

**BUDGET, FINANCE AND INVESTMENT COMMITTEE
BOARD OF TRUSTEES
UNIVERSITY OF VERMONT AND STATE AGRICULTURAL COLLEGE**

A meeting of the Budget, Finance and Investment Committee of the Board of Trustees of the University of Vermont State and Agricultural College was held on Friday, October 23, 2009 at 9:45 a.m., in the Silver Maple Ballroom, 401 Dudley H. Davis Center.

MEMBERS PRESENT: Co-Vice Chairs Robert Cioffi and Samuel Bain, Bill Botzow, Carolyn Branagan, Jason DePatie, Daniel Fogel, John Hilton, Jr., Susan Hudson-Wilson, John Snow, Donna Sweaney, and Mark Young

REPRESENTATIVES PRESENT: Faculty Representatives Albert Joy and Bud Meyers, Alumni Representative Meg Guziwicz, Staff Representatives Kit Ardell and Rodman Corey, and Student Representatives Kate Ash and Tram Tran (attending for Nick Cafarelli)

OTHER TRUSTEES PRESENT: Board Chair Ian Boyce and Board Vice Chair Frank Cioffi

PERSONS ALSO PARTICIPATING: Vice President for Finance and Administration Richard Cate and Associate Vice President for Budget and Resource Management Ted Winfield

ABSENT: Chair Debbie McAneny, Alumni Representative Walt Blasberg, and Student Representative Nick Cafarelli

Co-Vice Chair Cioffi called the meeting to order at 10:00 a.m.

Approval of Minutes

A motion was made, seconded, and voted to approve the minutes of the May 15, 2009 meeting.

Use and Availability of Net Assets

Vice President Cate reported on the status of net assets recorded in the University financial statements at the end of FY 2008 and preliminary estimates for FY 2009. Net assets include all forms of financial resources including cash and accounts receivable, and may be unrestricted in nature or restricted to a specific purpose. The trustees discussed the scale, nature and use of net assets across the University with a focus on the degree of oversight and the decision making process associated with spending decisions.

The University's reappropriations policy, which allows academic units to carry forward unspent general fund dollars from one fiscal year to the next to fund multi-year commitments, was also discussed. Starting in FY 2010, prior year-end general fund balances, which have been approved for spending, will be transferred to a new fund type (fund 108) to clearly identify them as available to units for spending. Associate Vice President Winfield provided examples of academic commitments to fund 108, such as multi-year staffing plans and faculty start-up packages. He added that it was the dean's responsibility to demonstrate the use of both annual operating general fund dollars and the long-term plan for balances in fund 108. Board Chair Boyce expressed the need for a robust analysis on a year-to-year basis of the continued need for

balances held in fund 108. Trustee Hudson-Wilson expressed her concern as to how unspent general fund balances were treated. She recommended that surplus dollars be returned to the general fund for redistribution by central administration based on strategic need as demonstrated by academic units. There was a discussion about different approaches to the re-appropriation policy.

The Committee also discussed the balance in the Treasury Operations account, which accrued as a result of the difference between the amount of money collected internally for debt service payments and that paid for external debt service obligations. Trustee Young asked whether sufficient funds were being collected to cover out-year payments. When Treasury Operations was first established, the internal budgeting practice had University budgets contributing toward external debt payment obligations on a consistent basis using a blended interest rate and shorter repayment schedule than the underlying long-term debt. The plan was to create a fund balance to use as the basis for future capital needs. Recognizing budget challenges in FY 2009, the administration amended the internal debt service amortization schedule so that internal funding collected more nearly equals external debt service obligations. Vice President Cate explained that the internal debt service would cover the external obligations in the out years. Trustee Young asked that he have the opportunity to review the changes in policy and practice that have occurred since Treasury Operations was set up. Associate Vice President Winfield said he would be happy to do so.

The discussion concluded with a request from the Committee for Vice President Cate to bring to the February Committee meeting information related to:

- Further details on the encumbrances against the University's cash assets.
- Separate listings of cash and accounts receivable net assets.
- A description of the process for cash flows in and out of the net asset accounts.
- The appropriate balances for the various accounts.
- A cash management plan to be first vetted with the Investment Subcommittee.
- More details about the academic unit reappropriations process.
- A description of any outliers among the various subaccounts.

Greening of Aiken Financing

The Committee reviewed the proposal to proceed with the Greening of Aiken renovation, originally approved in December 2007. The project is proposed to cost \$13.4M, with at least \$3.4M coming from non-debt sources. Vice President Cate led the Committee through the different permanent financing methods that may be used to secure the funds to proceed with the Aiken project (tax exempt bonds at a rate of approximately 4.7%; taxable Build America Bonds with a rate of approximately 3.55%; Recovery Zone Economic Development Bonds with a rate of approximately 3.0%). The up to \$10M in new bonds would be combined with a potential tax exempt refunding of approximately \$22M of 1998 bonds, which are not eligible for Build America Bonds. The University's debt advisors and the University Administration agree that it would be best to make two external bullet payments in the last two years of the amortization schedule for the bonds. However, Vice President Cate recommends making annual debt service payments to the internal bank in order to ensure that the funds are available in the out years to make the bullet payments.

