

**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 29, 2010 at 1:30 p.m., in the Silver Maple Ballroom, 401 Dudley H. Davis Center.

**MEMBERS PRESENT:** Chair Debbie McAneny, Vice Chair Samuel Bain, Bill Botzow, Ian Boyce, Carolyn Branagan, David Daigle, Daniel Fogel, Brian Sozansky, Donna Sweaney, and Mark Young

**REPRESENTATIVES PRESENT:** Faculty Representative Albert Joy, Alumni Representatives Walt Blasberg and Meg Guzewicz, Staff Representatives Kit Ardell and Rodman Cory, Student Representatives David Maciewicz and Alex Mallea, and Graduate Student Representatives Eric Garza and Eduardo Cotilla-Sanchez

**OTHER TRUSTEES PRESENT:** Board Chair Robert Cioffi

**PERSONS ALSO PARTICIPATING:** Vice President for Finance and Administration Richard Cate, Associate Vice President for Budget and Resource Management Ted Winfield, and Controller Claire Burlingham

**ABSENT:** Trustee Susan Hudson-Wilson and Faculty Representative Donald Ross

Chair Debbie McAneny called the meeting to order at 1:35 p.m.

**Approval of Minutes**

A motion was made, seconded and voted to approve the minutes of the May 21, 2010 meeting.

**Ten-Year Budget Forecast**

Chair McAneny stated that today's meeting would open discussions on FY 2012 budget planning that would continue at February's meeting. No action would be taken. Vice President Cate led the discussion of the ten-year budget forecast. The Committee was provided with three ten-year budget projections. The alternative projections illustrate the effects of a 3.0%, 4.5%, and 6.0% tuition increase combined with conservative assumptions for expenditure increases over the next decade. He reminded the Committee that 6.0% was the ten-year tuition projection in the latest version of the Strategic Financial Plan.

The Committee discussed challenges in projecting and managing financial aid expenditures. This includes finding the balance between the financial aid necessary to build quality and diversity in a class while staying within a predictable and acceptable budget level. Chair McAneny commented that while she understood the economic downturn resulted in increases in financial aid need, she questioned the forecast's continual growth of the expense given signs of

an economic recovery. She requested a detailed analysis of historical financial aid spending as well as the underlying assumptions of the ten-year projections, which Vice President Cate agreed to provide. He explained that the growth in financial aid was projected at 1.5% above the tuition rate increase in the forecast. The reason financial aid grows faster than the tuition increase is that the departing senior class has fewer students and receives less financial aid per capita than the incoming class. The goal is to slow the growth in financial aid expense while keeping pace with tuition. Trustee Botzow asked if there were predictors to student aid behavior and volatility. Vice President Cate replied that the University employs Noel Levitz, an enrollment management consulting firm, to predict financial aid expense against the quality and diversity of the incoming class. He offered to have Noel Levitz staff attend the next meeting for this review. President Fogel commented that the University's behavior was similar to other institutions as indicated by the College Board. He added that financial aid is awarded based on need and merit and that factors other than economics influence student behavior. Trustee Branagan asked that a detailed analysis of graduate student aid spending be provided along with undergraduate.

Vice President Cate reviewed other revenue and expense items contained in the forecast. The State appropriation is forecasted to grow 2% annually after 2012, which he indicated might be too optimistic given the State's budgetary challenges. He referred the Committee to the base budget fund balance line on the forecast. The projection reflected the inflated cost of continuing all current activities with no significant changes. The negative fund balance grows each year in the model with the 3% tuition increase; with the 4.5% increase the negative balance declines and then becomes positive in FY 2016; and the 6% increase results in a positive fund balance beginning in FY 2013. Listed below the base budget fund balance are additional investments in academic initiatives, debt service, and facilities maintenance and IT infrastructure. The analysis of the University's facilities consultant, Sightlines, indicates that the current deferred maintenance backlog is approximately \$250 million. Spending of approximately \$18 million per year on deferred maintenance is necessary to prevent the backlog from growing even larger. The forecast indicates a slow progression to achieve the \$18 million level.

