# Supplemental Retirement Income Plan of North Carolina and North Carolina Public Employee Deferred Compensation Plan

(Fiduciary Funds of the State of North Carolina)

## Financial Report

December 31, 2016

## Supplemental Retirement Income Plan of North Carolina and North Carolina Public Employee Deferred Compensation Plan (together "Supplemental Retirement Plans of North Carolina")
**December 31, 2016**

**Page(s)**

CliftonLarsonAllen LLP
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## Independent Auditors' Report

Board of Trustees
Supplemental Retirement Plans of North Carolina
Raleigh, North Carolina

### Report on the Financial Statements

We have audited the accompanying financial statements of the Supplemental Retirement Income Plan of North Carolina (401(k) Plan) and the North Carolina Employee Deferred Compensation Plan (457(b) Plan), collectively referred to as the Supplemental Retirement Plans of North Carolina (the Plans), which comprise the statements of fiduciary net position as of December 31, 2016, and the related statements of changes in fiduciary net position for the year then ended, and the related notes to the financial statements, as listed in the table of contents.

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

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

#### *Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' 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 entity'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 entity'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 fiduciary net position of the Plans as of December 31, 2016, and the respective changes in their fiduciary net position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

#### *Other Matters*

*Required Supplementary Information*

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

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated July 27, 2017, on our consideration of the Plans' internal control over financial reporting and on our tests of their compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Plans' internal control over financial reporting and compliance.

CliftonLarsonAllen LLP

Baltimore, Maryland
July 27, 2017

The Supplemental Retirement Plans of North Carolina (the "Plans") include the Supplemental Retirement Income Plan of North Carolina (the "401(k) Plan") and the North Carolina Public Employee Deferred Compensation Plan (the "457(b) Plan"). This discussion and analysis of the Supplemental Retirement Plans of North Carolina's financial performance provides an overview of the Plans' financial activities for the year ended December 31, 2016. It is intended to be a narrative supplement to the Plans' financial statements.

### Using the Financial Report

This discussion and analysis is an introduction to the Plans' basic financial statements. This financial report for each Plan consists of two financial statements and the notes to the financial statements.

The Statements of Fiduciary Net Position report the Plans' assets, liabilities, and resultant fiduciary net position where Assets - Liabilities = Fiduciary Net Position. The assets are held in a trust for the benefit of participants at the end of the Plans' fiscal year. It can be thought of as a snapshot of the financial position of the Plans at that specific point in time.

The Statements of Changes in Fiduciary Net Position report the Plans' transactions that occurred during the fiscal year where Additions - Deductions = Net Change in Fiduciary Net Position. It is a record of the activity that occurred over the year, and explains the changes that have occurred to the prior year's fiduciary net positions on the Statements of Fiduciary Net Position.

The Plans' investments are divided among 13 options – nine equity funds, two fixed income funds, and an inflation responsive fund (referred to collectively herein as the "Pooled Account") and the NC Stable Value Fund. The assets in the Pooled Account are held in separate accounts, collective investment trusts, and a mutual fund.

The notes to the financial statements are an integral part of the financial statements and include additional information not readily evident in the statements themselves.

### Financial Highlights – 401(k) Plan

The following financial highlights occurred during the 401(k) Plan year ended December 31, 2016:

- The 401(k) Plan's fiduciary net position increased by approximately $645 million to approximately $8.8 billion during the 2016 plan year. Asset growth was primarily due to an increase in net investment income. Net investment income, which measures net appreciation in the fair market value of investments and interest earned on those investments, was approximately $572 million. In addition, contributions to the plan exceeded distributions to plan participants by approximately $68 million. Contributions to the plan were $516 million, an increase of approximately 6% from the prior year. Please see the Economic and Portfolio Discussion for additional information.

- The total number of participants in the plan declined approximately 5% to approximately 245,500 on December 31, 2016, from approximately 257,600 participants the year prior. The decline in the number of accounts was due in part to the "cash-out" of terminated employees with small account balances. Account holders were given the option to "roll" funds to another qualified plan or receive the funds as a taxable distribution.

**Condensed Statements of Fiduciary Net Position (401(k) Plan), as of December 31:**

| (in thousands of dollars) | 2016 | 2015 |
|---|---|---|
| Investments | | |
| Pooled account, at fair value | $ 6,477,345 | $ 5,947,914 |
| Stable value fund | 2,068,331 | 1,949,726 |
| Receivables | | |
| Notes receivable from participants | 286,942 | 292,561 |
| Other | 7,979 | 5,040 |
| Liabilities | (1,066) | (1,134) |
| Fiduciary net position | $ 8,839,531 | $ 8,194,107 |

The Pooled Account increased by approximately $529 million or approximately 9% reflecting positive returns in the financial markets for the year. The S&P 500 Index finished the year up 12%. International Equity markets were also up with the MSCI ACWI ex-US Index up 4.5% for the year. The Fixed Income market produced solid returns with the Bloomberg Barclays Aggregate Index returning 2.6% for the year. High Yield Bonds returned 17.1%, outperforming equities for the year. Commodities also performed well with the Bloomberg Commodity Index returning 11.8% for the year. The assets of the NC Stable Value Fund increased by approximately 6% for the year, due to participant activity and earnings generated from the underlying portfolios.

**Condensed Statements of Changes in Fiduciary Net Position (401(k) Plan), for the year ended December 31:**

| (in thousands of dollars) | 2016 | 2015 |
|---|---|---|
| **Additions** | | |
| Contributions | $ 516,454 | $ 489,177 |
| Net investment income | 572,014 | 3,095 |
| Interest on notes receivable from participants | 12,138 | 12,104 |
| Miscellaneous income | 2,019 | 1,848 |
| Total additions | 1,102,625 | 506,224 |
| **Deductions** | | |
| Distributions to participants and beneficiaries | 448,350 | 438,246 |
| Administrative expenses | 8,851 | 2,503 |
| Total deductions | 457,201 | 440,749 |
| Net increase in fiduciary net position | $ 645,424 | $ 65,475 |

Also of note are administrative expenses which increased to approximately $8.9 million from $2.5 million the year prior. This increase is primarily a result of the Supplemental Retirement Board of Trustees modifying the manner in which the participants' recordkeeping fee is assessed. Historically, this fee was assessed as an asset-based fee calculated as a percent of assets and therefore not reflected in the Statement of Changes in Fiduciary Net Position. The Board elected to modify the fee to a single, flat fee per account, assessed quarterly. At the plan level, this represented a significant fee savings. January 1, 2016, was the effective date of the new fee schedule.

We are not aware of any other currently known facts, decisions or conditions that are expected to have a significant impact on fiduciary net position or changes in fiduciary net position as of December 31, 2016.

### Financial Highlights – 457(b) Plan

The following financial highlights occurred during the 457(b) Plan year ended on December 31, 2016:

- The 457(b) Plan's fiduciary net position was approximately $1.2 billion on December 31, 2016, representing an increase of approximately $74 million during the 2016 plan year. This increase was primarily due to net investment income of approximately $76 million. Net investment income measures net appreciation in the fair value of investments and interest earned on those investments. Please see the Economic and Portfolio Discussion for additional information.

- There were approximately 52,600 and 55,600 participants in the 457(b) Plan at December 31, 2016, and 2015, respectively. The decline in the number of accounts was due in part to the "cash-out" of terminated employees with small account balances. Account holders were given the option to "roll" funds to another qualified plan or receive the funds as a taxable distribution.

### Condensed Statements of Fiduciary Net Position (457(b) Plan), as of December 31:

| (in thousands of dollars) | 2016 | 2015 |
|---|---|---|
| Investments | | |
| Pooled account, at fair value | $ 822,608 | $ 758,518 |
| Stable value fund | 405,748 | 395,999 |
| Receivables | | |
| Notes receivable from participants | 19,134 | 19,117 |
| Other | 940 | 481 |
| Liabilities | (209) | (228) |
| Fiduciary net position | $ 1,248,221 | $ 1,173,887 |

Fiduciary Net Position increased approximately 6% in 2016. This increase is due in large part to a significant increase in net investment income reflecting positive returns in the financial markets. The Pooled Account rose 8% while the NC Stable Value Fund increased 2%. The S&P 500 Index finished the year up 12%. International Equity markets were also up with the MSCI ACWI ex-US Index returning 4.5% for the year. The Fixed Income market produced solid returns with the Bloomberg Barclays Aggregate Index returning 2.6% for the year. High Yield Bonds returned 17.1%, outperforming equities for the year. Commodities also performed well with the Bloomberg Commodity Index returning 11.8% for the year.

**Condensed Statements of Changes in Fiduciary Net Position (457(b) Plan), for the year ended December 31:**

| (in thousands of dollars) | 2016 | 2015 |
|---|---|---|
| **Additions** | | |
| Contributions | $ 78,716 | $ 77,696 |
| Net investment income | 75,733 | 2,910 |
| Miscellaneous income | 391 | 260 |
| Interest on notes receivable from participants | 797 | 801 |
| Total additions | 155,637 | 81,667 |
| **Deductions** | | |
| Distributions to participants and beneficiaries | 79,623 | 73,283 |
| Administrative expenses | 1,680 | 404 |
| Total deductions | 81,303 | 73,687 |
| Net increase in fiduciary net position | $ 74,334 | $ 7,980 |

Net investment income was approximately $76 million, due in large part to positive performance in the financial markets. The Equity markets had a strong year with the S&P 500 Index returning 12% for the year. Other asset classes also had solid performance during the year, with the fixed income markets returning 2.6% and commodities returning 11.8% for the year.

Contributions to the 457(b) Plan remained somewhat consistent, increasing approximately $1 million or 1% in 2016, compared to 2015. Distributions to participants and beneficiaries increased by approximately $6.3 million, or approximately 9%. The increase in distributions was due in part to the "cash-out" of terminated employees with small balances.

Also of note are administrative expenses, which increased to approximately $17 million from $0.4 million the year prior. This increase is primarily a result of the Supplemental Retirement Board of Trustees modifying the manner in which the participants' recordkeeping fee is assessed. Historically, this fee was assessed as an asset-based fee calculated as a percent of assets and therefore not reflected in the Statement of Changes in Fiduciary Net Position. The Board elected to modify the fee to a single, flat fee per account, assessed quarterly. At the plan level, this represented a significant fee savings. January 1, 2016, was the effective date of the new fee schedule.

We are not aware of any other currently known facts, decisions or conditions that are expected to have a significant impact on fiduciary net position or changes in fiduciary net position as of December 31, 2016.

