)	(2,026,292)
Proceeds from sale of trading securities	2,437,201	3,829,656
Changes in:		
Other assets	195	(110)
Grants payable	(4,000,248)	(2,884,313)
Accounts payable and accrued expenses	<u>705</u>	<u>15,184</u>
Net cash used in operating activities	<u>(3,642,089)</u>	<u>(2,277,549)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of investments	(32,370,170)	(99,489,954)
Sale of investments	<u>36,293,361</u>	<u>100,766,164</u>
Net cash provided by investing activities	<u>3,923,191</u>	<u>1,276,210</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	281,102	(1,001,339)
CASH AND CASH EQUIVALENTS:		
Beginning of year	<u>417,305</u>	<u>1,418,644</u>
End of year	<u>\$ 698,407</u>	<u>\$ 417,305</u>

See notes to financial statements.

CONE HEALTH FOUNDATION

NOTES TO FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED SEPTEMBER 30, 2014 AND 2013

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization—The Moses Cone—Wesley Long Community Health Foundation, Inc. (dba Cone Health Foundation) (the “Foundation”) was incorporated on December 2, 1996, as a North Carolina nonprofit corporation by Wesley Long Community Hospital. On October 1, 1997, the Wesley Long Community Hospital and The Moses H. Cone Memorial Hospital merged. An outcome of the merger was the consolidation of the community health program of the Moses Cone Health System (the “Health System”) with the Foundation. The purpose of the Foundation is to invest in the development and support of activities, programs, and organizations that measurably improve the health of people in the greater Greensboro Area. The Foundation is a 509(a)(3) supporting organization of the Health System.

The Foundation’s board of directors (the “Board of Directors”) has sole authority over the disbursements of net assets and consists of 17 members. The Board of Directors is composed of two ex officio members (the chairman and vice chairman of the Health System or their designees), eight members appointed by the Health System, and seven self-perpetuating members.

Use of Estimates—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (US GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Risks and Uncertainties—The Foundation invests in debt and equity investment securities that are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risks in the near term would materially affect the investment balances in the financial statements.

Cash and Cash Equivalents—Cash and cash equivalents are held in the Foundation’s operating bank account and include demand deposits and certain investments in highly liquid debt instruments with original maturities at the time of purchase of three months or less.

Investments—Investment assets of the Foundation are to be used at the direction of the Board of Directors to accomplish the stated purpose of the Foundation. Investments in equity securities with readily determinable fair values, investments in common/commingled/collective trusts, and all investments in debt securities are measured at fair value in the accompanying balance sheets and are generally classified as available for sale, with the exception of certain securities held in managed accounts, which are classified as trading. Interest, dividends, and realized gains and losses on available-for-sale investments (including other than temporary impairment) and all changes in fair value for trading securities are included in revenues in the accompanying statements of activities and changes in net assets. Changes in unrealized gains and losses on available-for-sale investments are reported separately in the accompanying statements of activities and changes in net assets and are excluded from the excess of revenues over expenses. Interests in alternative investments, whose operating and financial policies the Foundation’s management has virtually no influence over, are measured at cost in the accompanying balance sheets.

Fair Value Measurements—US GAAP 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 at the measurement date. Additionally, the inputs used to measure fair value are prioritized based on a three-level hierarchy. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

Level 1—Valuations based on unadjusted quoted prices for identical instruments in active markets that are available as of the measurement date

Level 2—Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly

Level 3—Valuations based on inputs that are unobservable and significant to the overall fair value measurement

US GAAP permits, as a practical expedient, a reporting entity to measure the fair value of certain investments without readily determinable fair values by using the reported net asset value (NAV) per share of the investment without further adjustment if the investment is in an entity that meets the description of an investment company whose underlying investments are measured at fair value as set forth in the Accounting Standards Codification.

The fair values of investments in common/commingled/collective trusts, which are recorded at fair value in the statements of financial position, and alternative investments, which are recorded at cost in the statements of financial position and disclosed at fair value in Note 2, are measured using the NAV per share reported by the respective fund managers or the general partners.

The estimated fair values of certain alternative investments, such as private equity interests, are based on valuations performed prior to the balance sheet date by the external investment managers and adjusted for cash receipts, cash disbursements, and securities distributions through September 30. Because alternative investments are not readily marketable, their estimated fair value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for such investments existed. Such differences could be material.

The Foundation's management, with the assistance of a third-party investment consultant, where appropriate, evaluates the NAV information and valuations provided by external fund managers or general partners for appropriateness through review of the most recently available annual audited financial statements and unaudited interim reporting for the respective funds, review of the methodologies used to determine fair value, and comparisons of fund performance to market benchmarks.

The carrying amounts of cash equivalents, accounts payable, and grants payable approximates fair value based on the nature and short duration of these accounts.

