To: Ben Teague, NCI Audit Committee Chair, NCInnovation
Michael Botzis, BDO
Michelle Bolas, CEO and Linda Hall, CFO
Cc; Audit Committee Members
From: Art Pope, Member NCInnovation Board of Directors and Audit Committee
Date: September 25, 2026

Re: Correction of NCInnovation Audited Financial Statements for FYE June 30, 2024 and subsequent years, in regard to the Accrual of the Pilot Grant

I. Executive Summary

It is well documented that N.C. Gen. Stat. § 143-178(d), the NCInnovation Board resolution dated May 14, 2024, the NCI Funding Agreements with the Pilot Grant university recipients, and the NCI and NC Collaboratory Master Service Agreement (the "MSA") all required NCI to consult with the Collaboratory before NCI could finalize the Pilot Grant terms and amounts, distribute the state "investment funds," and for the university recipients to have the right to receive the Pilot Grants.

Pursuant to the statute, resolution, and agreements, NCI had no obligation to pay the Pilot Grants unless and until the consultation with the Collaboratory was completed. It is correct that the consultation did not give the Collaboratory the right to disapprove of the grants. However, NCI retained the right to revise the terms and amounts of the Pilot Grants, or even cancel a grant, in response to its consultation with the Collaboratory.

It is now well-documented that, until mid-September 2024, NCI did not initiate the consult, the Collaboratory did not respond to the consult, and the university recipients of the Pilot Grants were not notified of the consultation.

Applying the standards and test under GAAP, specifically ACS 958-605-25-5A, the requirement for the consult—the barrier that had to be overcome—was not completed until September 2024, during NCI's Fiscal Year beginning July 1, 2024 and ending June 30, 2025.

NCI's management and BDO erred in accruing the Pilot Grants as an expense and liability for NCI's previous fiscal year ending June 30, 2024. According to BDO (when the audit for this year was being reviewed on November 1, 2024) the decision to make the accrual for that year was based on NCI's management's representation that it expected the requirement to consult to be fulfilled and that this would be "perfunctory." Relying on expectations is not the correct standard or test for satisfying a condition under ASC 958-605-25-5A.

This error by NCI's management and BDO is material, as the amount of the Pilot Grant accrual for FYE June 30, 2024 was $4,011,370. This increased NCI's expenses from $4,139,000 to $8,150,425, a 96% increase in expenses for the year.

As a material error, NCI should restate its audited financial statement for its FYE June 30, 2024 and subsequent years, in accordance with FASB ASC 250, This will also require amending (once again) NCI's Form 990 for FYE June 30, 2024 and subsequent years, including the calculation of the NCI's allowable lobbying expenses under an H election.

NCI's management, based on different reasons offered at different times, has determined that the original accrual was proper and that no correction is necessary. BDO, as auditor, has apparently indicated that it will rely on NCI's management representations and decisions; accordingly, BDO is not requiring a restatement of its previously issued audit of NCI's fiscal year ended June 30, 2024.

The NCI Board of Directors and its Audit Committee have a duty to provide oversight to help ensure NCI's compliance with applicable law and GAAP standards. I respectfully recommend and request that the NCI Board of Directors review the following and not defer to or rely on management's decision at this time—particularly in light of the additional documentation and information—to determine whether restatement of NCI's audited financial statements is necessary.

II. **Requirement for NCInnovation to Consult with NC Collaboratory for Grants**

A) Statutory Requirement

N.C. Gen. Stat. § 143-178(d) sets forth the "requirements" that "must be met" by NCInnovation for it to receive and retain state funds.[1] N.C. Gen. Stat. § 143-178(d)(3) sets forth the specific requirement:

> *"NCInnovation shall act on behalf of, and perform its duties for the benefit of, the State. Where those duties involve the distribution of investment income* ***NCInnovation shall (i) consult with the North Carolina Collaboratory …"*** Emphasis Added.