**Other Highlights**

On January 4, 2016, the North Carolina Supplemental Retirement Plans Group Trust was established to facilitate the "unbundling" of the Plans. To effect this change and following a competitive bid process, separate contractual agreements were established with the Plans' recordkeeper and custodian. Plan assets were transferred to the group trust, and the variable annuity, which had held Plan assets, was dissolved. The Plans' "unbundling" resulted in greater service provider role clarity, full transparency and ease of vendor management. As a result of these new agreements, member services were enhanced and plan level fees were reduced. A participant communication plan was implemented to inform all participants of this change.

In 2016 the Plans conducted a review of the assets transferred between custodians as part of the "unbundling" of the Plans. The results of this custodial bank transfer review confirmed that all assets had been accounted for following the transition between Plan custodians and no errors had been identified in the reconciliation process.

In 2016 the Plans issued a "Request for Proposals" ("RFP") for audit services. Through a competitive bid process CliftonLarsonAllen LLP was selected based upon their technical and cost proposals.

Plan expenses remain competitive when compared to a peer group of institutional mutual funds. At the end of 2016, the average total plan expenses were approximately 37 basis points. This compares favorably to the median expense ratio of the Mercer Institutional Mutual Fund Universe of 58 basis points.

**Asset Class and Economic Discussion**

Net Investment Income for the 457(b) and 401(k) Plans was $76 million and $572 million, respectively primarily due to strong performance in the financial markets during 2016.

Global growth in 2016 came in at a post-crisis low of 2.3%, with stagnant global trade, subdued investment and heightened policy uncertainty marking another difficult year for the world economy. Major developed-market economies struggled in an environment of increased uncertainty about politics, policy direction, tepid investment, and sluggish productivity growth.

*U.S. Equities*

Early in the year, U.S. equities fell sharply as investors looked for safety amid concerns of high Chinese debt, rising U.S. rates, and falling commodity prices. As policy makers allayed these concerns, the markets quickly reversed direction. However, the market was surprised and sold off heavily in late June when the U.K. voted by referendum to leave the European Union ("EU"). More defensively-oriented stocks soared while cyclicals were negatively impacted. Despite the vote, it became apparent that the EU and Great Britain would both survive and the markets rebounded quickly.

A rebound in corporate earnings, accelerating U.S. economic growth, and the stabilization of energy prices all contributed to renewed investor enthusiasm for equities later in the reporting period. The rally gained further momentum after the U.S. Presidential election as investors expected business friendly policies from the new administration, such as tax cuts, less regulation and fiscal stimulus. Domestic equities hit all-time highs following the U.S. election in November. The prospects for banking deregulation and higher interest rates caused financial stocks to rally. Energy stocks also rose on the potential of more drilling and less regulation. Industrial names also traded up in anticipation of future infrastructure spending measures and trade reforms.

The bulk of the U.S. stock market gains came in the second half of the year, with U.S. Equities finishing the year strong. For the year, the S&P 500 returned 12% with Energy and Telecomm Services showing the strongest returns at 25.9% and 23.8%, respectively. Health Care was the only sector in negative territory, down 2.9% for the year, as the industry garnered increased political scrutiny over pricing practices.

Small Cap stocks, up 21.3%, outperformed large cap stocks, which were up 12.1%. Mid Cap stocks finished the year up 13.8%. Small Cap Value stocks were the best performing sector, gaining 31.7% for the year. Value outperformed Growth across all market capitalizations during the year.

2016 proved to be a difficult year for active managers. The North Carolina Large Cap Growth Fund had the largest underperformance relative to the benchmark for the year as well as the lowest absolute performance of the equity funds, returning 0.4%, versus 7.1% for the benchmark. Growth managers trailed through the first half of 2016, when investors were paying a premium for higher yielding equities in a low interest rate environment. The North Carolina Large Cap Value Fund returned 16.8% for the year, trailing the benchmark return of 17.3%. The North Carolina Small / Mid Cap Value Fund, up 20.6% and the North Carolina Small / Mid Cap Growth Fund, up 8.6%, also underperformed their respective benchmarks for the year, by 4.6% and 1.1% respectively.

*Global Equities*

For the year, global small caps outperformed large caps by 3.7%. The North Carolina Global Equity Fund was up 6% for the year underperforming its benchmark, the MSCI All Country World Index ("ACWI") by 250 basis points (i.e., 2.5 percent).

*International Equities*
International stock markets fell sharply early in the year on concerns of weak oil prices, slowing economic growth in China and a strengthening U.S. dollar. Though markets improved post-Brexit, sub-par economic expansion and other political issues continued to suppress international developed market sentiment. In U.S. dollar terms, the MSCI Europe, Australia-Asia and Far East ("EAFE") was up 1.0% in 2016. In local currency terms, the index was up 5.3%.

The North Carolina International Equity Fund returned 5.5% for the year, outperforming its benchmark, the MSCI ACWI ex USA by 50 basis points.

*Emerging Market Equities*
Emerging market equities outperformed developed international equities for most of the year, due to a strong rebound in commodity prices and currency valuations. Emerging market equities saw declines in the fourth quarter of 2016 as dollar strength and the potential for a decline in global trade weighed on markets. Emerging markets declined 4.2% during the fourth quarter, but finished the year up 11.2%.

*Currencies*
Brighter domestic economic prospects and higher interest rates helped boost the U.S. Dollar. The Dollar strengthened significantly during the fourth quarter of 2016, particularly after the U.S. election. The Dollar Index (DXY) rose 7.1% during the fourth quarter and finished 2016 up 3.6%. For the year, the euro declined by 3.2% relative to the dollar. The yen appreciated by 2.9% against the dollar due to a strong first half of 2016. The British pound and Mexican peso experienced significant declines in 2016. The British pound weakened significantly in the immediate wake of the U.K.'s Brexit decision. The Mexican peso fell largely due to the newly elected U.S. President's views on foreign trade. The Brazilian real was the strongest performing currency for the year, as Brazil has benefitted from a more market friendly government and stability in the energy markets.

*Fixed Income*
Interest rates rose during the fourth quarter as the market began to price a more rapid pace in Fed rate increases. After holding off raising rates for most of the year, the Fed increased rates by 0.25 percentage points in December.

Expectations for higher rates hurt bond prices, with bonds experiencing their second consecutive year of declines. Treasury yields fell sharply in the first half of the year, but rebounded sharply in the second half of 2016. While the U.S. Treasury 10-year rate dipped to a historic low of 1.4% in July, it finished the year at 2.4%. In December, the European Central Bank held interest rates at current levels and extended their planned stimulus through the end of 2017, although at a reduced rate. The Bank of Japan also held interest rates flat in its December meeting.

The Bloomberg Barclays Aggregate Index ended the year up 2.6%. Long-duration bonds generally fared poorly given the pronounced interest rate increases at the longer end of the curve.

While rising interest rates impacted the prices on all bonds towards the second half of 2016, corporate bonds performed better than most other fixed income securities during the year as credit spreads tightened alongside an improving economy. U.S. Corporate Bonds were up 6.1% for the year, outperforming U.S. Treasuries by 510 basis points. For 2016, high yield bonds, returned 17.1%, outperforming global equities.

North Carolina's Fixed Income Fund, up 4% in 2016, outperformed the Bloomberg Barclays Aggregate Index by 140 basis points, due to the fund's exposure to spread sectors such as corporates and high yield bonds which outperformed during the year.

*Commodities & Real Assets*
The Bloomberg Commodity Index finished the year up 11.8%. U.S. REITs finished the year up 8.6%, while global REITs lagged, returning 5% for the year. The Bloomberg Barclays U.S. TIPS Index was up 4.7%. Oil saw its biggest annual gain since the financial crisis, propelled by a deal among OPEC nations and major oil producers to cut production. Oil prices rebounded from a low of $26 per barrel in February and subsequently increased to $53 by year-end.

The North Carolina Inflation Responsive Fund returned 10.5% in 2016, exhibiting strong performance during the year given the fund's exposure to commodities, REITs and TIPs.

*Economic Discussion*
The U.S. economy was sluggish in 2016 due to lower exports and a deceleration in private investment. During the year there was a further tightening of labor markets leading to slowly rising wage growth. Real GDP increased 1.6% in 2016, compared with an increase of 2.6% in 2015. Consumer Price Inflation ("CPI") came in at a modest 1.26% for the year. The year ended with the Federal Reserve ("Fed") increasing interest rates by 0.25% in December as economic growth was improving in the last half of the year. Growth within the Euro area also slowed from 2% in 2015 to 1.6% in 2016, as both domestic demand and exports lost momentum.

Growth in China slowed to 6.7% with growth concentrated primarily in the services sector and industrial production stabilizing at moderate levels. The rise in U.S. yields since early November led to tightening of financing conditions for emerging market and developing economies resulting in currency depreciation and portfolio outflows for several emerging markets. Despite this tightening, financing conditions still remain fairly benign, as central banks maintain accommodative monetary policies.

Note: All NC fund performance is net of fees

For detailed information regarding investment performance of the funds, please access the Plan website at www.ncplans.prudential.com.

### Requests for Information

This financial report is designed to provide a general overview of the finances of the Supplemental Retirement Plans of North Carolina. If you have any questions or concerns about this report or need additional financial information, contact Mary Buonfiglio, Deputy Director of Supplemental Retirement Plans, North Carolina Department of State Treasurer, 3200 Atlantic Avenue, Raleigh, NC 27604.

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# Supplemental Retirement Plans of North Carolina
## Statements of Fiduciary Net Position
## December 31, 2016

**(in thousands of dollars)**

| | 401(k) | 457(b) |
|---|---|---|
| **Assets** | | |
| Investments | | |
| Pooled Account, at fair value | $ 6,477,345 | $ 822,608 |
| North Carolina Stable Value Fund | | |
| Unallocated insurance contracts, at contract value | | |
| Synthetic Guaranteed Investment Contracts | 1,225,449 | 240,399 |
| Insurance Company Separate Accounts | 680,297 | 133,456 |
| Wells Fargo Stable Return Fund, at contract value | 145,323 | 28,507 |
| Wells Fargo Government Money Market Fund, at amortized cost | 17,262 | 3,386 |
| Total stable value fund | 2,068,331 | 405,748 |
| Total investments | 8,545,676 | 1,228,356 |
| Receivables | | |
| Contributions | | |
| Participants | 3,981 | 624 |
| Employers | 2,555 | 33 |
| Notes receivable from participants | 286,942 | 19,134 |
| Other | 1,443 | 283 |
| Total receivables | 294,921 | 20,074 |
| Total assets | 8,840,597 | 1,248,430 |
| **Liabilities** | | |
| Accounts payable | 1,066 | 209 |
| Total liabilities | 1,066 | 209 |
| **Fiduciary net position** | $ 8,839,531 | $ 1,248,221 |

The accompanying notes are an integral part of these financial statements.

