UNIVERSITY OF TORONTO

Borrowing Strategy

Review
January 2011

Courtesy of Cicada Design Inc. & Kuwabara Payne McKenna Blumberg Architects

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University of Toronto
Borrowing at a Glance to January 31, 2011
(in Millions of dollars)

Maximum borrowing capacity:	
External	771.5
Internal	200.0
	971.5
Borrowing allocated:	
Total allocated	(962.6)
Minus repayment eligible for reallocation	68.5
	(894.1)
Unallocated to January 31, 2011	77.4
Actual outstanding external borrowing:	
Series A debenture due July 18, 2031	160.0
Series B debenture due December 15, 2043	200.0
Series C debenture due November 16, 2045	75.0
Series D debenture due December 13, 2046	75.0
Borrowing prior to 2001 net of repayments	14.6
Loan from City of Toronto	1.3
	525.9
Actual outstanding internal borrowing to January 31, 2011	214.4 *
Total actual outstanding borrowing to January 31, 2011	740.3

* internal borrowing is greater than $200 million maximum target because internal funds are providing short to medium-term bridge-financing until the University issues the next debenture of up to $200 million.

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PURPOSE OF REPORT

The purpose of this report is to review the borrowing strategy that was approved by the Business Board on June 17, 2004 to assess:

- Is the current strategy financially prudent?
- Are any additional parameters needed to ensure that it continues to be financially prudent?
- Does it continue to provide sufficient borrowing capacity to meet carefully reviewed priorities?

The borrowing strategy was last reviewed on February 8, 2010.

CURRENT BORROWING STRATEGY

The current borrowing strategy is to borrow both internally from the expendable funds investment pool (EFIP), and externally from third parties. The key elements of the current strategy are:

- Maximum external borrowing capacity equals 40% of net assets averaged over 5 years.
- In the event that outstanding external borrowing exceeds 40% of net assets averaged over 5 years, no further borrowing is permitted until such time as the actual outstanding external borrowing is not greater than 33% of net assets averaged over 5 years.
- Maximum internal borrowing capacity is $200 million loaned from EFIP and excludes internal financing of fund deficits and short-term construction financing of capital projects.
- In the event that the funds invested by EFIP were needed for short-term expenditures, the borrowing would have to be re-financed externally.
- An internal financing program.
- An internal sinking fund to accumulate funds for repayment of debentures.
- No credit rating parameters.
- No external borrowing debt service or debt repayment parameters.

CURRENT STATUS

Maximum borrowing capacity:

The maximum external borrowing capacity is updated annually every April 30. At April 30, 2010, the maximum external borrowing capacity was $771.5 million.

The utilization of up to $200 million of internal borrowing from EFIP is also reassessed annually. At April 30, 2010, it was confirmed that $200 million can continue to be allocated to internal borrowing.

Therefore, maximum external plus internal borrowing capacity was set at $971.5 million, effective April 30, 2010.

Borrowing allocated to capital projects and other requirements:

At January 31, 2011, the Business Board has allocated $962.6 million to capital projects and other requirements. With $68.5 million repayments that can be reallocated, this leaves $77.4 million to be allocated to future projects, at this time.

Actual borrowing:

At April 30, 2010 there was $525.9 million in outstanding external long-term debt, comprised as follows:

$ 14.6 million borrowing prior to 2001(excluding $7.1 million to be repaid during 10-11)
$ 1.3 million loan from City of Toronto (excluding $0.1 million to be repaid during 10-11)
$160.0 million Series A debenture
$200.0 million Series B debenture
$ 75.0 million Series C debenture
$ 75.0 million Series D debenture
$525.9 million

As of January 31, 2011, there is $525.9 million in outstanding external long-term debt. This represents 27.3% of net assets averaged over 5 years or 29.2% of net assets as at April 30, 2010. In January 2009, the Business Board approved an additional $200 million of external borrowing, which has not been issued to date.

Additionally, at January 31, 2011, outstanding internal long-term borrowing from EFIP was $214.4 million. Outstanding borrowing from EFIP is higher than the $200 million target, because we have temporarily used EFIP funding to finance loans that will eventually be assigned to our next debenture issue. This short-term bridging gives the University flexibility to find an opportune timing for the next external financing and will enable us to choose a desired timing for adding external debt to the balance sheet.

BENCHMARKING

To assess the financial prudence of the current borrowing strategy, we have compared a number of balance sheet and income statement ratios for the University of Toronto to other universities.

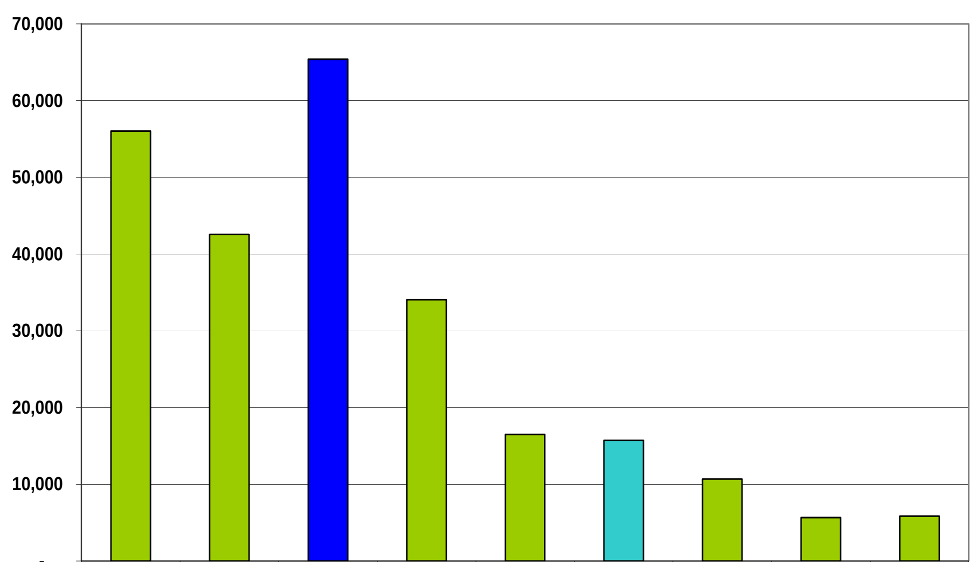
The benchmarks that have been used as comparators are from Moody's Fiscal Year 2009 U.S. Public College and University Medians issued in July 2010. Moody's currently rates "220 public universities on an underlying basis, with over $100.9 billion debt outstanding"[1].