Transfers between Levels—The availability of market observable data is monitored to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or valuation methodologies may require the transfer of financial instruments from one fair value hierarchy level to another. In such instances, the transfer would be reported at the beginning of the reporting period. The Foundation evaluates the significance of transfers based on the nature of the financial instrument and the size of the transfer. There were no transfers of investments between levels for the years ending September 30, 2014 and 2013.

Grant Expense—The Foundation records grants as expense in the fiscal year in which the grants are authorized by the Board of Directors and awarded to the recipient.

Income Taxes—The Foundation is organized as a corporation exempt from federal and state income taxes under Internal Revenue Code Section 501(c)(3) and North Carolina laws.

Subsequent Events—The Foundation has evaluated events and transactions occurring after September 30, 2014, and through March 10, 2015 (the date these financial statements were available to be issued), for potential recognition or disclosure. No events or transactions were identified that would require recognition or disclosure in the financial statements.

Recently Issued Accounting Guidance—In February 2013, the Financial Accounting Standards Board (FASB) issued ASU No. 2013-04, *Liabilities (Topic 405): Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation Is Fixed at the Reporting Date*. ASU No. 2013-04 provides guidance for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this guidance is fixed at the reporting date. ASU No. 2013-04 requires entities to measure these obligations as the sum of the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. ASU No. 2013-04 is effective for nonpublic entities for fiscal years ending after December 15, 2014. The Foundation is currently evaluating the provisions of this update and its impact on its financial statements.

In June 2013, the FASB issued ASU No. 2013-06, *Not-for-Profit Entities (Topic 958): Services Received from Personnel of an Affiliate*. ASU No. 2013-06 addresses the diversity in practice about what guidance not-for-profit entities should apply for recognizing and measuring personnel services received from an affiliate, that is, a party that directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with the recipient not-for-profit entity. The new guidance is effective for fiscal years beginning after June 15, 2014. The Foundation is currently evaluating the provisions of this update and their impact on its financial statements.

2. INVESTMENTS

At September 30, 2014, the composition of the Foundation's investments, recorded at fair value within long-term investments, is as follows:

	Fair Value Measurement Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Fixed-income funds and securities	\$ 21,322,983	\$ 4,810,042	\$ -	\$ 26,133,026
U.S. equity funds and securities	11,159,300	9,329,407		20,488,707
International equity securities funds		25,115,019		25,115,019
Commodity securities funds		1,996,012		1,996,012
	<u>\$ 32,482,284</u>	<u>\$ 41,250,480</u>	<u>\$ -</u>	<u>\$ 73,732,764</u>

At September 30, 2013, the composition of the Foundation's investments, recorded at fair value within long-term investments, is as follows:

	Fair Value Measurement Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Fixed-income funds and securities	\$ 25,143,815	\$ 4,926,000	\$ -	\$ 30,069,815
U.S. equity funds and securities	12,000,713	6,839,480		18,840,193
International equity securities funds		20,122,936		20,122,936
Commodity securities funds		2,146,919		2,146,919
Emerging market funds		2,688,472		2,688,472
	<u>\$ 37,144,528</u>	<u>\$ 36,723,807</u>	<u>\$ -</u>	<u>\$ 73,868,335</u>

Alternative investments include limited partnerships, limited liability corporations, and offshore investments funds. Included in investments of the limited partnerships are certain types of financial instruments, including, among others, futures and forward contracts, options, and securities sold not yet purchased, intended to hedge against changes in the market value of investments. These financial instruments, which involve varying degrees of off-balance-sheet risk, may result in loss due to changes in the market (market risk). Alternative investments are less liquid compared to the Foundation's other investments.

The Foundation's alternative investments recorded at cost within long-term investments at September 30, 2014 and 2013, are summarized in the following table:

	2014		2013	
	Cost	Estimated Fair Value (Level 3)	Cost	Estimated Fair Value (Level 3)
Private equity funds	\$ 3,703,165	\$ 4,799,771	\$ 2,150,248	\$ 2,583,526
Private debt funds	7,265,520	9,536,395	5,924,886	7,553,553
Hedge funds	16,313,074	18,554,656	16,156,457	17,506,099
Risk parity funds	9,137,636	10,660,329	10,549,627	11,025,990
Real estate funds	3,674,020	4,313,173	3,619,814	3,974,816
	<u>\$ 40,093,415</u>	<u>\$ 47,864,324</u>	<u>\$ 38,401,032</u>	<u>\$ 42,643,984</u>

A summary of the investments with a reported NAV recorded within investments as of September 30, 2014, is as follows:

	Fair Value	Unfunded Commitment	Redemption Frequency	Redemption Notice Period
Investments in common, comingled, and collective trust funds:				
Equity securities	\$ 32,530,009	\$ -	Daily and monthly	1 day to 30 days
Equity securities	1,914,417		End of any calendar quarter	65 days
Fixed-income securities	4,810,042		Daily and monthly	1 day to 30 days
Commodity Securities	<u>1,996,012</u>	<u> </u>	Daily	None
	<u>\$ 41,250,480</u>	<u>\$ -</u>		
Alternative investment funds:				
Private equity	\$ 4,799,771	\$ 4,758,064	N/A—Illiquid	N/A—Illiquid
Private debt	1,586,287	847,030	N/A—Illiquid	N/A—Illiquid
Private debt	5,904,614	196,798	Quarterly	60 day to 90 days
Hedge funds	11,098,503		Monthly and quarterly	30 day to 90 days
Hedge funds	9,501,647		Daily, monthly, and quarterly	1 day to 90 days
Risk parity	10,660,329		Monthly	15 days
Real estate	<u>4,313,173</u>	<u> </u>	Quarterly	90 days
	<u>\$ 47,864,324</u>	<u>\$ 5,801,892</u>		

A summary of the investments with a reported NAV recorded within investments as of September 30, 2013, is as follows:

	Fair Value	Unfunded Commitment	Redemption Frequency	Redemption Notice Period
Investments in common, comingled, and collective trust funds:				
Equity securities	\$ 28,321,161	\$ -	Daily and monthly	1 day to 30 days
Equity securities	1,329,727		End of any calendar quarter	65 days
Fixed-income securities	4,926,000		Daily and monthly	1 day to 30 days
Commodity securities	<u>2,146,919</u>	<u> </u>	Daily	None
	<u>\$ 36,723,807</u>	<u>\$ -</u>		
Alternative investment funds:				
Private equity	\$ 2,583,526	\$ 2,878,944	N/A—Illiquid	N/A—Illiquid
Private debt	1,125,287	1,460,815	N/A—Illiquid	N/A—Illiquid
Private debt	5,476,224	110,114	Quarterly	60 day to 90 days
Hedge funds	8,660,940		Monthly and quarterly	30 day to 90 days
Hedge funds	9,797,201	1,025,394	Daily, monthly, and quarterly	1 day to 90 days
Risk parity	11,025,990		Monthly	15 days
Real estate	<u>3,974,816</u>	<u> </u>	Quarterly	90 days
	<u>\$ 42,643,984</u>	<u>\$ 5,475,267</u>		

At September 30, 2014 and 2013, the reported amount of the Foundation's long-term investment assets was as follows:

	2014	2013
Equity funds and securities	\$ 20,488,708	\$ 18,840,193
International equity securities funds	25,115,019	20,122,936
Fixed-income funds and securities	26,133,025	30,069,815
Commodity securities funds	1,996,012	2,146,919
Emerging market funds		2,688,472
Alternative investments	<u>40,093,415</u>	<u>38,401,032</u>
	<u>\$ 113,826,179</u>	<u>\$ 112,269,367</u>

Other-Than-Temporary Impairment of Investments—The Foundation evaluates the near-term prospects for improvement of unrealized losses on available-for-sale investments in relation to the severity and duration of the loss for each category of assets by analyzing the earnings trends and economic conditions. Based on this evaluation, the Foundation recorded realized losses of \$464,909 on investments that were other-than-temporarily impaired at September 30, 2014. The Foundation recorded no other-than-temporary impairment of investments as of or during the year ended September 30, 2013. The total amount of unrealized losses remaining at September 30, 2014, was \$1,319,936 million, substantially all of which relates to investments that have been in a continuous unrealized loss position for less than 12 months.

Investment income and gains and losses for the years ended September 30, 2014 and 2013, consist of the following:

	2014	2013
Dividend and interest income	\$ 1,477,948	\$ 1,876,256
Realized gains on sales of securities—net	<u>2,723,079</u>	<u>3,448,993</u>
	<u>\$ 4,201,027</u>	<u>\$ 5,325,249</u>

3. TRANSACTIONS WITH THE HEALTH SYSTEM

The Health System performs certain administrative functions for the Foundation. Funds disbursed on behalf of the Foundation are reimbursed to the Health System. The total amount of expenses paid by the Health System and reimbursed by the Foundation for the years ended September 30, 2014 and 2013, were \$1,047,134 and \$937,567, respectively. As of September 30, 2014 and 2013, amounts due to the Health System related to these services totaled \$77,804 and \$80,755, respectively, reflected in accounts payable and accrued expenses within the statements of financial position.

The Foundation leases its office space from the Health System for a defined amount each year with an indefinite lease term. The lease expense is based on the square footage occupied, plus a prorated share of allocated costs, such as janitorial services, utilities, and facility management. The lease expense was \$34,843 and \$34,110 for the years ended September 30, 2014 and 2013, respectively.

The Foundation and the Health System are obligated parties under the Health System's Master Trust Indenture. As of September 30, 2014 and 2013, outstanding bonds under this Master Trust Indenture totaled \$461,410,000 and \$340,350,000, respectively.

Grant expense for the year ended September 30, 2013, includes funds granted to the Health System in the amount of \$42,020. There were no funds granted to the Health System for the year ended September 30, 2014. Grants payable as of September 30, 2014 and 2013, include grants due to the Health System in the amounts of \$164,640 and \$540,405, respectively.

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