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UNIVERSITY OF TORONTO

UNIVERSITY FUNDS INVESTMENT POLICY

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1. DESCRIPTION OF UNIVERSITY FUNDS

1.1. Long-Term Capital Appreciation Pool (LTCAP)

The LTCAP, formerly known as the Consolidated Investment Pool (CIP), consists of the university's endowed trust funds or other funds of a permanent or long-term nature. In addition, external funds may be invested in the LTCAP including funds of affiliated organizations and funds where the university is a beneficiary.

1.2. Expendable Funds Investment Pool (EFIP)

The EFIP consists of expendable funds, which are pooled for investment purposes until the funds are required for expenditure.

1.3. Specifically Invested Trust Funds

The specifically invested trust funds consist of both endowed and expendable funds which cannot be pooled for investment purposes because of constraints or conditions attached to the funds.

2. LONG-TERM CAPITAL APPRECIATION POOL (LTCAP)

2.1. General Description of the Fund and Governance

The LTCAP represents the pooling of invested assets accumulated by or donated to the University for endowed purposes.

The Governing Council has delegated management of the LTCAP assets to the University of Toronto Asset Management Corporation in accordance with the Service Agreement dated May 1, 2000 between The Governing Council and the University of Toronto Asset Management Corporation (UTAM). The investment decisions of UTAM and its Board of Directors are subject to the overall policy direction of the Business Board as reflected in this policy and in amendments the Board may make from time to time.

3. THE NATURE OF LTCAP LIABILITIES

The LTCAP provides funding to the faculties and departments of the university to be used for endowed purposes in accordance with the terms of each endowment or trust. The LTCAP is subject to the capital preservation policy currently in place and as may be amended from time to time, and as such the distribution and reinvestment rates must be harmonized on an inflation-adjusted basis.

4. INVESTMENT POLICIES AND GOALS OF LTCAP

4.1. Investment Policy, Objectives and Risk Tolerance

The University of Toronto has engaged the University of Toronto Asset Management Corporation (UTAM) to manage the LTCAP. As a client of UTAM, it is important that the University delivers to its fund manager a concise statement of return objectives as well as risk tolerance, and that these two components are congruous. The purpose of this policy is to establish both of these objectives with regard to the Long-Term Capital Appreciation Pool (LTCAP).

The purpose of the LTCAP is to provide cash flows that will grow each year at a minimum of the rate of inflation in order to preserve the purchasing power of the fund and provide the same or better level of support for future generations. This necessitates a balance between the desire to reward unit holders in the present and a long-term view toward developing a sustained or increasing contribution from endowed assets. In addition, the University's Policy for the Preservation of Capital of Endowment Funds identifies the following:

a) The need to maintain the inflation-adjusted value of endowment capital; and

b) The need to provide a stable flow of expendable income for the purposes of each fund.

4.2. Return Expectations and Risk Tolerance

In order to meet the planned payouts, the return objective is a 4.0% real, inflation-adjusted return over a 10-year period. This return objective is net of all fees and levies. For purposes of this return objective, the level of University levies should be set at 0.4% to 0.5% of assets.

To keep risk at a reasonable level, UTAM shall manage the asset portfolio to achieve a target standard deviation of 10.0% or less in nominal terms over 10 year periods.

4.3. Asset Mix

UTAM shall establish the asset mix investment mandates and then select investment managers to be responsible for the management of the portfolios in accordance with those mandates. Funds will normally be allocated to external managers in accordance with those mandates. Funds will normally be allocated to external managers, or when determined to be advantageous, may be allocated to internal management.

Performance benchmarks against market indices and peer universes will be established for the fund. The details of these benchmarks will be described in the service agreement between the University and UTAM. Portfolio diversification, categories and subcategories of investments, use of derivatives, and investment restrictions will be accountabilities of UTAM and a requirement that UTAM develop, approve and review these policies will be incorporated into the service agreement between the University and UTAM.

Each investment manager shall adhere to this policy and shall follow the investment policies and goals with the care, diligence and skill that a person of ordinary prudence would use in dealing with the property of another and shall use all relevant knowledge and skill that the investment manager possesses or ought to possess. Investment managers are expected to be in compliance with the standards of professional conduct and code of ethics established by the CFA Institute.

5. INVESTMENT POLICIES AND GOALS OF EFIP

5.1. Investment Policy, Objectives, Risk Tolerance, Asset Mix and Performance Benchmarks:

The expendable funds investment pool (EFIP) contains expendable funds that are pooled and invested until spent. It includes the University's cash for operations, capital projects, ancillary operations, expendable donations, expendable payouts from endowments and research grants. It excludes endowments funds and the supplemental retirement arrangement, which are part of the long term capital appreciation pool (LTCAP).

