University of Toronto TORONTO ONTARIO M5S 1A1

(ORIGINATING OFFICE)

TO: Business Board

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DATE: June 13, 2007 for June 21, 2007

AGENDA ITEM: 7 (b)

ITEM IDENTIFICATION:

University Funds Investment Policy

JURISDICTIONAL INFORMATION:

The Business Board is responsible for:

- The review and approval from time to time of the investment policies for university investment funds and amendments thereto, such policy to include, without limitation: normal asset mixes, asset-mix ranges, risk tolerances, quality criteria, and rate of return objectives including benchmarks for each fund.
- The approval of the conditions for the delegation of authority to a University-controlled asset management corporation of the management of the investment of university funds.

PREVIOUS ACTION TAKEN:

The University Funds Investment Policy was last approved by the Business Board at its meeting of March 27, 2007.

HIGHLIGHTS:

The University Funds Investment Policy provides investment direction from the University to the University of Toronto Asset Management Corporation (UTAM) with respect to the long-term capital appreciation pool (LTCAP, the expendable funds investment pool (EFIP), and specifically invested funds. The policy is reviewed annually and either confirmed or amended as necessary.

During 2006-07, the EFIP investment risk and return targets were reviewed and the LTCAP investment risk and return targets will be reviewed during 2007-08.

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LTCAP – SECTION 4 OF THE POLICY:

LTCAP consists of the University's endowed funds, and a few other funds of a long-term or permanent nature such as the supplemental retirement arrangement. Investment returns generated through investments of these funds support payouts to faculties and divisions for expenditures in accordance with the terms and conditions of individual endowments and other funds.

Section 4.2 specifies a return objective of a 4.0% real return and a risk tolerance of 10% in nominal terms, net of all fees and levies. These targets were established in 2003. At this time, no change is recommended to these targets.

During 2007-08 we will be conducting a review of the LTCAP investment risk and return targets.

EFIP – SECTION 5 OF THE POLICY:

The expendable funds investment pool contains expendable funds which 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.

EFIP includes three categories of funds: very short-term funds that are managed within the University in cash and cash-like investments, longer term assets that are invested in internal loans in support of capital projects, and longer term assets that are managed by UTAM.

The investment risk and return targets that are currently in place were established in 2005. The University has reviewed the EFIP risk and return targets to assess whether they continue to be appropriate. An asset/liability study has been completed for us by Hewitt Associates. Since this represents the University's cash pool, every year we want no shortfalls and positive cash flows. Therefore, the University has a minimal risk requirement to avoid investment losses that would have to be repaid from the operating fund. This means that higher risk strategies, such as those involving equities, were not considered.

Based on the results of that study we are comfortable that the current risk and return targets continue to be appropriate, and no changes are recommended to the EFIP risk and return targets.

POLICY REVIEW:

Section 7.3 of the policy dated March 27, 2006 provided in clause 7.3 that "this statement shall be reviewed at least once a year and either confirmed or amended as necessary". While the statement will continue to be reviewed by the administration on a regular basis, it will only be brought to the Business Board for consideration if changes are proposed. Therefore, this requirement for annual confirmation has been removed from the policy.

FINANCIAL AND/OR PLANNING IMPLICATIONS:

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RECOMMENDATION:

THAT the proposed *University Funds Investment Policy* dated June 21, 2007 be approved, replacing the *Policy* approved by the Business Board on March 27, 2006.

Attachment 1
June 21, 2007

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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 no more than 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).

EFIP has three categories of investments: very short-term funds that are held and managed within the University in cash and cash-like investments, longer term assets that are invested in internal loans in support of capital projects, and longer term assets that are managed by UTAM.

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 Government of Canada bonds of similar duration	Minimal Risk	University to issue internal loans using EFIP funds, or using externally borrowed funds, at discretion of Chief Financial Officer.	N/A
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 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.

Catherine Riggall
Vice-President, Business Affairs
June 21, 2007