The Pilot Grants were a "distribution of investment income."

The use of the term "consult," as commonly understood and as used in North Carolina statutes, requires one party to formally present a detailed report of a proposed expenditure and to hear recommendations from the other party.[2] [3]

When the statute uses the terminology "requirements" that "must be met" and the imperative "shall consult,"; this clearly establishes a condition—a "barrier that must be overcome"—before NCI can expend state investment funds on grants. Note, the statutory condition is imposed on NCI itself, as the recipient of state funds, rather than imposed on university recipients of NCI's Pilot Grants.

B) NCI Board of Directors Approval Subject to Meeting Condition

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[1]N.C. Gen. Stat. §143-728(d) Requirements. – In order to receive the endowment and retain State funds, all of the following requirements must be met:

[2] N.C. Gen. Stat. § 12-76.1 sets forth the detailed procedure the Governor must follow to consult. Specifically, it requires the Governor or relevant state agencies to consult with the Joint Legislative Commission on Governmental Operations (Gov Ops) before authorizing certain over-expenditures, grant distributions, or capital projects.

[3] In North Carolina the term "consult" is ordinarily understood to require the party to confer with or seek advice from the specified entity. Where an agreement or statute directs that a party "shall…consult with" another party before taking a specified action, the requirement is generally interpreted to mean that consultation must occur in a manner that allows the advice or input to be considered prior to the decision or action at issue

In order to comply with the statutory requirements, the Board of Directors approval of the Pilot Grants was expressly made conditional. The May 14, 2024 Board minutes stated, in relevant part:

*"motion to approve the eight projects **subject to** the completion of the required legislative requirements."* [Emphasis added.]

The Board discussion before the adoption of the motion expressly referred to the fact that NCI had not yet entered an agreement with the North Carolina Collaboratory ("Collaboratory") to conduct the statutorily required consultation. Then NCI CEO Bennet Waters acknowledged at the time this was these were "conditions" imposed by Board of Directors.[4] Again, it should be noted the Board, in compliance with the statute, imposed the condition on NCI itself, not on the university recipients of the Pilot Grants.

C) Pilot Grant Funding Agreements

NCI entered into "Funding Agreements" with seven of the eight university recipients of the Pilot Grants on or about June 27-28, 2024, before the end of the June 30, 2024 Fiscal Year.[5] However, consistent with the statute and Board's conditional approval, the Funding Agreements expressly put the Pilot Grant recipients on notice and incorporated the terms that NCI consult with the Collaboratory before any state funds could be distributed. Page 2 of the standard Funding Agreement stated in part:

> ***The NC Collaboratory's Role as Funding Agent***
> *The NC Collaboratory "Collaboratory" serves as the Funding Agent for transferring funds to the recipient university. As stated in Article 76B of House Bill 259,*
>
> *"NCInnovation shall act on behalf of, and perform its duties for the benefit of, the State. **Where those duties involve the distribution of investment income, NCInnovation shall (i) consult with the North Carolina Collaboratory (Collaboratory),** established under G.S. 116-255, **for purposes of making determinations regarding terms and amounts** of distributions and ii) use the Collaboratory to manage the distributions.* Emphasis added.

Implication:

> ***This Funding Agreement is written in compliance with the statutory requirements** as described in Article 76B. For the purposes of this funding agreement, all funds must be managed in accordance with the attached Appendices and Terms and Conditions of this Agreement, and the original*

[4] Email 2024.05.15 from Bennet Waters, "Next Steps to Resolve BOD Grant Requirements." See Attachment A
[5] See "2024 Pilot Awards NC Collab Document Tracker," provided September 21, 2026, prepared by NCI CFO Linda Hall.

proposal submitted to NCI by the Project's Principal Investigators. Emphasis added.