Moody's credit ratings applied to U.S. public colleges and universities in descending order are Aaa, Aa1, Aa2, Aa3, A1, A2, and A3.

The University of Toronto was ranked Aa1, with a stable outlook, by Moody's in its most recent review.

Moody's publishes many ratios for public colleges and universities. We have selected several ratios and have compared University of Toronto to other universities with similar ratings. The chart shows that universities with larger numbers of students tend to be in the higher rating categories.

Larger Universities in Higher Rating Categories (Moody's Medians)
Plus University of Toronto



	Aaa	Aa1	Toronto Aa1	Aa2	Aa3	All Public medians	A1	A2	A3
2009 FTEs	56,046	42,553	65,402	34,060	16,507	15,736	10,713	5,674	5,857

[1] Moody's Fiscal Year 2010 Public College and University Medians (p. 2).

Here are the comparators in the Aaa, Aa1 and Aa2 categories:

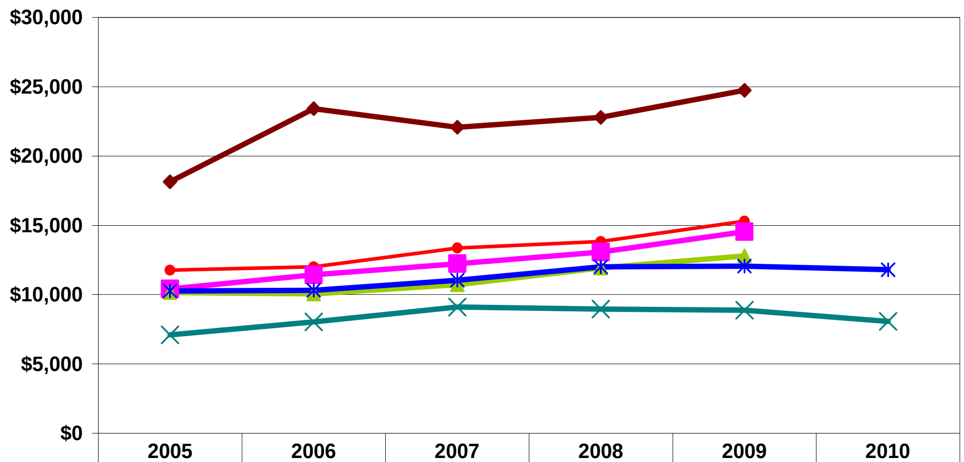
Aaa	
Indiana University	University of North Carolina at Chapel Hill
Purdue University	University of Texas System
Texas A&M University System	University of Virginia
University of Michigan	University of Washington
Aa1	
Michigan State University	University of Minnesota
New Mexico Military Institute	University of Missouri System
North Carolina State University at Raleigh	University of Nebraska
Ohio State University	University of Pittsburgh
Pennsylvania State University	University System of Maryland
State University of Iowa	Virginia Polytechnic Inst. & State University
University of California	Tennessee State School Bond Authority
University of Kansas	**University of Toronto**
Aa2	
Auburn University	University of Arizona
Board of Regents	University of Arkansas
California State University	University of Colorado
Clemson University	University of Connecticut
East Carolina University	University of Florida
Florida State University	University of Georgia
Iowa State University of Science and Technology	University of Hawaii
Massachusetts State College Building Authority	University of Houston System
Minnesota State Colleges $ Universities	University of Illinois
Mississippi Inst. of Higher Learning	University of Kentucky
Nevada System of Higher Education	University of Louisville
New Mexico State University	University of Massachusetts
Rutgers, The State of New Jersey	University of New Mexico
State System of Higher Education	University of North Texas System
State University of New York	University of South Carolina
State University System of Florida	University of South Florida
Texas State University System	University of Utah
Texas State University System	University of Wyoming
University of Alabama at Birmingham	Virginia Commonwealth University
University of Alabama	Washington State University
Kansas State University	Wayne State University
University of Alaska	Appalachian State University

Direct Debt per Student:

Moody's compares the direct debt to the size of the student body. Direct debt is defined as the legal obligations of the institution, e.g. bonds, notes, commercial paper, capital leases, bank loans and draws upon lines of credit. The size of the student body is the FTE (full-time equivalent enrolment).

The chart below illustrates that U of T's direct debt per student is well below the medians. The maximum external borrowing capacity is very much in line with the medians for the Aa2 and Aa3 comparators and well below the median for the Aaa/Aa1 group. This means that U of T has borrowed less to date and has set a maximum external borrowing capacity to date per student that is less than the actual outstanding external borrowing of its rating peers.