The size of EFIP varies over the course of a year. Its average cash balance for 2003-04 was about $400 million, ranging from a low of $264 million in July 2003 to a high of $535 million in January 2004. Multi-year analysis of actual cash inflows and outflows shows that the University's outflows generally doe not exceed inflows by more than about $50 million in a particular month. Even with a margin of safety, this historical data would suggest that we need to keep only about $75 million on average in short term investments and that the remainder of EFIP can be invested for medium and longer periods of time.

Taking account of the overall fluctuation in the size of EFIP over the course of each year and historical analysis of EFIP cash balances over several years, the maximum amount that can be invested longer term is $200 million.

The current strategy is that EFIP will provide all short-term construction financing and up to $200 million in long-term loans for internal purposes, predominantly capital infrastructure, which generates predictable investment returns for EFIP. (If the funds invested by EFIP in these long term loans were needed for short-term expenditures, the borrowing would have to be re-financed externally).

There are, therefore, three investment strategies for EFIP: the short-term portion (estimated to be up to about $75 million) to be held in cash and cash-like investments; the long-term portion of up to $200 million to be held in internal loans to the University; and the remaining balance, which fluctuates over the course of each year, to be invested by UTAM.

A projection of cash flow patterns and balances for the next 10 years, suggests that the average 10-year capital for these categories would increase well above the $400 million average recorded for 2003-04 and would be approximately as follows:

Assets managed by U of T	$ 75.0 million
Internal loans	$156.5 million
Assets managed by UTAM	$329.8 million
	$561.3 million

The return objective, risk tolerance and performance benchmark for each category of EFIP funds is as follows:

	Return Objective	Risk Tolerance	Asset Mix	Performance Benchmark
Assets managed by U of T.	30 day T-bill return	Minimal Risk	University shall establish investment mandate and select investment vehicles. Assets normally held in bank accounts or short-term institutional money market pooled funds.	N/A
Internal loans	Appropriate spread over	Minimal Risk	University to issue internal loans using EFIP funds, or using	N/A

	Government of Canada bonds of similar duration		externally borrowed funds, at discretion of Chief Financial Officer.	
Assets managed by UTAM	1 Year T-bill return plus 0.5%	Minimal Risk (standard deviation not appropriate for short duration).	UTAM shall establish the asset mix investment mandates and then select investment managers to be responsible for the portfolios in accordance with those mandates. Funds will normally be allocated to external managers in accordance with those mandates, or when determined to be advantageous, may be allocated to UTAM's internal management.	Performance benchmarks will be established for funds managed by UTAM. The details of those benchmarks are part of the service agreement between UTAM and U of T.

5.2 Additional accountabilities of UTAM:

For EFIP funds managed by UTAM, portfolio diversification, categories and subcategories of investments and investment restrictions will be accountabilities of UTAM and a requirement that UTAM develop, approve and review these policies is a part of the service agreement between the University and UTAM.

Each investment manager shall adhere to this policy and shall follow the investment policies and goals with the care, diligence and skill that a person of ordinary prudence would use in dealing with the property of another and shall use all relevant knowledge and skill that that the investment manager possesses or ought to possess. Investment managers are expected to be in compliance with the standards of professional conduct and code of ethics established by the CFA Institute.

6. SPECIFICALLY INVESTED TRUST FUNDS

The assets of Specifically Invested Trust Funds shall be invested to achieve the maximum total rate of return through a combination of capital appreciation and current income consistent with any liquidity or other constraint specified and subject to any consultation required by contractual agreement, or by condition of the estate, or administrative arrangement.

7. GENERAL

7.1. Conflict of Interest Guidelines

Anyone involved directly or indirectly with the University's fund investments shall immediately disclose, at the time of its discussion of the policy or of matters related to the investment of University funds, any actual or perceived conflict of interest that could be reasonably expected to impair, or could be reasonably interpreted as impairing, his/her ability to render unbiased and objective advice to fulfill his/her fiduciary responsibility to act in the best interests of the funds.

7.2. Custody

Custody requirements will be an accountability of UTAM and a requirement that UTAM develop, approve and review these requirements will be incorporated into the service agreement between the University and UTAM.

7.3. Policy Review

This statement shall be reviewed at least once a year and either confirmed or amended as necessary.

Catherine Riggall
Vice-President, Business Affairs
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