In summary, while six of the eight pilot grant Funding Agreements were entered into prior to the end of the June 30, 2024 Fiscal Year, the Funding Agreements were expressly conditional upon—subject to—the requirement that NCI consult with the Collaboratory before the Pilot Grant terms and amounts were finalized and the recipients were entitled to payment of the grants.

D) NCI Master Service Agreement with the NC Collaboratory, August 30, 2024

NCI did not enter into an agreement with the Collaboratory until August 30, 2024, two months after the end of the June 30, 2024 Fiscal Year. [6] Rather than the agreement and expected consultation being "perfunctory," NCI CEO Bennet Waters stated in July that NCI and the Collaboratory were at an "impasse" in reaching an agreement.[7]

The Service Agreement states the parties acknowledge that the statute requires NCI to consult with the Collaboratory and it sets forth the process for the consult, including "when it will take place." Because the Service Agreement was not effective until August 30, 2024, NCI could not have completed the consultation with the Collaboratory before that date. Therefore*, "the completion of the required legislative requirements"* could not have been met prior to the end of NCI's June 30, 2024 fiscal year. Likewise, the Board motion making the Pilot Grant approval subject to meeting these statutory requirements, was not satisfied before the FYE of June 30, 2024.

E) NCI Consult with NC Collaboratory and Requirement Met in September 2024

Jeffery Warren, Executive Director of the NC Collaboratory, sent Bennet Waters, President of NCI, a "Summary of Completed Pilot Project Fund Transfers," dated October 24, 2024, ("Consult Memo:).[8] The Consult Memo included on page 2 a table setting forth the dates when the consultation between NCI and the Collaboratory were initiated and completed. The steps and dates were:

Consult Request [by NCI]:	9/11/24
Consult Response [by the Collaboratory]:	9/12/24
Ex D sent to campus:	9/17/24
Ex D returned:	date range from 9/18/24 to 10/8/24

On September 21, 2026, CFO Linda Hall provided the NCI Audit Committee the previously refernced "2024 Pilot Awards NC Collab Document Tracker." While the information is more limited and the terminology is different, the dates are consistent with the above Consult Memo.

[6] MSA uploaded to BoardEffect September 19, 2024. See https://ncinnovation.boardeffect.com/downloads/vfile/21369550

[7] Email 2024.08.18 From Bennet Waters re NC Collaboratory Consult Highlight Added. See Attachment B.

[8] "Summary of Completed Pilot Project Fund Transfers," dated October 24, 2024, from the NC Collaboratory to Bennet Waters, NCI. See Attachment C.

CFO Linda Hall also provided a document titled "NC Collaboratory Document Summary Request for FY26 Audit Contents." This long document contained sections with copies of "Consultation Briefs and Approval Emails" beginning on p.33; "Funding Directive Memos" beginning on p.58; and, Recipient Acknowledgements" beginning on p.67. While the copies of these documents omitted the dates they were signed, I do not think CFO Linda Hall would dispute that they were exchanged and signed in September 2024. [I do not have information as to whether NCI's prior management shared any of these documents with BDO during the 2024 audit of the FYE June 30, 2024.]

Given the consultations for the Pilot Grants required by statute, the Board motion, and the Funding Agreements were not initiated and completed until September 2024—more than two months after the end of the FYE June 30, 2024—the Pilot Grants should not have been accrued for NCI's FYE June 30, 2024. Instead, the Pilot Grants should have been accrued in NCI's Fiscal Year that began July 1, 2024 and ended June 30, 2025, because the consult requirement, the condition, the barrier to be overcome, to authorize the final terms and amounts of grant payments was not met and completed until September 2024.

III) NCI's Management and BDO Justification for Accruing the Pilot Grants in FYE of June 30, 2024

A) NCI Management and BDO Position in November 2024 that Consult Requirement was "Perfunctory" and therefore Not a Condition

The question of whether or not the Pilot Grants were properly accrued in FYE of June 30, 2024 was raised at the November 1, 2024 NCI Audit Committee meeting.