Trustee Bain questioned the modest growth forecasted on state appropriation and other revenue items. Vice President Cate responded that there was no basis to grow revenue at a higher rate at this time. President Fogel added that the University had taken a conservative approach and reiterated that the current projections might be too optimistic. Additional investments in key areas such as academic initiatives and debt service provide some indication of the types of budget choices to be made. The debt service line illustrates the potential impact of issuing \$75 million in bonds for capital projects in FY 2014 and again in FY 2018. Vice President Cate noted that the amounts shown were not sufficient to fund all initiatives but were stated with an attempt to stay within current debt ratio limits.

The Committee shared their thoughts and reactions to the data presented. Several members commented that the financial aid data requested would affect the tuition recommendation. Trustee Daigle suggested that the necessary growth in investment for facilities maintenance and IT infrastructure be built into the base operating budget. Trustee Botzow asked for the overriding risks with the different tuition levels presented. Vice President Cate replied that he did not believe the University could sustain operations with a 3.0% increase. With a 6.0% increase the University runs the risk of pricing itself out of the market over time. The challenge

with a 4.5% increase is whether it would generate sufficient resources to grow the quality of the student experience in order to remain competitive. Vice Chair Bain praised the work that the Committee was doing in reviewing the elements of the budget in greater detail. Chair McAneny closed with a few words on the September Board of Trustees retreat. She stated that there was unanimous agreement by the Board that investment in quality is where focus needed to be.

### **Report of the Investment Subcommittee**

Samuel Bain, Chair of the Investment Subcommittee, began by crediting the efforts and talents of Investment Subcommittee members Ian Boyce, David Daigle, and Susan Wilson-Hudson. He then led the Committee through a discussion of Long-Term Investment Pool allocations and performance through August 31, 2010, and preliminary results through September quarter-end. The August month end Long Term Pool market value was \$293 million and the overall return of the pool for the month was -1.8%. Chair Bain noted that the endowment was up 6% at the end of September with an aggregate market value approximating \$311 million. September was the strongest positive month for the global equity markets in about 70 years.

Since the last Budget, Finance and Investment (BFI) Committee meeting, the Subcommittee reengaged Cambridge Associates as the University investment advisor for a very competitive fee after an extensive RFP process that included interviewing other finalists. At the July 2010 meeting in New York, the Subcommittee met with four existing managers, which included hedge fund managers.

The Subcommittee has been busy rewriting the Investment Policy that will be brought forward February 2011. The plan is to grow the endowment and keep up with inflation.

The Committee developed a watch list to monitor managers who are under and over performing. Chair Bain reported that the Subcommittee made a few changes in managers since the May board meeting, with full redemption from SSgA's fixed income fund in favor of Vanguard. The University has increased its position in BlackRock's All Cap Energy fund, and with Mondrian.

### **Annual Approval of the Endowment Budget Policy**

Trustee Bain led a brief discussion surrounding the reaffirmation of the Endowment Budget Policy. The University uses a 13 quarter trailing average market value at a 4.5% spending rate. Cambridge Associates provided information to the Subcommittee they have not seen a change in rates amongst our peers and that the majority is in the 4-5 % range. Out of 138 universities, 72 spend 4.0-4.9% annually. Chair Bain commented that the Committee is very comfortable with the 4.5% rate. Trustee Branagan asked what the University spends the money on. Vice President Cate responded that the vast majority is used for restricted purposes in accordance with donor specifications. The Subcommittee agreed to continue to monitor the spending rate in relation to the rate of return on the investments. Trustee Bain presented the Resolution Reaffirming the Endowment Budget Policy.

**Resolution Reaffirming the Endowment Budget Policy**

RESOLVED, that the *Endowment Budget Policy* is reaffirmed as reads below:

BE IT RESOLVED, that the annual budget for spending from Endowment be set at 4.5 percent of the average market value 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 Budget Policy* each year no later than October 31.