Direct Debt per Student
Comparing University of Toronto to Moody's Medians for
Aaa, Aa1, Aa2 and Aa3

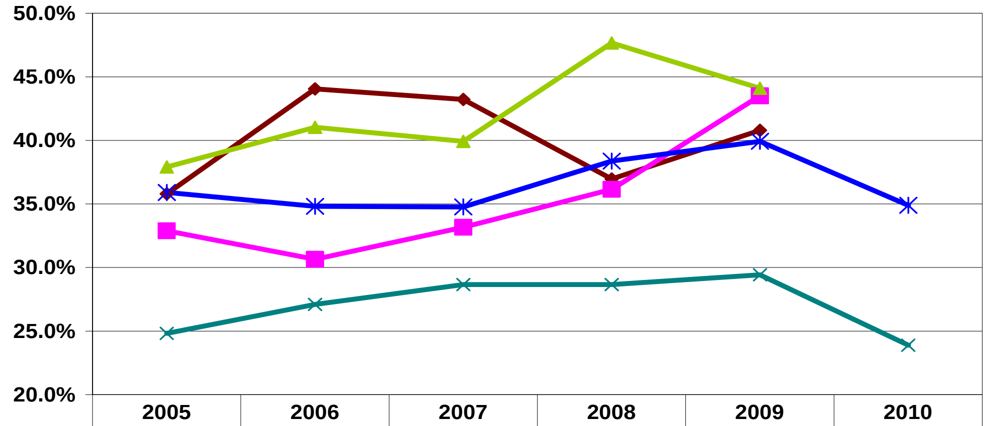


	2005	2006	2007	2008	2009	2010
Aaa direct debt per student	18,140	23,416	22,079	22,787	24,733	
Aa1 direct debt per student	11,759	12,002	13,360	13,834	15,295	
Aa2 direct debt per student	10,404	11,428	12,236	13,078	14,548	
Aa3 direct debt per student	10,149	10,050	10,714	11,930	12,798	
U of T direct debt per student	7,093	8,034	9,095	8,963	8,881	8,076
U of T max debt capapcity per student	10,260	10,318	11,031	12,006	12,051	11,796

Direct Debt to Total Revenues:

This Moody's ratio compares direct debt and the annual revenues of the institution. Direct debt is as defined above. Total revenues are the total revenues of the institutions.

Direct Debt to Total Revenues
Comparing University of Toronto to Moody's Medians for Aaa/Aa1, Aa2 and Aa3



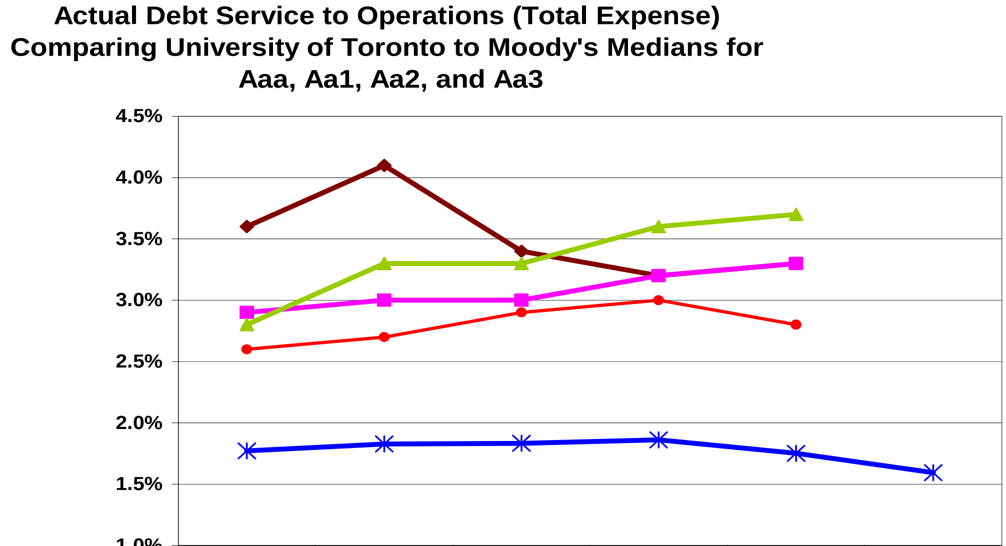
	2005	2006	2007	2008	2009	2010
Aaa/Aa1 direct debt/rev	35.8%	44.1%	43.2%	37.0%	40.8%	
Aa2 direct debt/rev	32.9%	30.6%	33.2%	36.2%	43.5%	
Aa3 direct debt/rev	37.9%	41.0%	39.9%	47.7%	44.1%	
U of T direct debt/rev	24.8%	27.1%	28.7%	28.7%	29.4%	23.9%
U of T max external debt capacity/rev	35.9%	34.8%	34.8%	38.4%	39.9%	34.9%

The chart illustrates that U of T's actual direct debt to revenues is well below the median while the maximum debt capacity is comparable to the current medians for its rating peers. This means that U of T has a better ratio of direct debt to revenues than its peers and that its external borrowing capacity to total revenues would be within the range of that of its rating peers.

Debt Service to Operations:

This Moody's ratio measures the debt service burden on expenses. Debt service is defined as the actual direct interest expense. Total expense is the total expenses as stated in the audited financial statements excluding student aid.

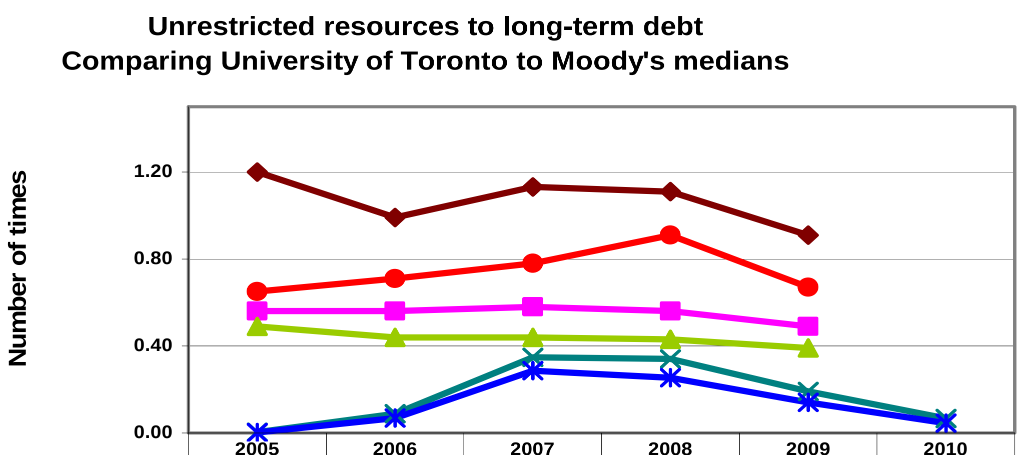
The chart below illustrates that U of T's ratio of direct debt service to operations was 1.6% at April 30, 2010, well below the medians for its rating comparators. This means that the U of T interest expense as a percentage of total operations was much less than its rating peers.