# Supplemental Retirement Plans of North Carolina
## Statements of Changes in Fiduciary Net Position
## Year Ended December 31, 2016

**(in thousands of dollars)**

| | 401(k) | 457(b) |
|---|---|---|
| **Additions** | | |
| Investment income | | |
| Net appreciation in fair value of investments | $ 534,719 | $ 69,110 |
| Interest | 37,295 | 6,623 |
| Total net investment income | 572,014 | 75,733 |
| Other income | | |
| Interest on notes receivable from participants | 12,138 | 797 |
| Miscellaneous income | 2,019 | 391 |
| Total other income | 14,157 | 1,188 |
| Contributions | | |
| Plan participant contributions, including rollover contributions of $55,539 for the 401(k) Plan and $15,583 for the 457(b) Plan | 325,848 | 77,130 |
| Employer contributions | 190,606 | 1,586 |
| Total contributions | 516,454 | 78,716 |
| Total additions | 1,102,625 | 155,637 |
| **Deductions** | | |
| Distributions to participants and beneficiaries | 448,350 | 79,623 |
| Administrative expenses | 8,851 | 1,680 |
| Total deductions | 457,201 | 81,303 |
| Net increase in fiduciary net position | 645,424 | 74,334 |
| **Fiduciary net position** | | |
| Beginning of year | 8,194,107 | 1,173,887 |
| End of year | $ 8,839,531 | $ 1,248,221 |

The accompanying notes are an integral part of these financial statements.

## 1. Plan Description

The following description of the Supplemental Retirement Plans of North Carolina ("Plans") is provided for general informational purposes only. The Supplemental Retirement Plans of North Carolina (the "Plans") include the Supplemental Retirement Income Plan of North Carolina (the "401(k) Plan") and the North Carolina Public Employee Deferred Compensation Plan (the "457(b) Plan"). More complete information regarding the Plans' provisions may be found in the respective plan documents.

### General

The 401(k) Plan, established effective January 1, 1985, is a defined contribution multiple-employer governmental plan sponsored by the State of North Carolina ("Plan Sponsor"). As of December 31, 2016, the Plan is utilized by 1,036 governmental employers in North Carolina consisting principally of state agencies, counties, school systems, cities, and towns.

The 457(b) Plan, established effective January 1, 1974, is a defined contribution multiple-employer governmental plan sponsored by the State of North Carolina ("Plan Sponsor"). As of December 31, 2016, the 457(b) Plan is utilized by 435 governmental employers in North Carolina consisting principally of state agencies, counties, school systems, cities, and towns.

### Plan Administration

The Supplemental Retirement Board of Trustees ("Board") and the Retirement Systems Division of the Department of State Treasurer ("Department") have the responsibility for administering the 401(k) Plan and the 457(b) Plan according to the plan documents and North Carolina General Statutes, with the Department serving as the Primary Administrator ("Primary Administrator") carrying out the provisions of the Plans, as directed by the Board. The Board and the Department have entered into an agreement with Prudential Retirement Insurance and Annuity Company ("Contractor") to perform recordkeeping, administration and education services.

The Pooled Account offers nine equity funds, an inflation responsive fund, two fixed income funds, and a stable value fund. The actively managed separate account funds have multiple investment managers, and the passively managed separate accounts each have a single investment manager.

The Board has engaged Galliard Capital Management, Inc. ("Galliard") to provide professional management of the NC Stable Value Fund. Under Galliard management, the NC Stable Value Fund allocates funds to five insurance contracts with six underlying investment managers, as well as the commingled funds of another manager.

### Participation

Those employees eligible for the 401(k) Plan include participants of the following:

- State of North Carolina Teachers' and State Employees' Retirement System of North Carolina ("TSERS")
- Consolidated Judicial Retirement System
- Legislative Retirement System
- North Carolina Local Governmental Employees' Retirement System ("LGERS")
- Optional Retirement Program

Those employees eligible for the 457(b) Plan are employees of the state, any county or municipality, the North Carolina Community College System and any political subdivision of the state that have elected to participate in the 457(b) Plan.

The 401(k) Plan had approximately 245,500 participants at December 31, 2016.

The 457(b) Plan had approximately 52,600 participants at December 31, 2016.

**Contributions**
401(k) Plan participants may elect to contribute between 1% and 80%, in whole percentages, of their compensation, as defined by the 401(k) Plan, subject to certain limitations under the Internal Revenue Code ("IRC"). 457(b) Plan participants may elect to contribute between 1% and 100%, in whole percentages, of their compensation, as defined by the 457(b) Plan, subject to certain limitations under the IRC. The Plans limit the amount of an individual's annual contributions to the maximum allowed by the IRC ($18,000 for 2016). Federal and state income tax on amounts contributed by participants are deferred until benefits are paid to the participants. An employee may begin contributing to the 401(k) Plan on the first enrollment date, which is at least 60 days, or such shorter period as the governmental employer determines, after the date he or she files with the governmental employer a notice whereby the employee: 1) makes an election to contribute a percentage of his/her compensation or fixed dollar amount to the Plans and 2) authorizes the governmental employer to reduce his/her compensation by such percentage or amount. An employee may become a participant in the 457(b) Plan by entering into an enrollment agreement prior to the beginning of the calendar month in which the enrollment agreement is to become effective or such other date as may be permitted under the Code. Participating employers may make contributions to the Plans. Employer contributions to the 401(k) Plan and the 457(b) Plan were approximately $190.6 million and $1.6 million, respectively, in 2016.

Roth contributions are permissible within the 401(k) Plan and 457(b) Plan. Roth contributions are elective deferrals that the participant elects to include in gross income. Qualified distributions from a designated Roth account are excludable from gross income. Generally, a distribution qualifies for income exclusion when it occurs more than five years after the initial contribution to the account and when the participant is age 59½ or older, dies or becomes disabled.

In-plan Roth conversion provisions were added to the 401(k) Plan and 457(b) Plan effective December 1, 2010 and April 1, 2011, respectively. As of the effective date, the Plans will accept Roth contributions made on behalf of participants. All contribution sources and earnings thereon, except Roth contributions and Roth rollover contributions, will be eligible for in-plan Roth conversions in accordance with the standard in-service withdrawal and termination distribution provisions of the Plans. Participants and spousal beneficiaries will be allowed to elect voluntary federal and state income tax withholding on in-plan Roth Conversion amounts. Withholding will be deducted from eligible amounts in advance of the in-plan Roth conversion. In-plan Roth conversion amounts will remain invested among the same plan investment options in which they were invested prior to the conversion ("like to like").

The 401(k) Plan allows participants age 50 or older to make catch-up contributions in accordance with and subject to the limitations of Section 414(v) of the IRC ($6,000 for 2016). The 401(k) Plan allows participants to contribute amounts being rolled over from other eligible retirement plans, as defined in the 401(k) Plan document. Participating governmental employers may elect to make discretionary contributions to the 401(k) Plan as determined by the General Assembly or the participating governmental employer. With respect to participants who are law enforcement officers, the governmental employer of the law enforcement officers shall contribute to the 401(k) Plan on behalf of each such law enforcement officer an amount equal to such percentage, as determined by the North Carolina General Assembly, of compensation received during the plan year (5% in 2016). Law enforcement officers, excluding sheriffs, shall also receive from the Department of State Treasurer a contribution, allocated on a per capita basis, of an amount equal to a division, as determined by the North Carolina General Assembly, of receipts collected under North Carolina General Statute 7A-304 on account of assessed cost of court.

The 457(b) Plan allows participants age 50 or older to make catch-up contributions in accordance with and subject to the limitations of Section 414(v) of the IRC. The 457(b) Plan allows participants to contribute amounts being rolled over from other eligible retirement plans, as defined in the 457(b) Plan document. In addition, the 457(b) Plan allows participants within three years of reaching a normal retirement age to contribute up to twice the amount allowed by the IRC ($36,000 for 2016) subject to certain limitations. The age 50 or older catch-up contributions cannot be used in conjunction with the three-year catch-up contributions.

On June 28, 2012, the North Carolina General Assembly ratified House Bill 153. House Bill 153 prohibits state and local law enforcement officers from receiving employer contributions made to the 401(k) Plan on or after December 1, 2012, if the law enforcement officer is convicted of a felony related to employment on or after December 1, 2012.

**Vesting**
Participants are at all times 100% vested in their contributions, employer contributions and their allocated earnings thereon.

**Payment of Benefits**
On termination of employment due to retirement, disability or death, the participant, or sole beneficiary, may receive the amount to the credit of the participant's account upon election of a payment option. Upon such election, a participant or sole beneficiary may elect to receive payments from their account in monthly, quarterly, semiannual or annual installments over a period not to exceed the participant's, or sole beneficiary's, life expectancy. In addition, hardship distributions are permitted if certain criteria are met.

**Participant Accounts**
Individual accounts are maintained by the Contractor for each of the Plans' participants to reflect the participant's and employer's contributions, as well as the participant's share of the Plans' income and any related administrative expenses. Allocations of income and expenses are based on the proportion that each participant's account balance bears to the total of all participant account balances. The benefit to which a participant is entitled is the benefit that can be provided from the participant's vested account.

**Notes Receivable from Participants**
Participants may borrow, on notice to the Contractor and on approval by the primary administrator under such rules as it shall adopt, up to 100% of their account subject to certain limitations.

A participant with an account balance equal to or less than $20,000 may borrow the lesser of i) 100% of the participant's account balance or ii) $10,000. A participant with an account balance of more than $20,000 may borrow the lesser of i) $50,000 (reduced by the excess, if any, of the participant's highest outstanding balance of loans from the Plans during the one-year period ending on the day before the date on which such loan is made) or ii) one-half (1/2) of the participant's vested account balance. The minimum loan shall be $1,000.

A participant may have only one loan outstanding at any time and must wait 15 days to initiate a new loan after paying off an existing loan. The interest rate charged on loans shall be reasonable as determined by the Primary Administrator. During 2016, the interest rate charged was equal to the prime rate, as shown in the *Wall Street Journal,* 15 business days prior to the start of each calendar quarter, plus 1%. At December 31, 2016, the interest rates on outstanding loans ranged from 4.25% to 5.00% for the 401(k) Plan and 4.25% to 9.75% for the 457(b) Plan. The term of the loan shall be arrived at by mutual agreement between the participant and the primary administrator. At December 31, 2016, the loans outstanding had initial repayment terms between one and five years for the 401(k) Plan and between one and fifteen years for the 457(b) Plan.