*Adopted by:* Board of Trustees - May 13, 1995  
*Reaffirmed:* Board of Trustees - September 8, 2007  
Board of Trustees - September 5, 2008  
Board of Trustees - October 24, 2009  
Board of Trustees –

The Committee unanimously approved the Resolution Reaffirming the Endowment Budget Policy for recommendation to the full Board.

**Annual Approval of Endowment Administration Fee Policy**

Trustee Bain reviewed the rationale for the Administration fee which was set at 25 basis points by the Investment Subcommittee in October 2009 and approved again in August 2010. The fee was reduced in October 2009 from 50 basis points. The University's investment advisors provided information that most fees run 10-50 basis points and that UVM is using an appropriate amount. Trustee Bain commented that the Endowment Administrative fees go directly to the general fund to support the salaries of those who work on endowment related activities. After a fair amount of deliberation, the Committee felt comfortable with the fee basis point set at 25. Trustee Bain presented the Resolution Reaffirming the Endowment Administration Fee Policy.

**Resolution Reaffirming Endowment Administration Fee Policy**

RESOLVED, that the *Endowment Administration Fee Policy* is reaffirmed as reads below:

BE IT RESOLVED, that the Board of Trustees hereby approves a 0.25 percent fee applied to the University endowment for FY 2012 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 reviewed and assessed annually as 0.25 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 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  
*Reaffirmed:* Board of Trustees -

The Resolution Reaffirming Endowment Administration Fee Policy was approved unanimously by the Committee for recommendation to the full Board.

### Annual Asset Reallocation Review

Trustee Bain briefly discussed the Subcommittee’s ongoing review of asset allocation targets in the Long-Term Pool. He noted that the asset allocation is within approved ranges. Not only is the Long Term Pool diversified by asset class, but the managers within the asset classes are also diversified. The next annual review of asset allocation meeting of the ISC is scheduled for January.

### University of Vermont Long Term Pool Target Asset Allocation As of August 31, 2010

Asset Class	Manager Allocation	Target Allocation	Allowable Range
U.S. Equity	24.6%	25.0%	15%-30%
Global ex U.S. Equity	24.0%	25.0%	15%-45%
Developed Markets	13.8%	14.0%	10%-25%
Emerging Markets	10.2%	11.0%	5%-20%
Marketable Alternatives	18.4%	17.5%	15%-25%
Real Assets (Inflation Hedging)	11.8%	12.5%	10%-25%
Venture Capital/Private Equity	9.8%	10.0%	5%-20%
Bonds	8.6%	8.0%	5%-25%
Cash and Cash Equivalents	2.7%	2.0%	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*  
*Exhibit I Targets revised by Investment Subcommittee: January 13, 2010*

## **Socially Responsible Investing Work Group Update**

Trustee Bain invited Work Group Leader and University Controller, Claire Burlingham, to give a brief update on the activities of the SRIWG. Controller Burlingham reported that the SRIWG is focused on reviewing and revising its procedures and protocols. The focus of their last two SRIWG meetings was on the development of a list of tasks that comprise its work plan for the fall 2010 semester. The SRIWG has developed a work plan for fall 2010 that includes the following tasks: to define the purpose of the Work Group; to restructure the Call for Issues process; to create a plan for the solicitation of Public Comment on proposals under consideration by the work group; to establish a protocol for ownership of the proposals should the original sponsor no longer be affiliated with the university; to develop a Conflict of Interest statement for members of the SRIWG; to establish clear procedures and guidelines and criteria for the evaluation of proposals; to improve education of work group members and proposers; and to establish a communication plan and outreach protocols.

The Work Group received materials from a presentation given by Dr. Stephanie Kaza, faculty representative to the SRIWG, regarding the STARS rating system, hosted through the Association for the Advancement of Sustainability in Higher Education (AASHE). This organization evaluates a University's sustainability rating. Categories for gaining points are: Education & Research; Operations; Planning, Administration and Engagement; and Investment. According to information received, the University is already accumulating credits and should have a STARS rating in a couple of years.