	2005	2006	2007	2008	2009	2010
Aaa actual debt service to operations	3.6%	4.1%	3.4%	3.2%	3.3%	
Aa1 actual debt service to operations	2.6%	2.7%	2.9%	3.0%	2.8%	
Aa2 actual debt service to operations	2.9%	3.0%	3.0%	3.2%	3.3%	
Aa3 actual debt service to operations	2.8%	3.3%	3.3%	3.6%	3.7%	
U of T actual debt service to operations	1.8%	1.8%	1.8%	1.9%	1.8%	1.6%

Unrestricted Resources to Long-Term Debt:

This Moody's ratio measures the coverage of direct debt by the most liquid resources, which it defines as unrestricted net assets.



	2005	2006	2007	2008	2009	2010
Aaa unrest. resources to debt	1.20	0.99	1.13	1.11	0.91	
Aa1 unrest. resources to debt	0.65	0.71	0.78	0.91	0.67	
Aa2 unrest. resources to debt	0.56	0.56	0.58	0.56	0.49	
Aa3 unrest. resources to debt	0.49	0.44	0.44	0.43	0.39	
U of T's unrestricted resources to debt	0.00	0.09	0.35	0.34	0.19	0.07
U of T's unrestricted resources to debt capacity	0.00	0.07	0.29	0.25	0.14	0.05

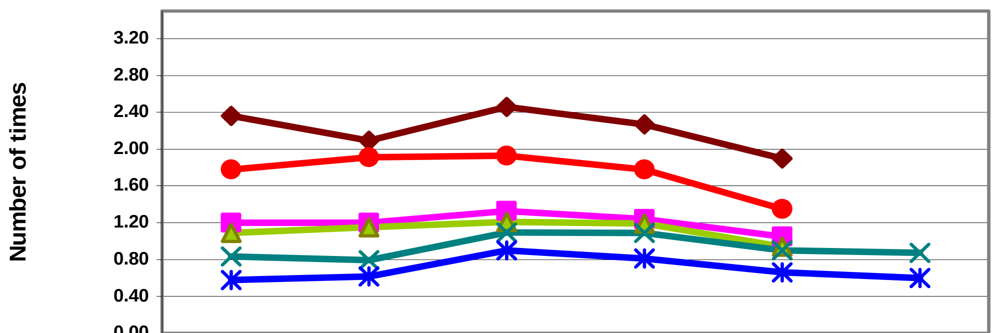
The chart illustrates that U of T's unrestricted resources to long-term debt ratio of 0.07 is well below the medians for its rating comparators. This means that U of T has fewer unrestricted resources to support long-term debt than its rating peers.

Expendable Resources to Long-Term Debt:

This Moody's ratio measures the coverage of direct debt by financial resources that are ultimately expendable, which it defines as the sum of unrestricted net assets plus restricted expendable net assets.

The chart below illustrates that U of T's expendable resources to long-term debt ratio of 0.9 is well below the medians for its rating peers. This means that U of T has fewer expendable resources to support long-term debt than its rating peers.

Expendable Resources to Long-Term Debt
Comparing University of Toronto to Moody's medians

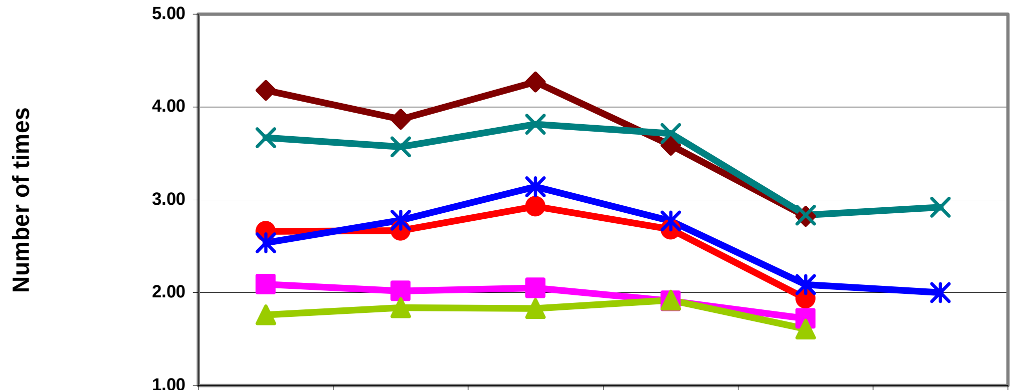


	2005	2006	2007	2008	2009	2010
Aaa expen. resources to debt	2.36	2.09	2.46	2.27	1.90	
Aa1 expen. resources to debt	1.78	1.91	1.93	1.78	1.35	
Aa2 expen. resources to debt	1.20	1.20	1.33	1.24	1.05	
Aa3 expen. resources to debt	1.09	1.15	1.21	1.19	0.94	
U of T's expendable resources to debt	0.83	0.79	1.09	1.09	0.90	0.87
U of T's expendable resources to debt capacity	0.58	0.62	0.90	0.81	0.66	0.60

Total Resources to Long-Term Debt:

This Moody's ratio measures the coverage of direct debt by total financial resources including permanent endowments.