Under the Loan Policy of the Plans, members are permitted to continue repaying loans after they separate from service. Members electing to continue loan repayments after separating from service are subject to a one-time $100 loan administration fee.

**Investment Elections**
Upon enrollment in the Plans, a participant may direct contributions to any investment option offered by the Plans. The participant has a broad range of options from which to choose, which allows the participants to diversify their investments. At December 31, 2016, the Plans offered 13 investment options across four categories - stable value, bonds/fixed income, inflation responsive, and stocks/equities. The participant exercises control over the assets in their individual account and is solely responsible for choosing the investment options for their account. Participants may change their investment elections daily provided they do not violate market timing policies. The Plans are not governed by any law or regulation restricting its deposits or investments other than that of following the prudent person rule and acting solely in the interests of participants.

**Transfer Benefit Option**
Members of TSERS and LGERS are allowed to convert their 401(k) Plan and 457(b) Plan balances into a monthly benefit. In 2013, the North Carolina General Assembly ratified House Bill 359. House Bill 359 allows members of TSERS and LGERS to transfer balances from other qualified plans into a monthly benefit from their TSERS and LGERS plans. Under such a transfer, the funds from the other qualified plans are first transferred into the 401(k) Plan or 457(b) Plan, and then transferred to TSERS or LGERS. When transferred into the Plans, these contributions are reflected in total contributions as the rollover contributions. Transfers to TSERS and LGERS are reflected as distributions on the Statement of Changes in Fiduciary Net Position.

## 2. Summary of Significant Accounting Policies

**Reporting Entity**
The Plans are reported by the State of North Carolina as fiduciary funds. The financial statements of the Plans are intended to present the fiduciary net position and the changes in fiduciary net position of only that portion of the total fiduciary funds that are attributable to the Plans. They do not purport to, and do not, present the financial position of the total fiduciary funds of the State of North Carolina as of December 31, 2016, and the changes in its financial position for the year then ended.

**Basis of Accounting**
The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, including all applicable effective statements of the Governmental Accounting Standards Board ("GASB"), and on the accrual basis of accounting.

**New Accounting Standards**
In 2016, the Plans implemented GASB Statement No. 72, *Fair Value Measurement and Application*, ("GASB 72"). This statement defines fair value and describes how state and local governments should define and measure fair value, what assets and liabilities should be measured at fair value, and what information about fair value should be disclosed in the notes to the financial statements. GASB 72 enhances transparency through new note disclosures as reflected in Note 6 Fair Value Measurement.

**Investments**
The Plans invest in various types of investment securities. Investment securities are exposed to various risks, such as interest rate, market and credit risks. The Plans invest in securities with contractual cash flows, such as asset-backed securities, collateralized mortgage obligations and commercial mortgage-backed securities. The value, liquidity and related income of these and other securities are sensitive to changes in economic conditions, including real estate values, delinquencies or defaults, or both.

Due to the level of risks associated with certain investment securities, it is at least possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported in the statements of fiduciary net position. Assets are reported at fair value, contract value or amortized cost, depending upon the investment type.

The Plans' investments are divided among 13 options – nine equity funds, two fixed income funds, and an inflation responsive fund (referred to collectively herein as the "Pooled Account") and the NC Stable Value Fund. The assets in the Pooled Account are held in separate accounts, collective investment trusts, and a mutual fund.

The Plans' investments in the Pooled Account are stated at fair value. The value of each Plan's account within the Group Trust is adjusted periodically to reflect each Plan's share of the value of the Group Trust. Units of common/commingled funds, including collective investment funds, are valued at the net asset value of shares held by the Plans. Investments in fixed income securities (U.S. treasuries and U.S. agency securities, asset-backed securities, collateralized mortgage obligations, domestic corporate bonds, foreign government bonds, foreign corporate bonds, state and local government bonds, and mortgage pass-throughs) are valued on the basis of valuations furnished by independent pricing services. These services determine valuations for normal institutional-size trading units of such securities using models or matrix pricing, which incorporates yield and/or price with respect to bonds that are considered comparable in characteristics such as rating, interest rate, maturity date and quotations from bond dealers to determine current value. If these valuations are deemed to be either not reliable or not readily available, the fair value will be determined in good faith by the custodian. Common stock is valued at the closing price reported on the active market on which the individual securities are traded.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date. Contributions to the group trust are credited to participant accounts as units. The value of a unit changes each day based on the current fair value of the investment portfolio. Earnings as well as market fluctuations, are reflected in unit values.

A valuation date occurs each day that the New York Stock Exchange ("NYSE") is open. The recordkeeper processes all participant transactions on the valuation date at the value of Pooled Account and Stable Value investments as of the close of the financial market's business day.

The Plans' investments in the NC Stable Value Fund are stated at contract value with the exception of the Government Money Market Fund, a fund of highly liquid assets used for liquidity and stated at amortized cost. Both contract value and amortized cost approximate fair value based on GASB standards. The NC Stable Value Fund's investments, excluding the Government Money Market Fund, consist of unallocated insurance contracts, which are nonparticipating investments. As such, GASB reporting standards provide they be reported at contract value. The NC Stable Value Fund ordinarily allows participants to withdraw their investment at contract value which represents their principal investment plus interest at a stated rate (known as the "crediting rate"), less withdrawals. As a result, participants are provided investment statements showing their activity in the NC Stable Value Fund at contract value rather than fair value. In addition to the contracts directly owned by the Plans, the Plans own units of participation in a Stable Return Fund that primarily invests in investment contracts, including traditional guaranteed investment contracts ("GICs") and security-backed contracts issued by insurance companies and other financial institutions.

The crediting rate of security-backed contracts will track current market yields on a trailing basis. The rate reset allows the contract value to converge with the fair value of the underlying portfolio over time, assuming the portfolio continues to earn the current yield for a period of time equal to the current portfolio duration. The net crediting rate reflects fees paid to security-backed contract issuers.

To the extent that the underlying portfolio of a security-backed contract has unrealized and/or realized losses, a positive adjustment is made to the adjustment from fair value to contract value under contract value accounting. As a result, the future crediting rate may be lower over time than the then-current market rates. Similarly, if the underlying portfolio generates unrealized and/or realized gains, a negative adjustment is made to the adjustment from fair value to contract value, and the future crediting rate may be higher than the then-current market rates.

**Contributions Receivable**

Participant contributions receivable represent amounts withheld from participants, but not remitted to the Contractor as of the Plans' year end. Employer contributions receivable represent the matching portion the employer owes the Plans on participant contributions receivable.

**Notes Receivable from Participants**

Notes receivable from participants are measured at their unpaid principal balance plus any accrued but unpaid interest. Delinquent notes receivable from participants are reclassified as distributions based upon the terms of the respective Plan documents.

**Payment of Distributions**

Distributions are recorded when paid.

**Administrative Expenses and Investment Management Fees**

All administrative costs of the Plans are deducted from participants' account balances. These costs include (a) benefit-responsive investment contract fees, which are included in the cost of investments and in determining net proceeds on sales of investments, and (b) operational expenses required for administration of the Plans including Primary Administrator expenses, trustee, and investment management fees which are charged against the various fund's assets on a pro rata basis throughout the year. An annual recordkeeping and communication fee of $31 is charged per account and is deducted from accounts quarterly on a pro rata basis. Loan initiation fees and trustee expenses are reported as administrative expenses. Loan initiation fees are deducted from the individual accounts under the Plan of the individual participants that are initiating loans. Custodian and investment management fees for commingled trusts are charged based on a percentage of net asset value and are paid from the assets of the respective funds. Certain other administrative expenses are paid by the Contractor.

**Use of Estimates in the Preparation of Financial Statements**

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, 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 additions and deductions during the reporting period. Actual results could differ from those estimates.

## 3. Investments

The following table presents a summary of investments at December 31, 2016:

**(in thousands of dollars)**

| | 401(k) Plan | 457(b) Plan | Total |
|---|---|---|---|
| **Pooled Account (Notes 4 and 6)** | $ 6,477,345 | $ 822,608 | $ 7,299,953 |
| **Stable Value Fund (Notes 5 and 6)** | | | |
| North Carolina Stable Value Fund | | | |
| Unallocated Insurance Contracts | | | |
| Prudential Synthetic Guaranteed Investment Contracts | 570,138 | 111,845 | 681,983 |
| Nationwide Life Insurance Company | 348,320 | 68,331 | 416,651 |
| American General Insurance Company | 306,991 | 60,223 | 367,214 |
| Great-West Deferred Stable Asset Fund Annuity | 415,613 | 81,532 | 497,145 |
| MetLife Insurance Company Separate Account | 264,684 | 51,924 | 316,608 |
| Wells Fargo Stable Return Fund | 145,323 | 28,507 | 173,830 |
| Wells Fargo Government Money Market Fund | 17,262 | 3,386 | 20,648 |
| Total stable value fund | 2,068,331 | 405,748 | 2,474,079 |
| Total investments | $ 8,545,676 | $ 1,228,356 | $ 9,774,032 |

## 4. Investments in Pooled Account

The Plans' investments are held in a group trust established as of January 4, 2016. The Board authorized the establishment of the North Carolina Supplemental Retirement Plans Group Trust (the "Group Trust") for the purpose of commingling the corpus of the separate trusts of the Plans; and the Board adopted the Declaration of Trust establishing the Group Trust. In addition, the Board agreed to act as trustee of the Group Trust, under the terms and conditions of the Declaration of Trust. The assets are managed by investment managers appointed by the Board and specified in investment agreements. The Plans are the beneficial owners of the assets in the Group Trust, which are accounted for in separate participating trust accounts for both Plans. The value of each Plan's account within the Group Trust is adjusted for the contributions and disbursements made with respect to each Plan; the investment gains and losses attributable to each Plan; and the costs allocated to each Plan. Each participating trust account is adjusted periodically to reflect each Plan's share of the fair market value of the Group Trust.