To date, three proposals have been submitted in response to the fall 2010 call for proposals, with the understanding that the Working Group would not be reviewing them until the spring given the fall work plan. Controller Burlingham informed the Committee that there will be a second call for proposals in January. Two proposals carried forward from spring 2010 will be addressed in spring 2011. The first is a proposal on the divestment from Israel, which is a continuation of a proposal submitted in the previous year. The second concerns divestment from companies involved with gene patenting.

## **Debt Policy & Ratio Annual Review**

The Committee conducted an annual review of the University's debt policy. The administration recommended a reaffirmation of the current ratios and editing of the policy to streamline and update some language within it. The substance of the policy is unchanged. A short discussion took place on the Commercial Paper (CP) section. The Committee decided to retain the second paragraph of the CP section, which was originally slated for deletion.

The Committee was provided with a history of existing debt ratio results with and without the impact of GASB 45, the University's post-retirement liability. While the viability ratio continues to demonstrate that the University is out of compliance with policy limits, the ratio has improved over FY 2009 results. The Debt Burden ratio remains within the policy limits. Controller Burlingham noted that the FY 2010 ratios were based on unaudited financial results and may improve slightly with the audited results. Peer comparison data compiled on recent debt ratio history was also provided. Trustee Daigle asked what impact, if any, being out of

compliance had on the rating agencies. Vice President Cate replied that agencies were allowing the industry time to take actions to mitigate this liability. The situation is being monitored but no action has been taken by the rating agencies at this time.

Chair McAneny presented the following resolution for approval:

**Annual Review of Debt Policy**

WHEREAS, in September 2004 the Board adopted a Debt Policy to guide the portfolio management of debt, to be reviewed annually; and

WHEREAS, since its creation in 2006, the Budget, Finance, and Investment Committee has been charged with the annual review of the Debt Policy, which it revised most recently in October 2009;

NOW, THEREFORE, BE IT RESOLVED, that the Board hereby reaffirms the current ratios and approves recommended edits to streamline and update language within the Debt Policy, appearing as appended in Attachment A.

The Committee voted unanimously to approve the resolution for recommendation to the full Board with the request that the second paragraph of the CP section be retained in the Debt Policy.

**Approval of Summer Session Tuition Rates**

Associate Vice President Winfield introduced the proposal for summer 2011 tuition rates. The recommendation is to increase the per credit hour cost by 4.0% above summer 2010. This increase will continue the 15% differential between summer credit hour cost and the balance of the year. The recommendation for Summer Session (summer 2011) is an increase of \$17 (+4%) to \$431 per credit hour for in-state students and \$42 (+4%) to \$1,088 per credit hour for out-of-state students.

Last year, the Educational Policy & Institutional Resources (EPIR) Committee authorized the administration to enter into an agreement to establish a U.S.-Sino Pathways Program (USPP) at the University of Vermont. All US-Sino Pathways Program students will attend a summer session to complete their preparation for studies in the U.S. Trustee Botzow asked what the University's position was on the program given that enrollment numbers were less than anticipated. Board Vice Chair Harry L. Chen responded to the question, saying that the EPIR Committee had recommended that participation in the program continue for one more year.

The BFI Committee was asked to consider the proposed USPP Bridge Program all-inclusive fee for summer 2011 (including tuition, room and board and student fees) of \$15,250.

The following resolution was presented for approval:

**Summer Tuition Resolution**

RESOLVED, that the Board of Trustees hereby approves the change in tuition for the Summer Session from \$414 to \$431 per credit hour for in-state students and from \$1046 to \$1088 per credit hour for out-of-state students. The changes will become effective for the 2011 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 2011 of \$15,250, pending re-approval of that academic initiative via the Educational Policy and Institutional Resources Committee.

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

**Approval of Reallocation of Existing Capital Project Funds**

Vice President Cate brought forward a proposal to reallocate \$1,000,000 of unused Jeffords Hall project funds for the purpose of addressing deferred maintenance at Waterman and Billings. The amount identified for reallocation is a combination of the unused contingency of the project and projected savings from the original estimate.