Total Resources to Long-Term Debt
Comparing University of Toronto to Moody's medians



	2005	2006	2007	2008	2009	2010
Aaa total resources to debt	4.18	3.87	4.27	3.59	2.82	
Aa1 total resources to debt	2.66	2.67	2.93	2.68	1.94	
Aa2 total resources to debt	2.09	2.02	2.05	1.91	1.72	
Aa3 total resources to debt	1.76	1.84	1.83	1.92	1.61	
U of T's total resources to debt	3.67	3.57	3.81	3.71	2.83	2.92
U of T's total resources to debt capacity	2.54	2.78	3.14	2.77	2.09	2.00

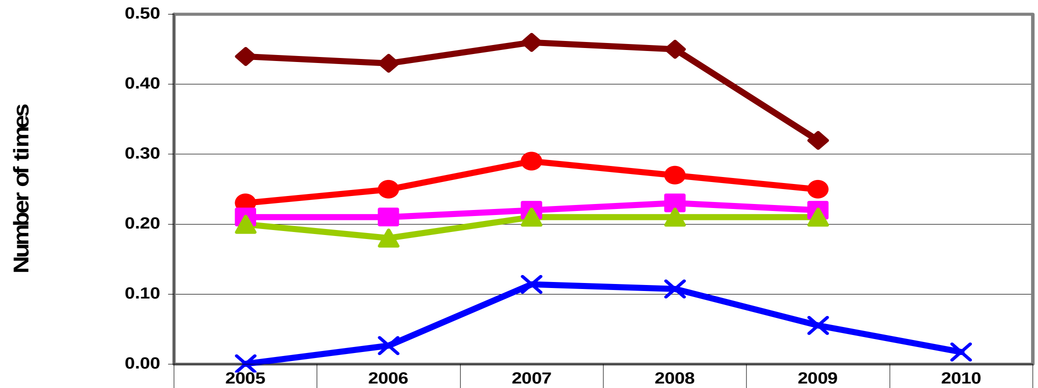
U of T’s total resources to long-term debt ratio of 2.92 is within the range of medians for its rating peers. This means that U of T has similar levels of total resources to support long-term debt as its rating peers.

Unrestricted Resources to Expenses:

This Moody’s ratio measures the coverage of annual expenses by the most liquid resources, the unrestricted net assets.

The chart illustrates that U of T’s ratio of 0.02 is well below its rating peers. This means that U of T has fewer unrestricted resources in comparison to its annual expenses than its rating peers.

Unrestricted Resources to Expenses
Comparing University of Toronto to Moody's medians

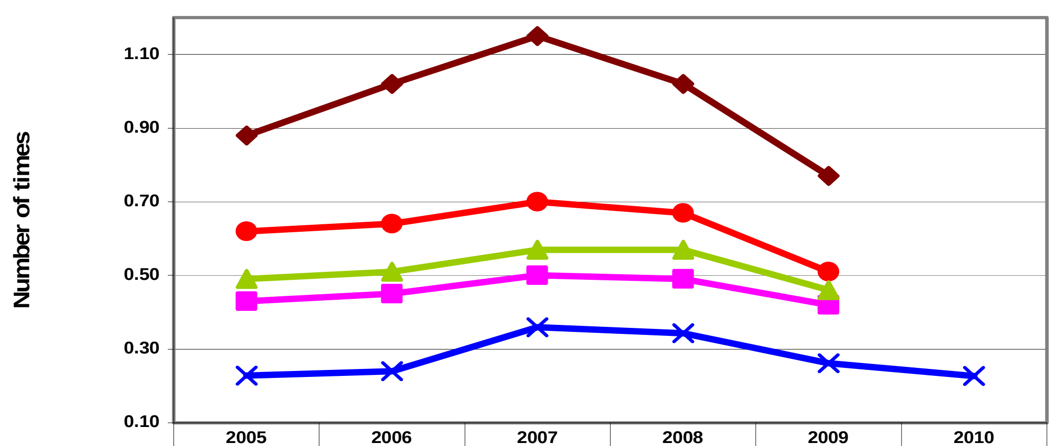


	2005	2006	2007	2008	2009	2010
Aaa unrest. resources to expenses	0.44	0.43	0.46	0.45	0.32	
Aa1 unrest. resources to expenses	0.23	0.25	0.29	0.27	0.25	
Aa2 unrest. resources to expenses	0.21	0.21	0.22	0.23	0.22	
Aa3 unrest. resources to expenses	0.20	0.18	0.21	0.21	0.21	
U of T's unrestricted resources to expenses	0.00	0.03	0.11	0.11	0.06	0.02

Expendable Resources to Expenses:

This Moody’s ratio measures coverage of annual expenses by financial resources that are ultimately expendable, defined as unrestricted net assets plus restricted expendable net assets.

Expendable resources to expenses
Comparing University of Toronto to Moody's medians



	2005	2006	2007	2008	2009	2010
Aaa expen. resources to expenses	0.88	1.02	1.15	1.02	0.77	
Aa1 expen. resources to expenses	0.62	0.64	0.70	0.67	0.51	
Aa2 expen. resources to expenses	0.43	0.45	0.50	0.49	0.42	
Aa3 expen. resources to expenses	0.49	0.51	0.57	0.57	0.46	
U of T's expendable resources to expenses	0.23	0.24	0.36	0.34	0.26	0.23

This chart illustrates that the U of T ratio of 0.23 is well below that of its rating peers. This means that U of T has fewer expendable resources in comparison to its annual expenses than its rating peers.

What do these comparisons tell us?

+ Debt per student is below medians
+ Debt to total revenue is below medians
+ Actual debt service to expenses is below medians
+ Total resources to long-term debt is within range of medians
- Unrestricted resources and expendable resources to long-term debt are below medians
- Unrestricted resources and expendable resources to expenses are below medians

In summary, we have borrowed externally less than our rating peers to date, but we also have fewer resources to support debt issuance and we have internal debt.

Those ratios, where it was possible to test maximum borrowing capacity also indicate that the maximum borrowing capacity to date is within the appropriate range as compared to our rating peers.

PROJECTING MAXIMUM BORROWING CAPACITY

The University performed the following steps to project maximum borrowing capacity under the current borrowing strategy:

- Projected net assets to 2015.
- Calculated projected maximum external borrowing capacity as 40% of net assets averaged over 5 years.
- Assessed continued ability to provide $200 million internal borrowing from EFIP.