The Committee discussed at length the potential for using cash reserves versus new debt for the project, including the issuance costs and carrying costs associated with a bond issuance. Co-Vice Chair Bain expressed his transition from opposition to support for the project and for debt financing. He stated that it is a good economic time to start this project, with availability of EPA grant funding and the low cost of Build America Bonds. Trustee Snow stated he is in favor of using the University's cash reserves and questioned the University's need to maintain the surplus and incur the expense of financing a new bond. Trustee Hudson-Wilson agreed. She also noted that the project's non-debt sources was reduced from \$5.0M to \$3.4M and felt that the Committee should challenge the Rubenstein School and Development and Alumni Relations to raise the original \$5.0M in non-debt resources as specified in 2007. Trustee Botzow raised the issue of whether the project would be eligible for either the Build America Bonds or the Recovery Zone Economic Development Bonds as the latter are allocated by county. If not, he added that perhaps the University should consider going to cash rather than the open bond market.

Vice President Cate clarified that the resolution is not to approve a bond issue, but to give permission for administration to bring forward a financing structure for Executive Committee approval. He explained that continued delays in proceeding could jeopardize the University's ability to retain the currently available EPA grant funding since the EPA grant is for the Aiken project only and has already received a two year extension. President Fogel stated that he is 100% behind the project and would support either borrowing or using University cash. He sees the merit of a rainy day fund - pandemic conditions could exhaust the University's cash in just a few payrolls. Co-Vice Chair Bain commented that there are structural issues with the budget and the Committee needs to be sympathetic to administration on bonding and not using the University's cash. The rates are low, the carrying cost is money well spent, and this will give the University breathing room to protect its future.

Trustee Young made a motion to consider the resolution approving a financing plan for the Greening of Aiken. The resolution was voted in two parts.

Part 1: Whether to proceed with the Greening of Aiken Project as per the 2007 Board of Trustees meeting. The Committee unanimously approved proceeding with the Greening of Aiken Project.

Part 2: Whether to approve the Resolution as amended, using debt to cover up to \$10M of the cost. The Committee approved the amended resolution, for recommendation to the full Board (8-3).

Resolution Approving Financing Plan for the Greening of Aiken

WHEREAS, the Trustees reviewed and authorized the renovation of Aiken Hall in November 2007 based on a total project cost of \$13,400,000, with \$5,000,000 to be funded from gifts and grants and \$8,400,000 to be funded from long-term borrowing; and

WHEREAS, the need for and strategic and operational importance of the project remain high, and it is now appropriate to proceed with the project;

NOW, THEREFORE, BE IT RESOLVED, that the President and the Vice President for Finance and Administration, or their successors or designees, are hereby authorized to commence the Aiken Hall Project and to execute any and all contracts and documents necessary to undertake the Project at a total Project cost not to exceed \$13,400,000 to be financed through use of ~~the existing~~ gift and grant support of at least \$3,400,000 and ~~long term borrowing financing~~ of up to \$10,000,000. The President and Vice President may immediately proceed to use ~~the existing the available gift and grant funds \$3.4 million~~ for this purpose.

BE IT FURTHER RESOLVED, that the President and Vice President shall ~~determine~~ develop the precise character of the long-term bond financing proposal, to be subsequently submitted for approval by the Board, that will secure up to the remaining \$10,000,000. ~~These~~ officials may include in the recommended financing package the use of taxable Build America Bonds and/or Recovery Zone Economic Development Bonds to the degree that the Project is eligible for these federal programs. The financing proposal may also include the redemption and refinancing of up to \$22,000,000 of bonds previously issued by the University. These bonding recommendations will be brought to the Executive Committee for action if they are fully developed before the February 2010 Board meeting, and that Committee is hereby authorized to approve a financing proposal that conforms with this resolution.

Report of the Investment Subcommittee

Long-Term Investment Pool, Performance and Manager Review

Robert Cioffi, Chair of the Investment Subcommittee, led the Committee through a discussion of Long-Term Investment Pool allocations and performance through June 30, 2009. At June 30, 2009, the aggregate market value of the endowment was \$260 million. The portfolio had returns of 11.1% for the quarter and (-20.4%) for the fiscal year, which was favorable to the benchmark and peers. The annualized returns since inception (5/31/87) were 7.7%. At August 31, 2009, the portfolio had returns of 1.5% for the month and 6.6% for the quarter. Chair Cioffi noted that the endowment was up at the end of September with an aggregate market value approximating \$280 million.

Chair Cioffi reported that the Subcommittee met several times with no major changes to the portfolio. The Subcommittee has made some changes to underlying managers, and made minor adjustments to asset allocation targets. The Subcommittee met with several current managers in September in New York City.

Annual Approval of the Endowment Budget Policy

The Subcommittee reviewed the spending rate for the fiscal year 2011 resolution for the pooled endowment. The members reaffirmed the spending rate of 4.5 percent of the average market value for the previous thirteen quarters ending in December 31 for the prior calendar year. Chair Cioffi asked the Budget, Finance, and Investment Committee to approve the Resolution Reaffirming the Endowment Budget Policy. The annual approval of the Endowment Budget Policy was approved unanimously by the Committee for recommendation to the full Board.