The following table presents the assets, including the investments and the percentage of each Plan's interest in each of the funds. Investment income and expense are presented in total for each fund in the Pooled Account:

| | |
|---|---|
| **NC Large CAP Index** | |
| *Blackrock Equity Index Non-Lendable Collective Investment Fund, at fair value | $ 1,383,382 |
| 401(k) plan interest in NC Large CAP Index | 1,229,256 |
| 401(k) plan interest percentage | 89% |
| 457(b) plan interest in NC Large CAP Index | 154,126 |
| 457(b) plan interest percentage | 11% |
| Investment income | |
| Net appreciation in fair value of investments - collective trust | 149,981 |
| **NC Large CAP Value** | |
| Domestic common stock, at fair value | 947,797 |
| Cash and cash equivalents | 161 |
| Accrued interest income | 1,293 |
| Due from broker for securities sold | 375 |
| Accounts payable - fees | (1,489) |
| Due to broker for securities purchased | (1,085) |
| Total net assets | 947,052 |
| 401(k) plan interest in NC Large Cap Value | 835,954 |
| 401(k) plan interest percentage | 88% |
| 457(b) plan interest in NC Large Cap Value | 111,098 |
| 457(b) plan interest percentage | 12% |
| Investment income and (expenses) | |
| Net appreciation in fair value of investments | 121,652 |
| Dividends and interest | 21,627 |
| Management and administrative fees | (3,651) |
| Net investment income | 139,628 |
| **NC Large CAP Growth** | |
| Domestic common stock, at fair value | 870,325 |
| Cash and cash equivalents | 89 |
| Accrued interest income | 387 |
| Due from broker for securities sold | 168 |
| Accounts payable - fees | (1,750) |
| Due to broker for securities purchased | (787) |
| Total net assets | 868,432 |
| 401(k) plan interest in NC Large Cap Growth | 758,913 |
| 401(k) plan interest percentage | 87% |
| 457(b) plan interest in NC Large Cap Growth | 109,519 |
| 457(b) plan interest percentage | 13% |
| Investment income and (expenses) | |
| Net appreciation in fair value of investments - domestic stock | 120 |
| Dividends and interest | 7,600 |
| Management and administrative fees | (4,009) |
| Net investment income | 3,711 |

| | |
|---|---|
| **NC Fixed Income** | |
| PIM (Prudential Investment Mgt) Core Plus Bond Fund - collective trust | 331,119 |
| Separate Account - JP Morgan Core Bond Fund | 327,971 |
| Total investments, at fair value | 659,090 |
| Cash and cash equivalents | 293 |
| Accrued interest income | 1,452 |
| Due from broker for securities sold | 49 |
| Accounts payable - fees | (324) |
| Total net assets | 660,560 |
| 401(k) plan interest in NC Fixed Income | 580,024 |
| 401(k) plan interest percentage | 88% |
| 457(b) plan interest in NC Fixed Income | 80,535 |
| 457(b) plan interest percentage | 12% |
| Investment income and (expenses) | |
| Net depreciation in fair value of investments - JP Morgan Core Bond Fund | (3,026) |
| Net appreciation in fair value of investments - PIM Core Plus Bond Fund | 17,436 |
| Interest | 9,887 |
| Management and administrative fees | (810) |
| Net investment income | 23,487 |
| | |
| **NC International** | |
| Domestic common stock and other investments, at fair value | 66,641 |
| Foreign stock | 517,781 |
| Total investments, at fair value | 584,422 |
| Cash and cash equivalents | 448 |
| Accrued income | 2,282 |
| Due from broker for securities sold | 8 |
| Payable for foreign exhange contract | (136) |
| Accounts payable - fees | (853) |
| Total net assets | 586,171 |
| 401(k) plan interest in NC International | 522,454 |
| 401(k) plan interest percentage | 89% |
| 457(b) plan interest in NC International | 63,717 |
| 457(b) plan interest percentage | 11% |
| Investment income and (expenses) | |
| Net appreciation in fair value of investments - domestic stock | 33,397 |
| Net depreciation in fair value of investments - foreign stock | (17,194) |
| Dividends and interest | 17,426 |
| Management and administrative fees | (3,286) |
| Net investment income | 30,343 |

| | |
|---|---|
| **NC Small MID CAP Index** | |
| Blackrock Russell 2500 Collective Investment Fund, at fair value | 248,509 |
| 401(k) plan interest in NC Small MID CAP Index | 226,065 |
| 401(k) plan interest percentage | 91% |
| 457(b) plan interest in NC Small MID CAP Index | 22,444 |
| 457(b) plan interest percentage | 9% |
| Investment income | |
| Net appreciation in fair value of investments - collective trust | 37,217 |
| | |
| **NC Small MID CAP Value** | |
| Domestic common stock, at fair value | 494,081 |
| Cash and cash equivalents | 263 |
| Accrued interest and dividend income | 697 |
| Accounts payable - fees | (1,086) |
| Due to broker for securities purchased | (64) |
| Total net assets | 493,891 |
| 401(k) plan interest in NC Small MID CAP Value | 413,569 |
| 401(k) plan interest percentage | 84% |
| 457(b) plan interest in NC Small MID CAP Value | 80,322 |
| 457(b) plan interest percentage | 16% |
| Investment income and (expenses) | |
| Net appreciation in fair value of investments | 84,898 |
| Dividends and interest | 7,947 |
| Management and administrative fees | (2,977) |
| Net investment income | 89,868 |
| | |
| **NC Global Equity** | |
| Domestic common stock and other investments, at fair value | 562,251 |
| Foreign stock | 291,888 |
| Total investments, at fair value | 854,139 |
| Cash and cash equivalents | 691 |
| Receivable for foreign exchange contracts | 1,067 |
| Accrued interest and dividend income | 1,817 |
| Due from broker for securities sold | 2,359 |
| Accounts payable - fees | (2,603) |
| Payable for foreign exchange contracts | (1,023) |
| Due to broker for securities purchased | (6,120) |
| Total net assets | 850,327 |
| 401(k) plan interest in NC Global Equity | 791,437 |
| 401(k) plan interest percentage | 93% |
| 457(b) plan interest in NC Global Equity | 58,890 |
| 457(b) plan interest percentage | 7% |
| Investment income and (expenses) | |
| Net appreciation in fair value of investments - domestic stock | 44,561 |
| Net depreciation in fair value of investments - foreign stock | (8,718) |
| Dividends and interest | 17,756 |
| Management and administrative fees | (4,922) |
| Net investment income | 48,677 |

| | |
|---|---|
| **NC U.S. Debt Index** | |
| *Blackrock U.S. Debt Index Non-Lendable Collective Investment Fund, at fair value | 439,483 |
| 401(k) plan interest in NC U.S. Debt Index | 393,623 |
| 401(k) plan interest percentage | 90% |
| 457(b) plan interest in NC U.S. Debt Index | 45,860 |
| 457(b) plan interest percentage | 10% |
| Investment income | |
| Net appreciation in fair value of investments - collective trust | 9,266 |
| **NC International Index** | |
| Blackrock MSCI ACWI ex-U.S. Index Non-Lendable Collective Investment Fund, at fair value | 46,632 |
| 401(k) plan interest in NC International Index | 35,638 |
| 401(k) plan interest percentage | 76% |
| 457(b) plan interest in NC International Index | 10,994 |
| 457(b) plan interest percentage | 24% |
| Investment income | |
| Net appreciation in fair value of investments - collective trust | 2,258 |
| **NC Inflation Responsive** | |
| * PIMCO Inflation Response Multi Asset Fund - mutual fund, at fair value | 403,212 |
| 401(k) plan interest in NC Inflation Responsive | 372,737 |
| 401(k) plan interest percentage | 92% |
| 457(b) plan interest in NC Inflation Responsive | 30,476 |
| 457(b) plan interest percentage | 8% |
| Investment income and (expenses) | |
| Net appreciation in fair value of investments | 34,195 |
| Dividends and interest | 1,989 |
| Management and administrative fees | (111) |
| Net investment income | 36,073 |

**NC Small MID CAP Growth**

| | |
|---|---|
| Domestic common stock, at fair value | 372,803 |
| Cash and cash equivalents | 246 |
| Accrued interest income | 431 |
| Due from broker for securities sold | 558 |
| Accounts payable - fees | (687) |
| Due to broker for securities purchased | (1,048) |
| Total net assets | 372,303 |
| 401(k) plan interest in NC Small CAP Growth | 317,676 |
| 401(k) plan interest percentage | 85% |
| 457(b) plan interest in NC Small CAP Growth | 54,627 |
| 457(b) plan interest percentage | 15% |
| Investment income and (expenses) | |
| Net appreciation in fair value of investments | 30,871 |
| Dividends and interest | 2,487 |
| Management and administrative fees | (2,463) |
| Net investment income | 30,895 |

| | |
|---|---|
| Total Pooled Account Asset | 7,299,953 |
| Total 401(k) plan interest in Pooled Account | 6,477,345 |
| Total 401(k) plan interest percentage in Pooled Account | 89% |
| Total 457(b) plan interest in Pooled Account | 822,608 |
| Total 457(b) plan interest percentage in Pooled Account | 11% |

* Represents individual investment greater than or equal to 5% of the fair value of the Plans' investments

### Interest Rate Risk

The Plans have a formal investment policy that limits duration as a means of managing its exposure to fair value losses arising from increasing interest rates. The managers within the NC Fixed Income Fund have duration targets relative to a specified benchmark. The maturities of the fixed income securities held in the NC Fixed Income Fund and collective investment funds in certain equity accounts, which are subject to interest rate risk, as of December 31, 2016, are as follows:

**(in thousands of dollars)**

| | Investment Maturities (in Years) at Fair Market Value | | | | |
|---|---|---|---|---|---|
| **Investment Type** | **Fair Value** | **Less than 1** | **1 to 5** | **6 to 10** | **More than 10** |
| Collateralized mortgage obligations | $ 67,447 | $ 6,653 | $ 5,484 | $ 17,118 | $ 38,192 |
| U.S. treasury strips | 60,023 | 1,664 | 24,263 | 11,941 | 22,155 |
| Mortgage pass throughs | 54,083 | 2,953 | 6,511 | 15,250 | 29,369 |
| Domestic corporate bonds | 56,083 | 2,781 | 18,491 | 24,232 | 10,579 |
| Asset-backed securities | 16,101 | 647 | 10,082 | 1,985 | 3,387 |
| Foreign corporate bonds | 13,169 | 423 | 5,485 | 5,540 | 1,721 |
| U.S. treasury securities | 24,933 | 2,521 | 9,881 | 4,372 | 8,159 |
| U.S. agencies securities | 6,465 | 2,674 | 2,595 | - | 1,196 |
| Foreign government bonds | 979 | - | 51 | 791 | 137 |
| State and local government bonds | 700 | - | - | - | 700 |
| **Common/commingled fund** | - | - | - | - | - |
| Fixed income core plus bond fund | 331,119 | - | - | 331,119 | - |
| Collective investment funds | 128,921 | 128,921 | - | - | - |
| Total | $ 760,023 | $ 149,237 | $ 82,843 | $ 412,348 | $ 115,595 |

Investments may also include various collateralized mortgage obligations, asset-backed securities, and commingled funds considered to be sensitive to changes in interest rates due to the existence of prepayment or conversion features.