Projecting Net Assets

Net assets increase due to:

1) net income mainly in operating and restricted funds, defined as revenues minus expenses for the year, and
2) growth in endowments from endowed donations and grants and from net reinvested investment earnings, offset by
3) change in the fair value of interest rate swap contracts.

At April 30, 2010, actual net assets were $1.8 billion. By 2015, net assets are projected to be between $1.7 billion and $2.2 billion, using the following assumptions:

- Long range operating budget to 2015, reflecting the draft pension funding and financing strategy presented to the Business Board, together with projected increases in pension and other employee future benefits. Pension expense which is determined based on accounting rules, is calculated on an actuarial basis and reflects the cost of providing one year of pension service. The increase in pension expense is mainly caused by the amortization of some of the 2009 investment losses incurred on the pension assets and the reduction in the discount rate required to be used to calculate the value of pension liabilities. For more information on pensions, please see the paper *Ensuring a Sustainable Pension Plan for the University of Toronto* (January 31, 2011 Business Board).
- Divisional carry forwards are projected to increase by $20 million in 2011, remain without change in 2012 and increase by $3 million from 2013 to 2015.
- Preliminary ancillary budgets submitted to SARG to 2015.
- Investment return on endowments and other long-term funds is forecasted to be 5% for 2011.

- No additional net losses for the capital fund, assuming that transfers from operating fund will offset.
- Endowed donations of $26 million in 2011, increasing to $35 million in 2012 and progressively increasing to $52.2 million by 2015.
- Endowed grants of $4.1 million per year.
- Endowment payout increases by 2% inflation annually from $7.26 per unit in 2009-10.
- A variety of endowment return assumptions from years 2012 to 2015: 6%, 10%, and 12%. These returns represent ten-year average returns of 4.3%, 5.8% and 6.5% respectively from fiscal years 2005 to 2015. A model using returns of 9% for 2012, 15% for 2013, 6% for 2014 and 12% for 2015 has been made to show some variability. These variable returns represent a ten-year average return of 6% from 2005 to 2015.

Projecting borrowing capacity:

At April 30, 2010 the maximum external and internal borrowing capacity was $971.5 million. The projected net assets of between $1.7 billion and $2.2 billion by 2015 would result in a projected maximum external borrowing capacity of between $694.3 million and $783.1 million by 2015.

We have thoroughly reviewed the University's cash flow requirements to confirm that the currently-assigned $200 million internal borrowing capacity can be maintained over the longer term and to assess whether additional funds could be invested by EFIP in long-term loans to the University to provide additional borrowing capacity.

This review has confirmed that the $200 million from EFIP can be continued and should not need to be replaced with comparable external borrowing during the period, that that increasing the limit temporarily beyond the $200 million target in the short-to-medium term is not expected to result in any risk of cash flow shortages.

This review has also indicated that there is significant additional cash available in EFIP that would support up to an additional $150 million of longer term investments by EFIP at a higher rate of return, with impairing cash flows.

While one option would be to increase the general internal maximum borrowing capacity from $200 million to $350 million, we believe that it makes more sense to:

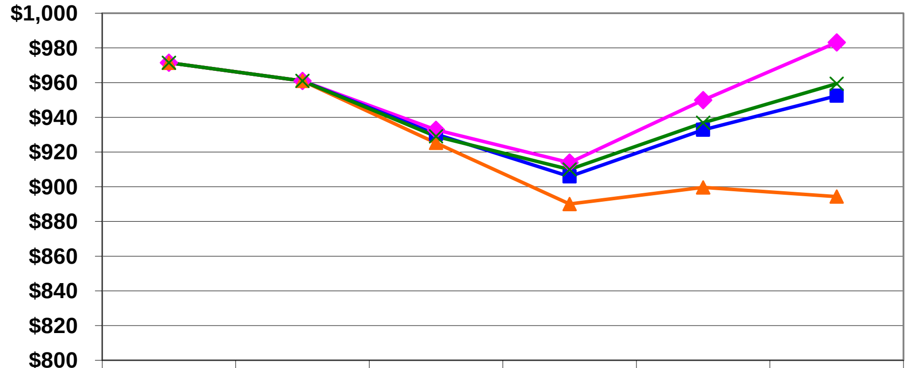
- maintain the current $200 million long term internal borrowing capacity under the current borrowing strategy, with the temporary overage as indicated above; and
- designate this additional $150 million as a pension borrowing capacity, separate and apart from the $200 million internal borrowing capacity, to support the borrowing requirement identified for pensions as discussed in the paper *Ensuring a Sustainable Pension Plan for the University of Toronto* (January 31, 2011 Business Board).

This approach would ensure that the additional amount identified would be reserved for pension purposes. It is also important to keep this pension borrowing capacity, and the actual associated borrowing, separate from the borrowing for predominantly capital purposes, because of the different impact on the University's balance sheet. While internal borrowing of funds for deposit into the pension plan reduces investments in the same way as borrowing for other purposes, it also reduces accrued pension liabilities by the same amount.

All amounts designated as borrowing capacity under both the current borrowing strategy and under this new pension borrowing capacity will continue to be assessed in determining the overall prudence of the University's overall borrowing. The utilization of the $150 million pension borrowing capacity will be reported separately from the maximum internal and external borrowing capacity under the current borrowing strategy to ensure that a clear line is maintained between borrowing for pension purposes and for other, predominantly capital, purposes. As with the existing $200 million internal borrowing capacity, if this additional $150 million invested by EFIP were needed for short-term expenditures, the borrowing would have to be re-financed externally.

Therefore, the remainder of this analysis will focus on the maximum external borrowing capacity plus the $200 million maximum internal borrowing capacity which is projected to be between $894.3 million and $983.1 million by 2015, as shown in the chart below, and excluding the additional $150 million reserved for pension purposes.

