

APPENDIX F

Establishment of an Associated Entity – The University of North Carolina at Chapel Hill

The Kenan-Flagler School of Business of the University of North Carolina at Chapel Hill has requested authority to establish three associated entities, the KFBSF Private Equity Fund I, L.P., the KFBSF Real Estate Fund I, L.P., and KFBSF, Inc., none of which would have tax exempt status at their time of establishment. Application for tax exempt status will be made after the entities are established, but there is no assurance the entities will qualify.

The University of North Carolina Regulation #600.2.5.2[R] requires that associated entities have not for profit corporate and tax exempt status unless the Board of Governors approves otherwise. The Kenan-Flagler School of Business at UNC-CH has requested establishment of a not for profit corporation and two LLC investment funds, to be structured as North Carolina limited partnerships, as associated entities without acquiring nonprofit tax exempt status. They would be educational programs of the Business School.

The LLCs will give selected students hands-on experience in operating private investment funds. These students will work with faculty and friends of the Business School to identify and evaluate investment opportunities and to make investment recommendations to the General Partner of each entity. The students will participate, without pay, as part of an investment management course, for academic credit. After an investment is made by the partnerships, the students will monitor the investment. Through the identification, evaluation and monitoring process, it is expected that students will gain insights into the operation and management of private investment funds and their portfolio companies and establish personal and professional relationships with investment managers. A secondary objective is to provide investment returns to the limited partners who are the investors.

The General Partner of each investment fund would be KFBSF, Inc., a North Carolina not for profit corporation of which the Kenan-Flagler Business School Foundation, Inc. (the Business Foundation) would be the sole member. The investors will be by invitation only and will be selected for their expertise and relationship with the school.

The General Partner would be organized and operated to support the Business School and its educational programs and would apply to the Internal Revenue Service for a determination that it is exempt from tax under Section 501(c)(3) of the Internal Revenue Code. However, there is no assurance that the General Partner would qualify as a tax exempt entity.

The General Partner would be managed under the direction of its Board of Directors. The Board of Directors would consist of five directors, three of whom would be employees of the University assigned to the Business School and two of whom would be elected by the Board of Directors of the Business Foundation. The University directors would be the Chief Financial Officer of the Business School and two members of the faculty at the Business School appointed by the Dean from time to time (one of whom may be the Dean).

From funds provided by the Business Foundation, the General Partner would make capital contributions to each investment fund equal to 1% of the total capital contributions to that fund. The General Partner would initially be entitled to receive from each investment fund a management fee equal to 2% per annum of each Limited Partner's capital commitment, payable quarterly in advance. The General Partner would be responsible for compensating its service providers and for its general overhead expenses, including rent, supplies, utilities and equipment, and for routine travel and related expenses incurred in investigating investment opportunities and monitoring investments.

After distributions to the Limited Partners equal to the amount of their capital contributions and an 8% preferred return on their capital contributions, the General Partner would be entitled to receive a portion of the net profits realized by the investment fund, 40% in the case of the real estate fund and 20% in the case of the private equity fund. To the extent that the amounts paid to the General Partner exceeded its operating expenses, the excess would be transferred to the Business Foundation and used to support the Business School.

The articles of incorporation of the General Partner would provide that, on dissolution, any remaining net assets would be transferred to the Business Foundation. In addition, the General Partner would adopt appropriate conflict of interest, document retention, and whistleblower policies. Accordingly, subject to obtaining tax exempt status, the General Partner would satisfy the requirements for associated entities of the UNC regulation. However, the Internal Revenue Service may take the position that the fees being charged by the General Partner are inconsistent with tax exempt status.

It is recommended that the Board of Governors allow the establishment of KFBSF Private Equity Fund I, L.P., KFBSF Real Estate Fund I, L.P., and KFBSF, Inc. as UNC-CH associated entities to manage the investment funds as educational programs at the Kenan-Flagler School of Business without their obtaining nonprofit tax exempt status.