*Collateralized Mortgage Obligation Securities*

Collateralized Mortgage Obligations (“CMOs”) generate a return based upon either the payment of interest or principal on mortgages in an underlying pool. The relationship between interest rates and prepayments makes the fair value sensitive to changes in interest rates. In falling interest rate environments, the underlying mortgages are subject to a higher propensity of prepayments. In a rising interest rate environment, the opposite is true.

*Asset-Backed Securities*

Asset-backed securities are securities that are primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other assets designed to assure the servicing or timely distribution of proceeds to the security holders.

*Commingled Funds*

The Plans own units in a commingled fixed income core plus bond fund, in a commingled inflation responsive multi-asset mutual fund, and in a short term collective investment trust. The weighted average maturity of the PIM Core Plus Bond Fund, which is a common/commingled fund and included in the NC Fixed Income Fund in the Pooled Account of the Plan, is approximately 8 years. As a result, the fund is sensitive to changes in interest rates. The weighted average maturity of the PIMCO Inflation Response Multi-Asset Fund, which is a common/commingled mutual fund and included in the NC Inflation Response Fund in the Pooled Account of the Plan, is approximately 6 years. As a result, the fund is sensitive to changes in interest rates.

**Credit Risk**

Credit risk is the risk an issuer or other counterparty to an investment will not fulfill its obligations, such as the chance that a bond issuer will fail to pay interest or principal in a timely manner, or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline. These circumstances may arise due to a variety of factors such as financial weakness, bankruptcy, litigation and/or adverse political developments. Certain fixed income securities, including obligations of the U.S. government or those explicitly guaranteed by the U. S. government, are not considered to have credit risk.

A bond's credit quality is an assessment of the issuer's ability to pay interest on the bond, and ultimately to repay the principal. Credit quality is evaluated by one of the independent bond-rating agencies - for example, Moody's Investors Service ("Moody's"), Standard and Poor's ("S&P"), or Fitch Ratings ("Fitch"). The lower the rating, the greater the chance, in the rating agency's opinion, that the bond issuer will default or fail to meet its payment obligations. Generally, the lower a bond's credit rating, the higher its yield should be to compensate for the additional risk. The investment policy statement applicable to the NC Fixed Income Fund places restrictions on the total risk exposure of the Fund and specifically the concentration of the debt securities in which the fund invests.

The following table presents the rating of debt securities held in the NC Fixed Income Fund and collective investment funds in certain equity accounts, as of December 31, 2016:

**(in thousands of dollars)**

| Investment Type | Fair Value | Aaa / AAA | Aa / AA | A / A- / A+ | Baa/BBB | Less than investment grade | Unrated | Exempt from credit quality (1) |
|---|---|---|---|---|---|---|---|---|
| Collateralized mortgage obligations | $ 67,447 | $ 4,907 | $ 55,884 | $ 1,204 | $ 3,241 | $ 1,483 | $ 728 | $ - |
| U.S. treasury strips | 60,023 | - | - | - | - | - | - | 60,023 |
| Mortgage pass throughs | 54,083 | - | 50,507 | - | - | - | - | 3,576 |
| Domestic corporate bonds | 56,083 | 890 | 4,071 | 18,055 | 30,680 | 2,387 | - | - |
| Asset-backed securities | 16,101 | 11,056 | 2,174 | 652 | 260 | 34 | 1,925 | - |
| Foreign corporate bonds | 13,169 | 721 | 1,176 | 7,003 | 3,964 | 305 | - | - |
| U.S. treasury securities | 24,933 | - | - | - | - | - | - | 24,933 |
| U.S. agencies securities | 6,465 | - | 6,465 | - | - | - | - | - |
| Foreign government bonds | 979 | - | - | - | 979 | - | - | - |
| State and local government bonds | 700 | - | 392 | 153 | 155 | - | - | - |
| **Common/commingled fund** | - | - | - | - | - | - | - | - |
| Fixed income core plus bond fund | 331,119 | - | - | - | - | - | 331,119 | - |
| Collective investment funds | 128,921 | - | - | - | - | - | 128,921 | - |
| Total | $ 760,023 | $ 17,574 | $ 120,669 | $ 27,067 | $ 39,279 | $ 4,209 | $ 462,693 | $ 88,532 |

(1) Obligations of the United States Government or obligations explicitly guaranteed by the United States Government are not considered to have credit risk and do not require disclosure of credit quality.

*Commingled Funds*
The Fixed Income Core Plus Bond Fund, which is a common/commingled fund and included in the NC Fixed Income Fund of the Pooled Account, has more than 75% of its debt securities rated BBB or better including 30% of which are rated AAA at December 31, 2016.

All assets of the NC Inflation Responsive Fund are invested in the PIMCO Inflation Response Multi-Asset Fund, a mutual fund. The PIMCO Inflation Response Multi-Asset Fund is more than 40% invested in US Treasury securities, which are exempt from rating. The other remaining investments are unrated.

**Custodial Credit Risk**
Custodial credit risk is the risk that, in the event of the failure of a counterparty financial institution, the Plan will not be able to recover the value of its investments and other assets that are in possession of an outside third party. The Plan does not have a formal policy to limit custodial credit risk.

**Concentration of Credit Risk**
Concentration of credit risk is the risk of loss attributed to the magnitude of a Plan’s investment in a single issuer. Money market funds and external investment pools are excluded from this disclosure requirement. Obligations explicitly guaranteed by the U.S. Government are not considered to have credit risk. Included in the Pooled Account are investments in individual collective trust funds under the various index funds and fixed-income options. Such funds that equal 5% or more of the fair value of the Plan's investments are identified with an asterisk in the presentation of the Pooled Account table within this footnote. The investment policy applicable to the NC Funds places restrictions on the concentration of the securities in which the funds invest.

**Foreign Currency Risk**
Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. There is no formally adopted investment policy to limit foreign currency exposure.

Within the NC International Fund and NC Global Equity Fund, the foreign investments expose the Plans to foreign currency risk. The following table presents in U.S. dollars the Pooled Account exposure to foreign currency as of December 31, 2016:

| **Currency (in thousands of dollars)** | |
|---|---|
| Euro | $ 234,387 |
| Pound Sterling | 131,879 |
| Japanese Yen | 131,337 |
| Swiss Franc | 68,511 |
| Hong Kong Dollar | 38,191 |
| South Korean Won | 30,300 |
| Swedish Krona | 28,940 |
| New Taiwan Dollar | 26,366 |
| Australian Dollar | 18,386 |
| Singapore Dollar | 16,613 |
| Canadian Dollar | 16,578 |
| South African Rand | 13,736 |
| Danish Krone | 11,739 |
| Indian Rupee | 11,608 |
| Brazil Real | 10,692 |
| Malaysian Ringgit | 4,830 |
| Thai Baht | 4,541 |
| UAE Dirham | 3,487 |
| Mexican Pesos | 3,467 |
| Indonesian Rupiah | 2,400 |
| Qatari Riyal | 1,576 |
| Turkish Lira | 1,564 |
| New Zealand Dollar | 1,486 |
| Philippines Peso | 143 |
| Norwegian Krone | 64 |
| Polish Zloty | 4 |
| | $ 812,825 |

## 5. Stable Value Fund

The NC Stable Value Fund consists of three synthetic guaranteed investment contracts, two separate account guaranteed investment contracts, a pooled stable value fund and a government money market fund. Galliard provides the professional management and oversight of the NC Stable Value Fund.

With a synthetic guaranteed investment contract, the Plan owns the underlying assets and negotiates a wrap contract for insurance protection. Because the synthetic GICs are fully benefit-responsive and nonparticipating investments, contract value, which approximates fair value, is the relevant measurement attribute for that portion of the net position attributable to the synthetic guaranteed investment contracts. Contract value represents contributions made under the contract, plus earnings, less participant withdrawals and administrative expenses. Participants may ordinarily direct the withdrawal or transfer of all or a portion of their investment at contract value. The interest crediting rate is reset, at a minimum, on a quarterly basis to reflect the performance of the underlying portfolio wrapped by the contract. The compound crediting rate methodology uses a formula to smooth out the gains or losses on the fixed income investments that back the wrap contract. The formula components are the current contract value, the fair value of the underlying portfolio, the annualized weighted average yield to maturity of the underlying portfolio and the weighted average duration of the underlying portfolio. The change in these factors from quarter to quarter impacts future crediting rate. The crediting rates of the contract may not fall below zero.

With a contract that is fully benefit-responsive and comprised of a separate account GIC, the contract value is the relevant measurement attribute for that portion of the net position attributable to the separate account GIC. Contract value represents contributions made under the contract, plus earnings, less participant withdrawals and administrative expenses. Participants may ordinarily direct the withdrawal or transfer of all or a portion of their investment at contract value. The interest crediting rate is reset, at a minimum, on a quarterly basis to reflect the performance of the underlying portfolio wrapped by the contract. The compound crediting rate methodology uses a formula to smooth out the gains or losses on the fixed-income investments that back the wrap contract. The formula components are the current contract value, the fair value of the underlying portfolio, the annualized weighted average yield to maturity of the underlying portfolio and the weighted average duration of the underlying portfolio. The change in these factors from quarter to quarter impacts the future crediting rate. The crediting rate may not fall below zero.

The five wrap contract issuers are Prudential, Nationwide Life, American General, Great West Life, and MetLife. Wrap contracts maintain a book value asset or fund balance for the underlying asset and report the yield credited on that book balance. The contracts are issued by insurance companies which guarantee the return of principal and a stated rate of interest. The contracts do not provide protection from all defaulting events of the underlying fixed income investments which could result in a negative return on the fund.

The contracts are described as follows:

***Prudential Synthetic GIC -*** The Plans have a fully benefit-responsive synthetic GIC with Prudential. The contract covers a commingled fixed-income collective investment fund managed by Jennison, and a fixed income portfolio managed by Prudential. The Plans own units of the underlying collective investment fund in addition to the securities within the fixed income bond portfolio. At December 31, 2016, the Prudential wrapper contract covering the fixed income investments had no fair value. Wells Fargo Bank is the custodian for the underlying investments and the trustee for the collective investment fund.

***Nationwide Life Synthetic GIC -*** The Plans have a fully benefit-responsive synthetic GIC with Nationwide Life. The contract covers a fixed income collective investment fund managed by Galliard. The Plans own units of the underlying collective investment fund. At December 31, 2016, there was no fair value to the wrap contract. Wells Fargo Bank is the trustee and custodian for the underlying investments.

***American General Synthetic GIC -*** The Plans have a fully benefit-responsive synthetic GIC with American General. The contract covers a fixed income separate account managed by Payden & Rygel. All of the underlying investments are owned by the Plans. At December 31, 2016, there was no fair value to the wrap contract. Wells Fargo Bank is the custodian for the underlying investments.