Projected Maximum External Borrowing at 40% Net Assets Smoothed over 5 Years Plus $200 Million internal Borrowing from EFIP, at various Endowment Return Assumptions (millions of dollars)



	2010 Actual	2011 Forecast (5%)	2012 Projection	2013 Projection	2014 Projection	2015 Projection
12% (average 6.5% 2005 to 2015)	971.5	961.0	932.8	914.0	950.0	983.1
10% (average 5.8% 2005 to 2015)	971.5	961.0	930.3	905.9	932.8	952.5
6% (average 4.3% 2005 to 2015)	971.5	961.0	925.3	890.1	899.6	894.3
2012:9%, 2013:15%, 2014:6%, 2015:12% (average 6% 2005 to 2015)	971.5	961.0	929.0	910.0	936.8	959.4

The table below summarizes the maximum borrowing capacity projected in January 2010 as compared to the projections in the current review, excluding the $150 million reserved for pension purposes:

Projected maximum total borrowing capacity ranges (in millions)

	January 2010 Review		January 2011 Review	
	LOW	HIGH	LOW	HIGH
April 30, 2010	958.5	958.5	971.5	971.5
April 30, 2011	943.6	956.8	961.0	961.0
April 30, 2012	907.8	942.1	925.3	932.8
April 30, 2013	874.5	944.9	890.1	914.0
April 30, 2014	886.8	1,009.2	899.6	950.0
April 30, 2015			894.3	983.1

The actual maximum borrowing capacity for 2010 is higher than the amount previously projected due to higher than expected return of the LTCAP (14.7% actual compared to expected 8%). However, the current projected maximum borrowing capacity for the outer years are lower than previously projected in January 2010 mainly due to the projected increases in pension and other employee future benefit expense.

Pension expense which is determined based on accounting rules, is calculated on an actuarial basis and reflects the cost of providing one year of pension service. The increase in pension expense is mainly caused by the amortization of some of the 2009 investment losses incurred on the pension assets and the reduction in the discount rate required to be used to calculate the value of pension liabilities. For more information on pensions, please see the paper *Ensuring a Sustainable Pension Plan for the University of Toronto* (January 31, 2011 Business Board). Obviously, an increase in interest rates would reduce these expenses and improve these projected figures. Better investment returns would also improve these projections.

Additionally, bank loans issued prior to 2001 are almost all amortizing loans, with principal being repaid to lenders each year. Similarly the internal loans from EFIP will decline over time as principal is repaid. External debenture borrowing is all repaid at maturity with no intervening principal repayments. The principal repayments from bank loans and EFIP loans provide another $140.1 million in loan potential by 2015.

Therefore, assuming that the projections of net assets are reasonable, we would expect to have available between $894.3 million and $983.1 million in borrowing capacity by 2015, excluding the additional $150 million reserved for pension purposes. The current borrowing allocated to projects and other requirements by Business Board to January 31, 2011 is $962.6 million. With the additional $140.1 million in principal repayments on amortizing loans, the additional borrowing available to be allocated is projected to be between $71.8 million and $160.6 million, excluding the additional $150 million reserved for pension purposes.

At April 30, 2010, the outstanding external debt was $525.9 million. This figure will become $725.9 million if issue debt for the $200 million of external borrowing already approved by Business Board in January 2009. If the external borrowing capacity falls below $725.9 million, no further external borrowing is permitted until such time as the actual outstanding external borrowing is lower than 33% of net assets averaged over 5 years. Therefore, if the maximum external borrowing capacity falls below $725.9 million, no further external borrowing would be permitted until such time when the net assets average over 5 years is greater than $2.2 billion. **In the event that this occurred, we would likely need to consider changing the constraints around**

the maximum borrowing capacity to sustain the University's momentum in what will otherwise be a period of some belt tightening.

It is also important to note that, apart from the uncertainties contained in the assumptions used to project net assets, the accounting rules could change in future, affecting net assets.

The following chart shows the projected range of remaining borrowing available in each future year after taking into account principal repayments that can be reallocated, excluding the additional $150 million reserved for pension purposes. From this chart we can observe that the maximum external borrowing capacity is expected to fall below $725.9 million in a number of the future years.

University of Toronto Debt Strategy

Borrowing Available Under Current Policy compared to Allocations (millions of dollars)

	Proj. 2011		**Proj. 2012**		**Proj. 2013**		**Proj. 2014**		**Proj. 2015**	
	LOW	**HIGH**	**LOW**	**HIGH**	**LOW**	**HIGH**	**LOW**	**HIGH**	**LOW**	**HIGH**
Maximum Borrowing Capacity										
Maximum external borrowing	761.0	761.0	725.3	732.8	690.1	714.0	699.6	750.0	694.3	783.1
Maximum internal borrowing	200.0	200.0	200.0	200.0	200.0	200.0	200.0	200.0	200.0	200.0
Total	**961.0**	**961.0**	**925.3**	**932.8**	**890.1**	**914.0**	**899.6**	**950.0**	**894.3**	**983.1**
Allocations:										
Approved up to January 31, 2011	962.6	962.6	962.6	962.6	962.6	962.6	962.6	962.6	962.6	962.6
Less:										
Repayments that can be reallocated	(83.9)	(83.9)	(101.0)	(101.0)	(115.6)	(115.6)	(128.4)	(128.4)	(140.1)	(140.1)
	878.7	**878.7**	**861.6**	**861.6**	**847.0**	**847.0**	**834.2**	**834.2**	**822.5**	**822.5**
Remaining to be allocated	**82.3**	**82.3**	**63.7**	**71.2**	**43.1**	**67.0**	**65.4**	**115.8**	**71.8**	**160.6**

We have temporarily allowed internal borrowing from EFIP to move beyond the $200 million maximum as bridge-financing, to provide flexibility in the timing of issuing external debt. EFIP current balances show there is no risk of cash shortages in temporarily allocating funds to internal borrowing beyond the target of $200 million. In fact, as noted earlier, we have identified additional capacity within EFIP of $150 million that can also be invested in a longer term without cash flow impairment and which we are designating as a pension borrowing capacity, to be maintained separate and apart from borrowing under this strategy, to supporting borrowing to be deposited into the pension plans.