Michael Botzis, on behalf of BDO ("BDO Botzis") initially stated in his presentation that the Board approved grants, *"**did not have a conditional requirement related to them. . . .** and met the GAAP revenue recognition for recording a liability.*"[9] *"When those non conditional grants were approved, those were accrued on the books at that time.*"[10] Emphasis added.

I questioned BDO Botzis about his statement that the Pilot Grants were "non conditional," pointing out the Board minutes stated the approval was made "subject to" compliance with the statute (as detailed above).[11]

Botzis on behalf of BDO then responded:

*"It was management's feeling that that would be obtained. And so that was not considered to be a substantial point that would block. It was viewed by to be more **perfunctory** than to exclude those. And so, we did not, we did not view that as something that would be of substantive nature to preclude accrual of those grants."*[12] Emphasis added.

Respectfully, the test is not what prior management believes is likely to happen in the future.

[9] NCI Audit Meeting, November 1, 2024, Recording in BoardEffect, begin about the 35:50 mark
[10] Ibid, begin about the 43:17 mark
[11] Ibid, begin about the 50:40 mark
[12] Ibid, begin about the 55:19

CFO Linda Hall on September 21, 2026 provided the NCI Audit Committee a publication by PwC that gives guidance and commentary on when grants should be accrued in accordance with ASC 958-605-25-5A.[13] In Question NP6-3, PwC addresses whether, when management believes a barrier [condition] is *"perfunctory," "the likelihood of achieving the barrier when initially classifying the grants as conditional or unconditional"* should be considered. PwC's response was unequivocal: "*No. Neither the likelihood that a barrier will be met nor the resource provider's intent to enforce a right of return may be considered in evaluating whether an agreement is conditional."*

BDO simply erred in considering NCI management's "feelings" that the consult would be "obtained" and viewing it as "more perfunctory."

Also it is important to note as of November 1, 2024, NCI management knew it had reached an "impasse" in negotiations with the Collaboratory in mid-July 2024[14]; the MSA between NCI and the Collaboratory was not agreed upon and signed until August 30, 2024; and the actual consultation pursuant to the MSA was not initiated until September 2024.

B) Linda Hall Assertion of a Consultation Separate from the Collaboratory MSA

The requirement for NCI to consult with the Collaboratory was discussed at a September 8, 2026 meeting with NCI Audit Chair Ben Teague, Audit Committee member Art Pope, NCI CFO Linda Hall, and BDO Botzis. At this meeting CFO Hall stated that, prior to the Service Agreement (the "MSA") being executed on August 30, 2024, there was a **"**consultation brief" that was completed in a timely manner with Jeff Warren at the Collaboratory, that satisfied the legislative requirement, and that there is evidence of this she could provide. Linda Hall failed to present any such evidence.

To the contrary, documentation provided by Linda Hall was from mid-September 2024 pursuant to the MSA signed August 30, 2024. This documentation confirms the statutory requirement, Board requirement, and Funding Agreement requirement to consult the Collaboratory was not completed until September 2024. Therefore, based on the documentation provided, the Pilot Grants should not have been accrued in NCI's fiscal year ending June 30, 2024.

[13] "6.6 Conditions on contributions" by PwC, published 27 August 2026.
[14] Email 2024.08.18 From Bennet Waters re NC Collaboratory Consult Highlight Added. See Attachment B for full text.