***Great-West Deferred Stable Asset Fund Annuity Contract -*** The contract is fully benefit-responsive and comprised of a separate account GIC issued by a life insurance company (issuer). The separate account GIC is backed by assets invested in an insurance separate account, a portfolio owned by the life insurance company but invested outside the insurance company's general investment account and managed by Great-West. The assets of the separate account are held exclusively for the benefit of the Plans and stated in the financial statements at contract value, which was $497 million at December 31, 2016. The fair value of the assets in the separate account was reported by Great-West to be $494 million. At December 31, 2016, there was no fair value to the wrap contract. The Bank of New York Mellon is the custodian for the underlying investments.

***MetLife Insurance Company Separate Account -*** The contract is fully benefit-responsive and comprised of a separate account GIC issued by a life insurance company. The separate account GIC is backed by assets invested in an insurance separate account, a portfolio owned by the life insurance company but invested outside the insurance company's general investment account and managed by Dodge & Cox. The assets of the separate account are held for the benefit of the Plans and certain other plans and stated in the financial statements at contract value, which was $317 million at December 31, 2016. The fair value of the Plan's portion of the assets in the separate account was reported by MetLife to be $319 million. State Street Bank is the custodian for the underlying investments. At December 31, 2016, there was no fair value to the wrap contract.

***Wells Fargo Stable Return Fund -*** A pooled stable value fund is a collective trust fund that holds unallocated, non-participating and benefit-responsive investment contracts issued by financial companies including GICs, Insurance Separate Account GICs, and Security Backed Investment Contracts. GICs are guaranteed insurance contracts backed by the general account of the insurance company while Insurance Separate Account GICs are backed by a segregated pool of assets owned by the issuer. Security Backed Investment Contracts are comprised of two components: investment contracts issued by a financial institution and underlying portfolios of fixed income securities (i.e. bonds) whose market prices fluctuate. The investment contracts held in the collective trust fund are designed to allow participants to transact at contract value without reference to the price fluctuations of the underlying fixed income securities. The NC Stable Value Fund holds units of the Wells Fargo Stable Return Fund. Terms of the underlying fund incorporate terms of the crediting rates and valuation at contract value. The Plans' investments in this fund are included in the disclosures of risk. At December 31, 2016, the fair value of the assets in the Stable Return Fund was $174 million.

***Wells Fargo Government Money Market Fund*** - This segment of the portfolio is invested in a money market fund managed by Wells Fargo, where the underlying securities are held at amortized cost (net asset value). The amortized cost accounting used in the fund very closely approximates the fair market value of the investments. The Plans' investments in this fund are included in the disclosures of risk. At December 31, 2016, the fair value of the assets in the Wells Fargo Government Money Market Fund was $21 million.

**Crediting Interest Rate for Fully Benefit-Responsive Contracts**

The crediting interest rate is based on a formula agreed upon with the issuer. Such interest rates are reviewed on a quarterly basis for resetting.

| **Average Yields at December 31, 2016** | **Earnings** | **Crediting Rate** |
|---|---|---|
| Prudential Synthetic GIC - Fixed Income Separate Account | 2.66% | 2.80% |
| Prudential Synthetic GIC - Fund N | 2.01% | 2.80% |
| Nationwide Life Synthetic GIC - Fund F | 1.75% | 1.70% |
| American General Synthetic GIC - Payden and Rygel | 1.48% | 1.28% |
| Great-West Group Deferred Stable Asset Fund Annuity | 2.46% | 2.14% |
| MetLife Insurance Company Separate Account | 2.51% | 2.52% |
| Wells Fargo Stable Return Fund | 1.94% | 1.94% |

### Fair Value of Fully Benefit-Responsive Contracts

The market values for which the Plans do not directly own the underlying assets are previously disclosed in the Great-West Deferred Stable Asset Fund Annuity Contract and MetLife Insurance Company Separate Account sections of this note. The market values of the fully benefit-responsive contracts for which the Plans own the underlying assets at December 31, 2016 are as follows:

**(in thousands of dollars)**

| | 401(k) Plan Total Contract Value | 401(k) Plan Underlying Investments Market Value | 457(b) Plan Total Contract Value | 457(b) Plan Underlying Investments Market Value |
|---|---|---|---|---|
| Prudential Synthetic GIC - Fixed Income Separate Account | $ 287,586 | $ 292,806 | $ 56,416 | $ 57,441 |
| Prudential Synthetic GIC - Fund N | 282,552 | 287,680 | 55,429 | 56,435 |
| Total Prudential | 570,138 | 580,486 | 111,845 | 113,876 |
| Nationwide Life Synthetic GIC - Galliard | 348,320 | 348,336 | 68,331 | 68,334 |
| American General Synthetic GIC - Payden and Rygel | 306,991 | 306,770 | 60,223 | 60,180 |
| Wells Fargo Stable Return Fund | 145,323 | 145,613 | 28,507 | 28,565 |
| Total Synthetic GIC Components | $1,370,772 | $ 1,381,205 | $ 268,906 | $ 270,955 |

### Interest Rate Risk

The fixed income securities underlying the synthetic GICs owned by the Plans are subject to interest rate risk. The fund's underlying investment manager guidelines and duration guidelines seek to manage the overall fund's exposure to interest rate risk. The maturities of the securities underlying the GICs owned by the Plans as of December 31, 2016 are as follows:

**(in thousands of dollars)**

| | | Investment Maturities (in Years) at Fair Market Value | | | |
|---|---|---|---|---|---|
| **Investment Type** | **Fair Value** | **Less Than 1** | **1 to 5** | **6 to 10** | **More Than 10** |
| Domestic corporate bonds | $ 191,059 | $ 31,335 | $ 100,441 | $ 57,388 | $ 1,895 |
| U.S. treasury securities | 209,498 | 49,349 | 149,893 | 5,670 | 4,586 |
| Foreign corporate bond | 73,878 | 10,523 | 57,556 | 5,444 | 355 |
| Asset-backed securities | 56,930 | - | 43,629 | 10,229 | 3,072 |
| Foreign government bonds | 9,713 | 802 | 8,057 | 854 | - |
| Mortgage pass throughs | 111,301 | 16,059 | 163 | 1,905 | 93,174 |
| U.S. agencies securities | 23,075 | 210 | 21,311 | 1,435 | 119 |
| State and local government | 7,935 | 4,108 | 3,651 | 176 | - |
| Collateralized mortgage obligations | 1,562 | - | 1,550 | - | 12 |
| Commerical mortgage backed securities | 42,198 | - | - | 17,262 | 24,936 |
| Common/commingled fund: | | | | | |
| Intermediate collective trust fund N | 344,115 | - | - | 344,115 | - |
| Short-core fixed income collective trust fund | 416,670 | - | 416,670 | - | - |
| Stable return collective trust fund | 174,178 | - | 174,178 | - | - |
| Government money market collective trust fund | 20,648 | 20,648 | - | - | - |
| Total | $ 1,682,760 | $ 133,034 | $ 977,099 | $ 444,478 | $ 128,149 |

Assets for which the Plans do not directly own the underlying securities are excluded from this chart.

Investments may also include various collateralized mortgage obligations and asset backed securities that considered to be sensitive to changes in interest rates due to the existence of prepayment or conversion features.

*Asset-Backed Securities*
Asset-backed securities are securities that are primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other assets designed to assure the servicing or timely distribution of proceeds to the security holders.

*Collateralized Mortgage Obligation Securities*
CMOs generate a return based upon either the payment of interest or principal on mortgages in an underlying pool. The relationship between interest rates and prepayments makes the fair value sensitive to changes in interest rates. In falling interest rate environments, the underlying mortgages are subject to a higher propensity of prepayments. In a rising interest rate environment, the opposite is true.

*Commingled Funds*
The NC Stable Value Fund owns units in various commingled funds, each with an investment objective relative to maturity and liquidity. This includes units in the Wells Fargo Advantage Government Money Market Fund, the Wells Fargo Stable Return Fund, the intermediate collective trust fund for one of the Prudential Synthetic GICs and the short core high quality fixed income collective trust fund for the Nationwide Life Synthetic GIC. The interest rate risk in each of the funds is dependent upon the weighted average maturity of each of the funds. The weighted average maturities of the Intermediate trust fund N and the Short-core fixed income collective trust fund are approximately 6.7 and 2.3 years, respectively. As a result, the funds are sensitive to changes in interest rates.

**Credit Risk**
Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations, such as the chance that a bond issuer will fail to pay interest or principal in a timely manner, or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline. These circumstances may arise due to a variety of factors such as financial weakness, bankruptcy, litigation and/or adverse political developments. Certain fixed- income securities, including obligations of the U.S. government or those explicitly guaranteed by the U.S. government, are not considered to have credit risk.

A bond's credit quality is an assessment of the issuer's ability to pay interest on the bond, and ultimately to pay the principal. Credit quality is evaluated by one of the independent bond rating agencies – for example, Moody's, S&P, or Fitch. The lower the rating, the greater the chance (in the rating agency's opinion), that the bond issuer will default or fail to meet its payment obligations. Generally, the lower a bond's credit rating, the higher its yield should be to compensate for the additional risk. The fund's underlying investment manager guidelines and credit quality guidelines seek to manage the overall fund's credit risk.

The following table presents the debt securities ratings of the GICs owned by the Plans as of December 31, 2016:

**(in thousands of dollars)**

| | | Credit Rating - Moody's/S&P | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Investment Type** | **Fair Value** | **Aaa/AAA** | **Aa/AA** | **A** | **Baa/BBB** | **Less than Investment Grade** | **Unrated** | **Exempt from Credit Quality (1)** |
| Domestic corporate bonds | $ 191,059 | $ 1,391 | $ 10,925 | $ 46,721 | $ 125,082 | $ 6,940 | $ - | $ - |
| U.S. treasury securities | 209,498 | - | - | - | - | - | - | 209,498 |
| Foreign corporate bond | 73,878 | - | 17,088 | 28,690 | 28,046 | 54 | - | - |
| Asset-backed securities | 56,930 | 56,930 | - | - | - | - | - | - |
| Foreign government bonds | 9,713 | 5,168 | 3,017 | 1,265 | 263 | - | - | - |
| Mortgage pass throughs | 111,301 | - | 86,889 | - | - | - | - | 24,412 |
| U.S. agencies securities | 23,075 | - | 23,075 | - | - | - | - | - |
| State and local government | 7,935 | - | 5,623 | 2,312 | - | - | - | - |
| Collateralized mortgage obligations | 1,562 | - | 1,562 | - | - | - | - | - |
| Commerical mortgage backed securities | 42,198 | 24,457 | 17,262 | 479 | | | | |
| Common/commingled fund: | | | | | | | | |
| Intermediate collective trust fund N | 344,115 | - | - | - | - | - | 344,115 | - |
| Short-core fixed income collective trust fund | 416,670 | - | - | - | - | - | 416,670 | - |
| Stable return collective trust fund | 174,178 | - | - | - | - | - | 174,178 | - |
| Government money market collective trust fund | 20,648 | - | - | - | - | - | 20,648 | - |
| | $ 1,682,760 | $ 87,946 | $ 165,441 | $ 79,467 | $ 153,391 | $ 6,994 | $ 955,611 | $ 233,910 |

(1) Obligations of the United States Government or obligations explicitly guaranteed by the United States Government, including mortgage pass-throughs, are not considered to have credit risk and do not require disclosure of credit quality.