The following resolution was presented:

**Reallocation of Existing Capital Project Funds Resolution**

WHEREAS, the University wishes to manage its debt in the most cost-effective way in accordance with its Board-adopted Debt Policy; and

WHEREAS, in September 2007, the Board of Trustees authorized funds totaling \$55,700,000 for the construction of the Jeffords Hall capital project; and

WHEREAS, the Jeffords Hall project has been completed to a level whereby a balance of funds will not be expended; and

WHEREAS, in May 2010, the Board of Trustees authorized the reallocation of \$1,500,000 to support deferred maintenance projects; and

WHEREAS, the University now wishes to authorize an additional expenditure of \$1,000,000 from the Jeffords Hall project towards priority deferred maintenance projects,

NOW, THEREFORE, BE IT RESOLVED, that the Vice President for Finance and Administration and University Treasurer, or his successor or designee, is hereby authorized



to reallocate \$1,000,000 from the Jeffords Hall project to finance priority deferred maintenance projects, and

BE IT FINALLY RESOLVED, that the Secretary or Assistant Secretary will provide certificates of incumbency, as required, showing the names and signatures of those people appointed to any of the positions heretofore mentioned, and further, that any officer of this corporation is hereby authorized to certify this resolution to whom it may concern.

The resolution to approve the recommended Reallocation of Existing Capital Project Funds Resolution was approved unanimously by the Committee for recommendation to the full Board.

### **Vice President's Report**

The Committee was provided with a FY 2011 budget to actual report as of September 30, 2010. Overall revenue is tracking at or above budget; expenditures are tracking in line with budget.

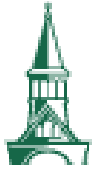
KPMG completed their field work on the FY 2010 financial statements the week of September 25<sup>th</sup> and found no issues that would rise to the level of material weaknesses or significant deficiencies. KPMG's opinion is expected to be issued by November 1st, and will reflect that the University's financial statements, as prepared by management, fairly represent the financial position of the University as of June 30, 2010. KPMG's final audited financial statements are to be presented at Audit Committee's December 15<sup>th</sup> meeting and at the February Committee of the Whole meeting.

### **Adjournment**

There being no further business, the meeting adjourned at 3:55 p.m.

Respectfully Submitted,

Debbie McAneny, 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  
Revised, October 2010

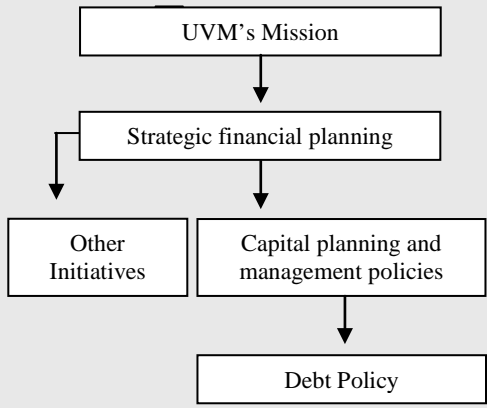
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**OVERVIEW**

**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 ~~S~~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 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 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, with an overarching objective of managing the balance sheet. ~~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/net assets 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 ~~it—its results and appropriateness~~ with the 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 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 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 other information 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.

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

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 (also called Expendable Financial Assets to Debt)

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

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 d~~Debt will be structured to meet the University’s comprehensive long-term objectives, and 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, and 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 CP can offer~~ 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 as well as offer 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 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 appropriate Board of Trustee committee and must receive 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 appropriate Board of Trustee committees and must receive Board approval prior to execution.

**PORTFOLIO MANAGEMENT OF DEBT**

**Purpose**

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.
  - 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 (i) 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) take into account liquidity needs and exposures for the portfolio, including 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. Note that this ratio measures interest rate exposure and liquidity exposure/requirements directly.

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.