C) Assertion that the Pilot Grants Were Not Conditional

NCI management has now taken the position that there was no condition, no requirement, that had to be met. In a September 21, 2026 "NCI FY26 Audit Questions and Requests Tracker," NCI management stated in full:

> *After review and discussion with BDO it has been determined that the expense recognition made in FY24 for the Pilot Grants was appropriate and no prior period adjustment is warranted.*
>
> *Despite the timing of the NC Collaboratory MSA execution and consultation briefs which occurred in August and September 2024, the grants were not conditional as a result of the NC Collaboratory process timing. The NC Collaboratory is not a party to the funding agreement, has no authority to approach or reverse the decision of the Board of NCI and is in effect a payment conduit to the grant university recipients.*
>
> *The consultation is a step in the payment process, and all documentation was in place prior to making payments for all 8 grants as evident in the supporting documentation requested.*

At best, this rationalization is a strawman argument. At worst, it is nonsensical. It has never been argued that the Pilot Grants were "*conditional as a result of the NC Collaboratory process timing."*

As set forth above, the Pilot Grants were conditional because of the requirements of the statute and the NCI Board motion approving the Pilot Grants "subject to" compliance with the statute, which includes the requirement to consult with the NC Collaboratory.

It is correct that the NC Collaboratory is not a "party" to the funding agreements for the Pilot Grants. However, as set forth above, the statutory requirement that NCI first consult with the NC Collaboratory to determine the terms and amounts of the Pilot Grants is expressly stated in the Funding Agreements, consistent with and implementing the statute, the NCI Board motion, and the Funding Agreements. Further, while the NC Collaboratory and NCI are not parties to the Funding Agreements, they are parties to the Master Service Agreement, under which NCI is again required to consult with the NC Collaboratory to determine the terms and amounts of the Pilot Grants.

It is correct, and has never been argued, that the NC Collaboratory could *"reverse the decision of the Board of NCI."* However, the statute does impose the requirement, a condition that the NCI Board "consult" with the NC Collaboratory before it spends state investment funds. In short, In short, the process enacted by the NC General Assembly required NCI to consult with the NC Collaboratory—not merely give it notice.

It is correct that N.C. Gen. Stat. § 143-178(d)(3)(ii) states that NCI shall *"(ii) use the Collaboratory to manage the distributions*." However, while this subsection (ii) obviously does make the NC Collaboratory *"a step in the payment process,"* it does not repeal the immediate preceding N.C. Gen. Stat. § 143-178(d)(3)(i) which requires the consultation. Again, N.C. Gen. Stat. § 143-178(d)(3)(i) states, :*Where those duties involve the distribution of investment income* ***NCInnovation shall (i) consult with the North Carolina Collaboratory …"*** Emphasis Added.

In the sections of PwC guidance quoted above, NCI's management highlighted the "6.6.1.3 Reporting and administrative stipulations." I anticipate NCI's management and/or BDO will now argue that the consult requirement was a "trivial reporting" requirement. It is agreed that, as summarized by PwC, *"routine administrative stipulations are not considered barriers that affect the timing of recognition of contribution revenue or expense."*

However, the consult requirement is <u>not</u> an administrative stipulation or trivial reporting requirement imposed on the university recipients of the Pilot Grants. As reviewed above, it is an express statutory requirement, that "must be met," requiring that ***"NCInnovation shall (i) consult with the North Carolina Collaboratory"*** before disbursing state funds. N.C. Gen. Stat. § 143-178(d). Emphasis added. The consult requirement is a substantive condition enaced by statute, imposed on NCI by its own board, and expressly set forth into the Funding Agreements and the MSA.

If NCI was not authorized by state statute to disburse state "investment" funds until the consultation in regard to the "terms and amounts" of grants with the Collaboratory was completed, and the Funding Agreements incorporated this requirement, then the Pilot Grants could not be accrued until this requirement (condition, barrier) was met. This occurred in September 2024, not during the Fiscal Year Ending June 30, 2024.

IV. Conclusion

The above error by NCI's management and BDO is material, as the amount of the Pilot Grant accrual for FYE June 30, 2024 was $4,011,370 of the total expenses $8,150,425. I respectfully request that the NCI Audit Committee and full Board of Directors to carefully consider the merits of this issue, and direct NCI's management to correct the mistaken accural of the Pilot Grants expense in the audited financial statement for Fsical Year End Juen 30, 2024, and the subsequent years as necessary.