Annual Approval of Endowment Management Fee

The Investment Subcommittee had discussed the Endowment Management Fee at their last meeting. Vice President Cate had provided the Subcommittee with a breakdown of endowment-related administrative expenses and fees. The Resolution reaffirming Endowment “Administration” Fee, first called Endowment Management Fee (September 2003) had a fee of 50 bps to offset the cost of running a capital campaign. The campaign ended 1.5 years ago. On October 21, 2009 the Subcommittee recommended reducing the fee from 50 basis points to 25 basis points, and to rename the fee as the endowment administration fee. The resolution of the Investment Subcommittee was approved unanimously by the Committee for recommendation to the full Board.

Resolution Reaffirming Endowment ~~Management~~ Administration Fee

RESOLVED, that the *Endowment Management Fee* is renamed the *Endowment ~~Management~~ Administration Fee Policy* and is reaffirmed as amended below:

BE IT RESOLVED, that the Board of Trustees hereby approves a 0.50.25 percent fee applied to the University endowment, to cover reasonable costs associated with endowment administration, management and operation; and

BE IT FURTHER RESOLVED, that on a fiscal year basis, the fee will be calculated reviewed and assessed annually as 0.50.25 percent of the average market value of the University endowment for the previous thirteen quarters ending December 31 of the prior calendar year; and

BE IT FINALLY RESOLVED, that the Investment Subcommittee will review and make recommendation to the Budget, Finance and Investment Committee regarding the reaffirmation or revision of the *Endowment ~~Management~~ Administration Fee Policy* each year no later than October 31.

Adopted by: Board of Trustees - September 13, 2003

Reaffirmed: Board of Trustees - September 8, 2007

Board of Trustees - September 5, 2008

Amended: Board of Trustees – October 24, 2009

Annual Asset Allocation Review

Chair Cioffi reported on the Subcommittee’s annual review of asset allocation targets in the Long-Term Pool, conducted on January 27, 2009 in Boston. The current asset allocations are on target.

EXHIBIT 1
UNIVERSITY OF VERMONT
ASSET ALLOCATION STRATEGY

Asset Class	Current Target	Revised Target	Current Range
U.S. Equity	22.0	25.0	15-30
Global ex U.S. Equity	23.0	22.0	15-45
Developed Markets	11.5	12.0	10-25
Emerging Markets	11.5	10.0	5-20
Marketable Alternatives	20.0	17.5	15-25
Real Assets (Inflation Hedging)	15.0	12.5	10-25
Private Equity/Venture Capital	10.0	10.0	5-20
Fixed Income	10.0	10.0	5-25
Cash and Cash Equivalents	0	3.0	0-5

Adopted by the Board of Trustees - August 13, 2000

Exhibit 1 Approved as revised by the Board of Trustees: May 21, 2004

Exhibit 1 Approved as revised by the Board of Trustees: February 11, 2005

Exhibit 1 Approved as revised by the Board of Trustees: February 9, 2006

Exhibit 1 Approved as revised by the Board of Trustees: September 6, 2007

Exhibit 1 Approved as revised by the Board of Trustees: September 5, 2008

Exhibit I Targets revised by Investment Subcommittee: January 27, 2009

Annual Review of the Debt Policy

The Committee performed an annual review of the University's debt policy. Chair McAneny had previously recommended an amendment that provides for the action to be taken should the University fall out of compliance with the debt policy. Because of the decline in the value of the endowment and the new requirement to include the future liability associated with post retirement medical benefits, the viability ratio as of June 30, 2009 is 0.48 rather than 0.80 as required by the policy. The Committee further recommended that "Budget, Finance, and Investment (BFI) Committee" be replaced throughout the document with a more generic committee reference, thus eliminating a policy revision should the committee structure change in the future. The Committee also directed that the sunset provision of the revised debt ratio be referenced in the policy. The Committee unanimously approved to reaffirm the current debt ratio standards and the proposed amendments to the Debt Policy (see Appendix A) for recommendation to the full Board.

Annual Review of Debt Policy

WHEREAS, in September 2004, the Board adopted a Debt Policy to guide the portfolio management of debt, which it updated most recently in December 2008; and

WHEREAS, the Debt Subcommittee of the Finance and Budget Committee was charged with the regular review of the Debt Policy;

NOW, THEREFORE, BE IT RESOLVED, that the Board hereby approves the modified Debt Policy as appended.

Approval of the FY 2011 State Capital Request

The FY 2011 State Capital Appropriation request was brought before the Committee for approval. Vice President Cate explained that the University chose 5.00% of the probable State Capital Bonding Authority in FY 2010 as its strategy for calculating the request for last fiscal year. If that strategy were followed for FY 2011 with the State Capital Bonding Authority at \$71.8 million, the University's request would be \$3.59 million. While still agreeing with this formula, but realizing the budget pressures facing the State this year, the administration is requesting that the Board adopt an FY 2011 state capital appropriation request in the amount of \$2.0 million. Vice President Cate affirmed that the appropriation request argues for the higher amount.