(2) Assets for which the Plans do not directly own the underlying securities are excluded from this chart.

*Commingled Funds*
The Intermediate collective trust fund N is comprised entirely of securities rated BBB or better (65% are rated AAA) at December 31, 2016. Over 99% of the securities comprising the Short-core fixed-income collective trust fund are rated BBB or better (74% are rated AAA) at December 31, 2016. The government money market fund consists of US Government obligations or repurchase agreements collateralized by U.S. Government obligations.

**Custodial Credit Risk**
Custodial credit risk is the risk that, in the event of the failure of a counterparty financial institution, the Plan will not be able to recover the value of its investments and other assets that are in possession of an outside third party. The Plan does not have a formal policy to limit custodial credit risk.

**Concentration of Credit Risk**
Concentration of credit risk is the risk of loss attributed to the magnitude of the Plans' investment in a single issuer or category of issuer with similar risk. Money market funds and external investment pools are excluded from this disclosure requirement. Obligations explicitly guaranteed by the U.S. Government are not considered to have credit risk. The NC Stable Value Fund did not have any investment in any one issuer equal to 5% or more of the fair value of the NC Stable Value Fund's investments.

## 6. Fair Value Measurement

The Plans categorize fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The Plans had the following recurring fair value measurements as of December 31, 2016:

**Investments at Fair Value**
**(in thousands of dollars)**

| | As of 12/31/2016 | Fair Value Measurements Using: Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) |
|---|---|---|---|---|
| **Pooled Account** | | | | |
| **Investments measured at fair value** | | | | |
| Domestic equity securities | $ 2,725,939 | $ 2,725,939 | $ - | $ - |
| Foreign equity securities | 1,289,679 | 1,289,679 | - | - |
| Collateralized mortgage obligations | 67,447 | - | 67,447 | - |
| U.S. Treasury STRIPS | 60,023 | - | 60,023 | - |
| Domestic corporate bonds | 56,083 | - | 56,083 | - |
| Mortgage pass-throughs | 54,083 | - | 54,083 | - |
| U.S. Treasury securities | 24,933 | - | 24,933 | - |
| Asset backed securities | 16,101 | - | 16,101 | - |
| Foreign corporate bonds | 13,169 | - | 13,169 | - |
| International preferred securities | 7,016 | 7,016 | - | - |
| U.S. agencies securities | 6,465 | - | 6,465 | - |
| Foreign government bonds | 979 | - | 979 | - |
| State and local government bonds | 700 | - | 700 | - |
| Total investments by fair value level | 4,322,617 | 4,022,634 | 299,983 | - |

**Investments measured at the Net Asset Value (NAV)**

| | | Unfunded commitments | Redemption frequency | Redemption notice (days) |
|---|---|---|---|---|
| Commingled equity funds (1) | 1,678,522 | - | Daily | 1 - 2 |
| Commingled fixed income (2) | 439,483 | - | Daily | 1 - 2 |
| Mutual fund (3) | 403,212 | - | Daily | 1 |
| Commingled U.S. debt fund (4) | 331,119 | - | Daily | 5 |
| Collective investment fund (5) | 128,921 | - | Daily | 1 |
| Total investments at the NAV | 2,981,257 | | | |
| **Total Pooled Account investments at fair value** | 7,303,874 | | | |
| Accruals | (3,921) | | | |
| **Total Pooled Account investments** | $ 7,299,953 | | | |

(1) Three funds. Each are valued at the net asset value of units held at the end of the period, based upon the fair value of the underlying investments.
(2) One fund. Valued at the net asset value of units held at the end of the period, based upon the fair value of the underlying investments.
(3) One fund. NAV is determined by dividing the total value of the fund's portfolio investments and other assets attributable to the fund, less liabilities, by the total number of shares outstanding. Value determined at the end of each day the New York Stock Exchange is open.
(4) One fund. Valued at the net asset value of units held at the end of the period, based upon the fair value of the underlying investments.
(5) This fund is invested in the BNY Mellon EB Temporary Investment Fund. The Fund primarily invests in instruments issued by the US Government and Federal agencies, short-term corporate obligations, commercial paper, and certificates of deposit. The average weighted maturity of these funds does not exceed 60 days.

| | | Fair Value Measurements Using | | |
|---|---|---|---|---|
| | As of 12/31/2016 | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) |
| **Stable Value Fund** | | | | |
| **Investments measured at fair value** | | | | |
| Domestic corporate bonds | $ 191,059 | $ - | $ 191,059 | $ - |
| U.S. treasury securities | 209,498 | - | 209,498 | - |
| Foreign corporate bond | 73,878 | - | 73,878 | - |
| Asset-backed securities | 56,930 | - | 56,930 | - |
| Foreign government bonds | 9,713 | - | 9,713 | - |
| Mortgage pass throughs | 111,301 | - | 111,301 | - |
| U.S. agencies securities | 23,075 | - | 23,075 | - |
| State and local government | 7,935 | - | 7,935 | - |
| Collateralized mortgage obligations | 1,562 | - | 1,562 | - |
| Commerical mortgage backed securities | 42,198 | - | 42,198 | - |
| Investments at fair value | 727,149 | - | 727,149 | - |
| **Investments measured at the Net Asset Value (NAV)** | | | | |
| | | Unfunded commitments | Redemption frequency | Redemption notice |
| Intermediate collective trust fund N (1) | 344,115 | - | Monthly | 1 day |
| Short-core fixed income collective trust fund(2) | 416,670 | - | Monthly | 1 day |
| Stable return collective trust fund(3) | 174,178 | - | Daily | 12 months |
| Government money market collective trust fund(4) | 20,648 | - | Daily | 1 day |
| Investments at NAV | 955,611 | | | |
| **Total Stable Value Fund investments** | $ 1,682,760 | | | |

Note: Assets for w hich the Plans do not directly ow n the underlying securities and cash balances are excluded from the above table. The fair value of the Great-West Deferred Stable Asset Fund Annuity Contract and the MetLife Insurance Company Separate Account have been previously disclosed in Note 5.

(1) One fund. Valued at the net asset value of units held at the end of the period, based upon the fair value of the underlying investments.

(2) One fund. Valued at the net asset value of units held at the end of the period, based upon the fair value of the underlying investments.

(3) One fund. Valued at contract value. Fair value is derived using a market/book ratio.

(4) One fund. Money market fund. NAV at $1/unit.

*Valuation Methodologies and Inputs*

Equity securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities.

Level 2 U.S. Treasuries are evaluated by using data from several live feeds which include active market makers and inter-dealer brokers. Sources are reviewed on the basis of their historical accuracy for individual issues and maturity ranges.

Level 2 Domestic bonds are priced using both spread-based and price-based evaluations. Evaluators survey the dealer community to obtain relevant trade data, benchmark quotes and spreads.

Level 2 Mortgage Pass-throughs are evaluated on interest rate movements and other market data to derive spread, yield and/or price data as appropriate allowing data points to be extrapolated for application across a range of related securities.

Level 2 Collateralized Mortgage Obligations evaluators monitor structured product markets, interest rate movements, new issue information and other market data. Market color such as trades, bids, and offers are applied to the model.

**7. Related Party Transactions**

The Plans contract with Galliard, a subsidiary of Wells Fargo, to act as a fiduciary investment advisor for the NC Stable Value Fund. Galliard has discretion over the benefit responsive contracts and the underlying investment managers, subject to approval by the Board and the Department. Galliard also has the authority to invest in securities subject to guidelines agreed upon by the Board. As an advisor, Galliard is primarily responsible for ensuring that negotiated investment contracts are adhered to by the insurance companies, bank or other eligible providers who have entered into such contracts. Not less than quarterly, Galliard reports the financial condition of the investment contracts and whether the contracts are being administered according to their respective terms. The fees for wrap coverage, investment management and advisory services are deducted from participants' account balances.

Prudential Retirement, a specialized unit of the Prudential Financial Investment Division, provides administrative services related to the NC Stable Value Fund and the Pooled Account. Prudential Retirement is also the provider of recordkeeping and participant services. The fees to Prudential are deducted from the participants' account balances. One of the funds within the NC Fixed Income Fund is a commingled vehicle offered by Prudential Trust Company and managed by Prudential Investment Management, Inc. Jennison Associates, a registered investment advisory division within Prudential Global Investment Management, manages a portion of the NC Stable Value Fund. Affiliates of Prudential Retirement also are a wrap provider (Prudential Insurance Company of America) and an investment manager (PGIM, Inc.) for the NC Stable Value Fund.

The Bank of New York Mellon serves as the custodian for the Plans and provides global custody services related to the Pooled Account. These fees are deducted from the participants' account balances. Bank of New York Mellon also provides a short term cash vehicle for the temporary investment of funds until they are invested on a longer term basis.

**8. Tax Status**

The 401(k) Plan received a favorable determination letter from the Internal Revenue Service ("IRS") on November 14, 2016. The determination letter stated that following review, the 401(k) Plan was in compliance with all applicable sections of the IRC. The 401(k) Plan document was modified on December 15, 2016.

The 457(b) Plan received a favorable determination letter from the IRS on July 6, 1993. The determination letter stated that following review, the 457(b) Plan was in compliance with all applicable sections of the IRC. Since that time, the 457(b) Plan document has been modified from time to time, with the last revision made December 10, 2015.

The Plans are subject to rules and regulations promulgated by the IRS. Failure to comply with the rules and regulations of the IRS could result in penalties to the Plans and for the Plan Sponsor. The Department has analyzed the tax positions taken by the Plans, and has concluded that as of December 31, 2016, 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.

**9. Plan Termination**

Although the General Assembly of North Carolina has not expressed any intent to do so, it has the right to terminate the Plans under the provisions of each of the Plans' documents. In the event of a plan termination, assets of that plan would be distributed to participants as soon as administratively possible.