The resolution authorizing the President to submit the state capital appropriations for FY 2011 request to the Governor and Legislature of the State of Vermont was approved unanimously by the Committee for recommendation to the full Board.

State Capital Appropriation Request - Fiscal Year 2011

RESOLVED, that the President be and is hereby authorized to request \$2.0 million from the Governor and Legislature of the State of Vermont toward construction, renovation, and major facility maintenance in advancement of the mission of the University of Vermont.

Approval of Summer Session Tuition rates

The proposal for summer 2010 is to increase the per credit hour cost by 6.0% above summer 2009. This increase will continue the 15% differential between summer credit hour cost and the balance of the year. Vice President Cate noted that the University saw an increase in summer enrollment last summer, which may in part be due to the reduced tuition. The recommendation for summer 2010 is an increase of \$23 to \$414 per credit hour for Vermont students and \$59 to \$1,046 per credit hour for out-of-state students.

The Educational Policy & Institutional Resources (EPIR) Committee will be asked to authorize the administration to enter into an agreement to establish a U.S.-Sino Pathways Program (USPP) at the University of Vermont. Students will attend a summer session that will include academic offerings as well participation in courses designed to begin integrating them into the UVM community. A group of 40-60 Chinese students are anticipated. The BFI Committee was asked to consider a proposed USPP Bridge Program all-inclusive fee for summer 2010 (including tuition, room and board and student fees) of \$13,099.

The resolution to approve the recommended summer session tuition rates was approved unanimously by the Committee for recommendation to the full Board.

Summer Tuition Resolution

RESOLVED, that the Board of Trustees hereby approves the change in tuition for the Summer Session from \$391 to \$414 per credit hour for in-state students and from \$987 to \$1,046 per credit hour for out-of-state students. The changes will become effective for the 2010 Summer Session.

BE IT FURTHER RESOLVED, that the Board of Trustees hereby approves an all-inclusive fee for the US-Sino Pathway Program (USPP) Bridge Program for Summer 2010 of \$13,099, pending approval of that academic initiative via the Educational Policy and Institutional Resources Committee.

Budget Update

Vice President Cate reported on the challenges in the FY 2010 budget and the administration's decision to implement \$3 million in strategic budget cuts to offset the overage in the financial aid budget. A significant portion of that has already been identified, which may include more controlled management of vacant general fund positions by the Administration. Work is underway to address the remainder of the structural budget deficit as part of building the FY 2011 budget.

Vice President's Report

Vice President Cate gave a brief report on the following:

Negotiations for Facilities and Administrative Cost Recovery

Negotiations for facilities and administrative (F&A) rates are underway. The F&A is the overhead rate received on grants. This rate is used to reimburse grants and contracts for the indirect costs of sponsored programs.

FY 2009 Budget Close Out

The FY 2009 financial statement audit is in progress. A final report is forthcoming.

FY 2010 Budget to Actual Report – 1st Quarter Year to Date

A Budget to Actuals Report as of September 30, 2009 was provided to the Committee. The quarterly reports are certified by the President, Provost, Vice President Cate, and academic deans. Revenue and expenditures are currently on track for the year.

Student Housing

Vice President Cate informed the Committee that the planning phase of the third party housing project at Redstone has been delayed temporarily and will likely be reinitiated in January.

Adjournment

There being no further business, the meeting was adjourned at 12:39 p.m.

Respectfully submitted,

Robert Cioffi, Co-Vice Chair



University of Vermont
Debt Policy
As Adopted by the Board of Trustees
September 2004, revised. November 2005,
Revised, November 2006,
Revised, November 2007,
Reaffirmed, December 2008,
Revised, October 2009

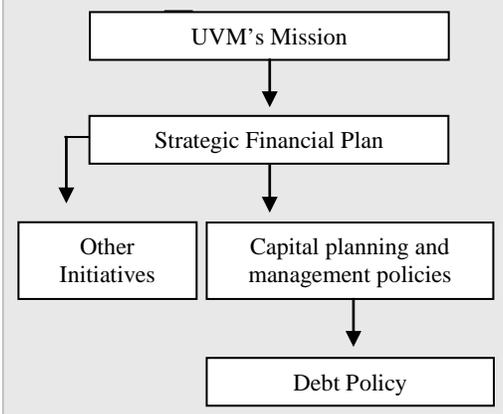
TABLE OF CONTENTS

Overview.....	1
Introduction and Objectives	2
Oversight.....	3
Policy Ratios.....	3
Types of Financings	5
Portfolio Management of Debt.....	7

OVERVIEW

Purpose

1. Articulate the role of UVM's debt policy within the strategic planning process.



The University of Vermont’s strategic planning is a long-term process that establishes University-wide priorities as well as University and divisional programmatic objectives to guide principles and practices. The University’s strategic plan identifies specific goals and initiatives, including capital plans that identify necessary and desired University facility investments. To fund its plan, the University will continue to utilize a mix of financing sources including State and Federal sources, philanthropy, internal reserves, and external University-supported debt.

As the University continues to balance the significant need for both current and future facilities investment, research, teaching, student, and other important needs and competing initiatives for capital from limited resources, the University is implementing this debt policy. This policy, in conjunction with the Strategic Financial Plan and capital planning, will aid management in ensuring that an appropriate mix and types of funding sources are utilized and that the University’s debt capacity is allocated strategically. A UVM-specific debt policy is appropriate to ensure adequate financial strength to service existing and proposed debt, maintain leverage within an acceptable risk tolerance while investing in priority capital projects, maintain a strong financial profile to ensure a competitive position relative to its peers, and maintain the budgetary capacity to invest in other initiatives. Additionally, this policy will provide the foundation for internal procedures to ensure that appropriate reporting and management requirements are in place in order to meet objectives outlined in this policy, and to provide a more efficient process for the ongoing external and internal management of debt in order to optimize its utilization on campus.

Management and the Board of Trustees, acting through the ~~Trustee Budget, Finance and Investment Committee~~ appropriate Board of Trustee committee, will assess this policy on an ongoing basis to ensure that it remains responsive to UVM’s evolving academic, research and strategic priorities and financial position. Additionally, a set of operating procedures will be established in order to implement the objectives set forth in this policy. The procedures will outline management roles and responsibilities including internal operating controls and fiduciary responsibilities consistent with the long-term objectives of this policy.

The University believes that financial discipline is a critical component of long-term debt management and that the Board and management, operating through the ~~Trustee Budget, Finance and Investment Committee~~ appropriate Board of Trustee committee should establish a limited number of financial ratios and limits in order to manage debt within acceptable ranges consistent with UVM’s objectives. These measures will be monitored and reported on in light of UVM’s evolving strategic initiatives and capital needs.



INTRODUCTION AND OBJECTIVES

Purpose

1. Articulate UVM's philosophy regarding debt.
2. Establish objectives for debt policy.
3. Provide for regular review and potential update of policy to reflect evolving needs.

Over time, appropriate financial leverage serves an important role in funding the University's capital investments and should be considered a long-term component of UVM's balance sheet. Just as investments represent an integral component of assets, debt is viewed to be a long-term component of liabilities that therefore should be managed on a long-term portfolio-basis consistent with the institution's policy objectives. Debt, especially tax-exempt debt, provides a limited low cost source of funding for capital projects in order to achieve the University's mission and strategic objectives, and, together with other limited resources, should be utilized and allocated appropriately, strategically, judiciously, and equitably.

This objectives of the policy are to:

- (i) Maintain the University's access to capital. Management will utilize and issue debt in order to provide timely access to capital to fund project priorities that have been approved by the Board;
- (ii) Manage the University's credit to meet its long-term strategic objectives while maintaining creditworthiness consistent with the most favorable relative cost of capital and borrowing terms. Maintaining the highest acceptable credit rating will permit the University to continue to issue debt and finance capital projects at favorable interest rates while meeting its strategic objectives;
- (iii) Limit risk of the University's debt portfolio. Debt will be managed on a portfolio, rather than a transactional or project-specific, basis. Management's continuing objective of incurring the lowest achievable long-term risk-adjusted cost of capital will be balanced with the goal of appropriately limiting exposure to market shifts within acceptable budgetary parameters. Various types of debt structures and financial instruments will be considered, monitored, and managed within the framework established in this policy and according to internal management procedures; and
- (iv) Permit the optimization of the investment of the University's working capital and cash balances. Management will explore various options and alternatives to internal cash holdings regarding the optimal funding mechanism for short-term equipment needs, bridge financing and cash requirements. Management recognizes that working capital requirements, debt management, and the investment of cash should be viewed comprehensively in order to optimize overall funding and investment return strategies.

In addition to establishing a framework relating to the administration of debt, the policy provides for periodic updates pertaining to UVM's debt capacity and financial management to both internal and external parties.



OVERSIGHT

Purpose

1. Provide mechanism for oversight and review on periodic basis.
2. Provide management flexibility to make ongoing financing decisions within the framework of the policy.

By adopting this policy and regularly reviewing its results and appropriateness with the ~~Trustee Budget, Finance and Investment Committee~~ appropriate Board of Trustee committee, management will follow and report on guidelines and requirements regarding debt utilization. With appropriate authorizations consistent with the policy, management will have flexibility to implement specific financial transactions and utilize approved financing vehicles (e.g. commercial paper) in accordance with stated procedures.

The Office of the Vice President for Finance and Administration and Treasurer will manage all funding sources, including debt, for capital projects authorized by the Board. The structure of any individual transaction (e.g., maturity, interest rate mode, use of derivative products, other financing structures) will be based upon overall University needs to ensure that (i) long-term costs to the University and its operating units are minimized consistent within the context of other strategic objectives and (ii) overall risk does not exceed acceptable levels as defined in this policy.

Because this debt policy is a living document, the ~~Trustee Budget, Finance and Investment Committee~~ appropriate Board of Trustee committee will review this policy on an annual basis and report any recommended changes or revisions to the Board of Trustees. This review process is necessary to ensure that the policy remains consistent with the University’s objectives and responsive to evolving practices, competitive pressures in the external environment, and financial indicators.

In addition, the ~~Trustee Budget, Finance and Investment Committee~~ appropriate Board of Trustee committee will hold regular meetings in order to review short and intermediate term financing needs, market opportunities, and financial performance. This regular review will help the University determine appropriate financial decisions as well as review capital investments and the timing of financing plans responsive to market conditions.

POLICY RATIOS

Purpose

1. Identify core ratios.
 - a. Operating Statement—Debt Burden Ratio.
 - b. Balance Sheet Leverage—Viability Ratio.
2. Clearly communicate with key parties such as rating agencies the University’s philosophy regarding debt and management’s ongoing assessment of debt capacity and affordability.

This policy establishes limits to measure the total amount of outstanding debt compared to University balance-sheet resources and the annual operating budget. These ratios can be derived from the financial statements and are subject to review periodically.

The policy identifies ratios that (i) are based on current GAAP requirements, including the GASB 34/35 reporting format and (ii) are consistent with ratios utilized in the higher education industry to permit benchmarking.

In addition to the two policy ratios below, the University may consider tracking other ratios in addition to the policy ratios. Listed below are the policy ratios and limits that will be followed.

Ratio 1 – Debt Burden Ratio

This ratio measures the University’s ability to repay debt service associated with all outstanding debt and the impact on the overall budget



and includes all activities of the University. The defined limit for this ratio is intended to maintain the University's long-term operating flexibility to fund existing requirements and new initiatives, although the University may target a desired ratio below this limit.

$$\frac{\text{ANNUAL DEBT SERVICE}}{\text{TOTAL EXPENSES}} < 6\% \text{ *}$$

The measure is based on aggregate operating expenses as opposed to operating revenues because expenses typically are more stable (e.g., no one-time operating gifts, investment return, variability of State funding) and better reflect the operating base of the University. Management recognizes that a growing expense base would make this ratio appear more attractive. The limit for this ratio is not to be greater than 6.0%. If more than 6.0% of the University's annual budget were committed to debt service expense, flexibility to devote resources to fund other objectives could be diminished. This ratio will be adjusted to include the impact of non-amortizing or non-traditional debt structures that could result in significant single year fluctuations, as well as an assumption of an appropriate variable rate.

**As adopted by the Board of Trustees, December 1, 2007:
"That the Board directs the Administration to develop and implement a plan to lower the debt burden ratio to 5% by 2017"*

Ratio 2 - Viability Ratio

This ratio indicates one of the most basic determinants of financial health by measuring the availability of liquid and expendable net assets compared to aggregate debt. The ratio measures the medium to long-term health of the University's balance sheet and debt capacity and is a critical component of universities with the highest credit quality.

Many factors influence the viability ratio, affecting both the assets (e.g., investment performance, philanthropy) and liabilities (e.g., timing of bond issues), and therefore the ratio is best examined in the context of changing market conditions so that it accurately reflects relative financial strength. For example, a viability ratio that is acceptable and entirely appropriate in one market condition may be relatively stronger or weaker in other market environments.

This policy establishes a debt policy limit (floor) for this ratio of 1.0x to ensure that sufficient balance sheet strength is maintained at all times.

$$\frac{\text{UNRESTRICTED NET ASSETS + TEMPORARILY RESTRICTED NET ASSETS - EQUITY IN PLANT}}{\text{AGGREGATE DEBT}} > 0.8x$$

This ratio will include any financings that impact the University credit, including guarantees of third-party debt.

The 0.8x limit is recognized as a limit, and not a long-term objective. Over time, to remain competitive and retain the flexibility to invest in future strategic initiatives, UVM will want to target and maintain a ratio above 0.8x

Annually, based on the results of the audited financial statements, the Vice



President for Finance and Administration will report to the Budget, Finance and Investment Committee appropriate Board of Trustee committee (BFI) on the actual ratio results and any existing conditions that put the University out of compliance with this policy. In the event that the University is out of compliance with the policy, the BFI appropriate Board of Trustee Committee will take up the matter for consideration and make what recommendations it deems appropriate to the Board of Trustees.

Ratios as a Credit Factor

The University has established its ratios and associated ratio limits based on internally-established guidelines. The ratios and limits are not intended to provide a long-term target or track a specific rating, but rather will enable the maintenance of the University’s competitive financial profile and complement the capital planning process.

The debt policy will be shared with external credit analysts and other third parties in order to provide them with the context regarding UVM’s assessment of self-determined debt capacity and affordability, which is subject to ongoing review.

TYPES OF FINANCINGS

Purpose
<ol style="list-style-type: none"> 1. Review of all potential funding sources for projects. 2. Maximize tax-exempt University-issued debt. 3. Commercial Paper program. <ol style="list-style-type: none"> a. Provide bridge funding. b. Provide continual access to capital. c. Issuance on a taxable or tax-exempt basis. 4. Manage derivative products, including swaps. 5. Consider other financing sources. <ol style="list-style-type: none"> a. Management will explore securitizations, joint ventures and other financial structures to provide for the optimal funding for any project.

The University recognizes that there are numerous types of financing structures and funding sources available, each with specific benefits, risks, and costs. All potential funding sources will be reviewed by management within the context of the debt policy and the overall portfolio to ensure that any financial product or structure is consistent with UVM’s objectives. Regardless of what financing structure(s) is(are) utilized, a full understanding of the transaction, including (i) quantification of potential risks and benefits, and (ii) analysis of the impact on University creditworthiness and debt capacity, will be required. Any financial transaction which, in management’s opinion utilizes the University’s credit, will be subject to the limits set forth in this policy regardless of source.

Tax-Exempt Debt

The University recognizes that debt will remain a long-term component of the University’s capitalization over the foreseeable future due in part to its continued need for capital and the substantial economic benefits associated with tax-exempt debt. Therefore, financial transactions will be managed on a portfolio basis with a long-term perspective. Management will manage the debt portfolio to maximize its utilization of tax-exempt debt relative to taxable debt whenever possible. (In all circumstances, however, individual projects must continue to be identified and tracked to ensure compliance with all tax and reimbursement requirements).

Recognizing the inherent benefit provided by tax-exempt borrowing, the University will prefer to consider maximizing the external maturity of any tax-exempt bond issue, subject to prevailing market conditions and opportunities, budgetary constraints, the useful life of projects being financed, and other considerations. Although debt will be structured to meet the University’s comprehensive long-term objectives, each project being financed will be required to provide a sound business plan, including the source of repayment for the debt and appropriate and realistic



repayment terms. Among other things, the repayment terms will require that the loan term is no greater than the expected componentized useful life of the asset financed. Additionally, the financed project will be required to budget and fund principal payments on a fully amortized basis.

Taxable Debt

While all of the University's capital projects may not qualify for tax-exempt debt, taxable debt should only be used in appropriate cases as it generally represents a more expensive source of capital relative to tax-exempt issuance. Issuing taxable debt reduces the University's overall debt affordability due to higher associated interest expense.

When utilized, taxable debt will be structured to provide maximum repayment flexibility and rapid external principal amortization.

Commercial Paper

The University is establishing a commercial paper program, which will include both a tax-exempt and taxable series. The CP program can provide substantial financial flexibility to the University including the ability to manage and optimize cash balances, provide an alternative to lease transactions, and other purposes. At this time, however, the University is limiting the use of the program to providing the University with interim financing for capital projects in anticipation of the receipt of funding either in the form of future philanthropy or the issuance of long-term debt for permanent financing, providing greater flexibility regarding the timing and structuring of individual bond transactions. It is expected that the University may consider expanding the permitted use of the CP program at some point in the future.

The University recognizes that the amount of project-related commercial paper is limited by the ratios established by this debt policy, and the University's available liquidity support however, the University will not include outstanding CP in the variable rate debts exposure, given the expected short-term nature of the CP. The existence and utilization of the commercial paper program has influenced the decision to limit variable rate exposure to no more than 35% of the long-term debt portfolio.

Derivative Products

Management recognizes that derivative products may enable more opportunistic and flexible management of the debt portfolio. Derivative products, including interest rate swaps, may be employed primarily to manage or hedge the University's interest rate exposure for a specific period of time. The University will utilize a framework to evaluate potential derivative instruments through consideration of (i) its variable rate allocation, (ii) market and interest rate conditions, (iii) impact on future financing flexibility, and (iv) the compensation for assuming risks, or the costs for eliminating certain risks and exposure. In addition, the University will analyze and quantify the cost/benefit of any derivative instrument relative to achieving desirable long-term capital structure objectives. Under no circumstances will a derivative transaction be utilized that is not understood fully by management or that imposes inappropriate risk on the University. Risks include but are not limited to tax risk, interest rate risk, liquidity risk, counterparty credit risk, basis risk, and any other potential risks either imposed or removed through the execution of any transaction. In addition, management will consider and



disclose the potential impact of any derivative product on the University’s financial statements and the appropriate treatment in calculating the debt policy ratios. The University will regularly report on the status and performance of its derivative products, if any, to the ~~Trustee Budget, Finance and Investment Committee~~ appropriate Board of Trustee committee.

Given the risks and complexity associated with derivative products, they will be considered more seriously only when: (i) conventional financing sources are relatively more expensive (e.g. exceed the portfolio blended interest rate, and (ii) can achieve desired financial objectives more efficiently or at a significantly lower risk-adjusted cost than traditional structures. Management is required to present any recommended derivative product to the ~~Trustee Budget, Finance and Investment Committee~~ appropriate Board of Trustee committee and must receive ~~the Subcommittee’s recommendation and~~ Board approval prior to execution.

Other Financing Sources

The University recognizes that a variety of transactions, not limited to debt insured directly by UVM, may impact the University’s credit while the University’s limited debt capacity and substantial capital needs require the consideration of various financing alternatives, including possible opportunities for alternative and non-traditional transaction structures., . The University recognizes these types of transactions may also impact the University’s credit and also often can be more expensive than traditional University debt structures.

Therefore all non-traditional financing structures including guarantees and third party debt can only be considered once the economic benefit and the likely impact on the University’s debt capacity and credit has been determined. Specifically, for any third-party or developer based financing, management will ensure the full credit impact of the structure is evaluated and quantified to the extent possible prior to execution and the analysis must be presented to the ~~Trustee Budget, Finance and Investment Committee~~ appropriate Board of Trustee committees and must receive ~~and must receive the Subcommittee’s recommendation and~~ Board approval prior to execution.

PORTFOLIO MANAGEMENT OF DEBT

Purpose
<ol style="list-style-type: none"> 1. Permit decisions regarding debt issuance and structure to be made on a portfolio basis, rather than on a per-project basis. 2. Manage variable rate exposure of the debt portfolio. <ol style="list-style-type: none"> a. Limit variable rate exposure. b. Manage the overall liquidity requirements associated with outstanding debt. c. Target overall variable rate debt exposure. 3. Evaluate exposure to other financing vehicles and third parties on a portfolio-wide basis.

The University considers its debt portfolio holistically; that is, it optimizes the portfolio of debt for the entire University rather than on a project-by-project basis, and takes into account the University’s cash and investments. Therefore, management will make decisions regarding project prioritization, variable rate allocation, and financing structures within the context of the overall needs and circumstances of the University.

Variable Rate Debt

It is recognized that a degree of exposure to variable interest rates within the University’s debt portfolio may be desirable in order to:

- (i) take advantage of repayment/restructuring flexibility;



- (ii) benefit from historically lower average interest costs; and
- (iii) diversify the debt portfolio; and,
- (iv) provide a hedge to short-term working capital balances

Management will monitor overall interest rate exposure, analyze and quantify potential risks, and coordinate appropriate fixed/variable allocation strategies. The portfolio allocation to variable rate debt may be managed or adjusted through (i) the issuance of debt (potentially new issues and refunding), (ii) and the use of interest rate swaps and other derivative products. While the utilization of commercial paper impacts the University's variable rate exposure, outstanding CP will not be included in the ratio, given the expected interim financing purpose.

Recognizing the desire to manage interest rate risk, the amount of variable rate debt outstanding shall not exceed 35% of the University's outstanding debt. This limit is based on (i) the University's desire to limit annual variances in its debt portfolio, (ii) provide sufficient structuring flexibility to management, (iii) keep the University's variable rate allocation within acceptable external parameters, (iv) utilize variable rate debt (and/or swaps) to optimize debt portfolio allocation and minimize costs, and (v) consideration of the commercial paper program.

$$\frac{\text{VARIABLE RATE AND LIQUIDITY EXPOSURE}}{\text{TOTAL LONG-TERM DEBT OUTSTANDING}} < 35\%$$

The University will exclude from this calculation project-related commercial paper used in advance of expected long-term financing since this commercial paper is used for interim purposes and should not be included in the University's desired long-term variable rate allocation calculation. The numerator, *Variable Rate and Liquidity Exposure*, is defined as including all variable rate debt, not adjusted for any floating to fixed swaps, if any, and plus any fixed to floating swaps, if any. Thus, any variable rate debt that is affected by floating-to-fixed interest rate swaps will be considered variable rate debt for the purposes of this calculation since it impacts the University's liquidity requirements and exposes the institution to counterparty credit exposure.

Overall Exposure

The University recognizes that it may be exposed to short-term interest rates, third-party credit, and other potential risks in areas other than direct University debt (e.g., non-traditional transactions, exposure in the investment portfolio, etc.) and, therefore, exposure will be considered on a comprehensive University-wide basis.

The University recognizes that during some periods it may be desirable to maintain a lower variable-rate allocation within its 35% limit, depending on prevailing long-term rates and/or opportunities in the short-term market.



GLOSSARY

Annual Debt Service – refers to the principal and interest due on long-term debt in a fiscal year.

Bridge Financing – refers to any type of financing used to “bridge” a period of time. For universities, it generally refers to financings that provide funding in advance of a long-term bond issue or the receipt of gift funding.

Capital Project – refers to physical facilities or equipment or software that may be capitalized.

Commercial Paper – an alternative to bank line for stronger rated borrowers, commercial paper is short-term promissory notes issued on the open market as an obligation of the borrower. The maturity of commercial paper is less than 270 days, and for most universities, the average maturity of all paper is between 30-50 days. Registration and disclosure for commercial paper is significantly less than traditional university bonds.

Derivative Products – generally referred to transactions which are an exchange of specified cash flows for a period of time. The most common types of derivatives are floating-rate-to-fixed-rate or fixed-rate-to-floating-rate swaps.

GAAP – refers to Generally Accepted Accounting Principles.

GASB 34/35 – Government Accounting Standards Board Statement Nos. 34 and 35. These statements dramatically changed the reporting format for the University effective Fiscal 2002 by consolidating fund balances into net assets and consolidating university-wide activity instead of distinct fund groups. The Statements also require a statement of cash flows and a change in representation of state appropriation and investment income.

Leverage – long-term debt as a component of the total assets of the University. “High leverage” indicates an institution that has a considerable portion of its assets that are debt financed.