Other Considerations - Credit Ratings

The purpose of credit ratings is to give lenders an assessment of a borrower's ability to repay debt.

The credit rating also influences the interest rate paid by the borrower, reflecting how much the lender wants to be compensated for assuming the risk related to repayment of the debt. Note that other influences on the interest rate are the underlying interest rates for benchmark on Government of Canada bonds and spreads between Canada and Ontario bonds at the moment of debt issue.

The following chart compares U of T credit ratings with our Canadian peers and with our U.S. AAU (Association of American Universities) peers and with the Province of Ontario, all at June 2010.

Credit Rating Comparison
University of Toronto with US and Canadian Peers at June 2010

Rating Definitions	**Moody's Investors Service**	**Standard & Poor's**	**Dominion Bond Rating Service**
Best quality	Aaa	AAA	AAA
Next highest quality	Aa1	AA+	AA(high)
and so on, declining	Aa2	AA	AA
	Aa3	AA-	AA(low)
	A1	A+	A(high)
	A2	A	A
	and so on	and so on	and so on

University	**Moody's Investors Service**	**Standard & Poor's**	**Dominion Bond Rating Service**
PROVINCE OF ONTARIO	**Aa1**	**AA-**	**AA(low)**
University of Texas system	Aaa	AAA	
University of Michigan	Aaa	AAA	
Queen's University		AA+	AA
University of Washington	Aaa	AA+	
University of British Columbia	Aa1	AA+	
University of Toronto	**Aa1**	**AA**	**AA**
University of California	Aa1	AA	
University of Ottawa	Aa1		AA
McMaster University		AA	AA(low)
University of Western Ontario		AA	
Ohio State University	Aa1	AA	
University of Pittsburgh	Aa1	AA	
University of Minnesota	Aa1	AA	
McGill University		AA-	
University of Illinois	Aa2	AA-	
University of Arizona	Aa2		

Source: Credit rating agencies' websites and reports.

The table above indicates the credit rating definitions and the ratings assigned to those of our US and Canadian peers that have been rated by the University of Toronto's rating agencies.

As the above chart illustrates, the University of Toronto continues to maintain excellent credit ratings, absolutely and in comparison to our peers and is rated above the Province of Ontario by two rating agencies.

The current borrowing strategy does not specify a minimum credit rating. Many factors affect credit ratings at any point in time, such as:

- Student demand.
- Government policy and funding.
- Debt per student ratios.
- Levels of unrestricted resources.
- Investment performance.
- Quality of management

While the University of Toronto should continue to maintain good credit ratings, both as comfort to our lenders regarding our ability to repay debt, and as a general indicator of financial health, we continue to believe that it is not necessary to set credit rating floors. There are too many variables involved, some of which can be quite short-term to enable credit ratings in themselves to act as a constraint to ensure the continued financial prudence of the borrowing strategy.

OTHER CONSIDERATIONS - DEBT SERVICE AND DEBT REPAYMENT

The question facing the University of Toronto is how much more do we want to spend ON the classrooms and other facilities rather than IN the classroom?

It is important to note that current outstanding debt is at fixed rates of interest, so that debt service and debt repayment on those obligations are declining as a percent of revenues and expenses over time.

Evaluation of ability to service and repay debt is done on a project by project basis, and it is assumed that the sum of these individual evaluations will aggregate to an overall ability to service and repay the debt with low risk of default.

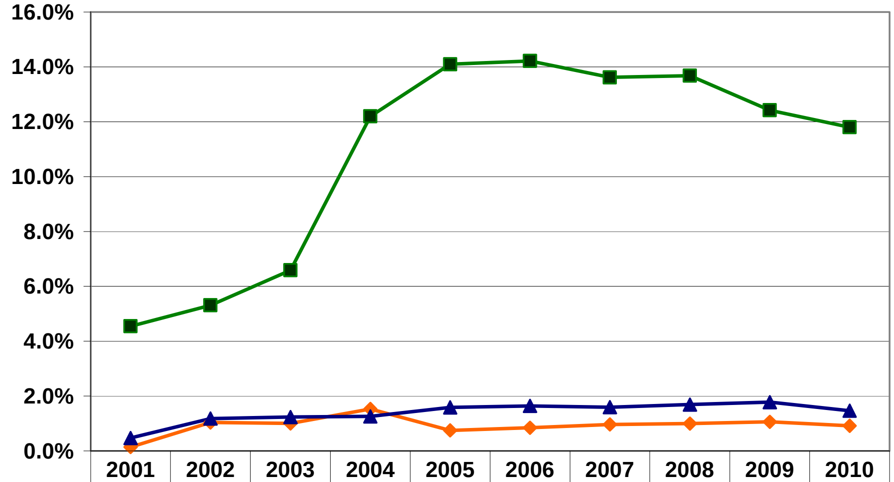
Internal borrowers, such as academic divisions or residence operations, are required to sign loan agreements under the University's internal financing program, which require regular principal and interest payments at specified fixed interest rates that are linked to market rates.

Those principal and interest payments are deposited into an internal sinking fund (the long-term borrowing pool, or LTBP) along with investment earnings on the LTBP balance. That sinking fund is drawn down by periodic interest payments to lenders and by payment of issue and ongoing administrative costs such as commission, legal and accounting fees and by ongoing trustee and rating fees. The expectation is that the net sum of additions and draw downs will be sufficient to repay each debenture upon maturity.

Debt Service – Interest Expense on External Debt:

At April 30, 2010, the interest expense on outstanding external debt was $32.4 million for the year. This was 1.5% of revenues, and 1.5% of expenses. Operating fund interest expense was 0.9% of operating fund revenues while ancillary interest expense was 11.8% of ancillary revenues.

Long-term Debt
Interest Expense as a % of Revenues
for the year ended April 30



	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Op Fund interest expense as a % of Operating revenue	0.1%	1.0%	1.0%	1.5%	0.8%	0.8%	1.0%	1.0%	1.1%	0.9%
Ancillary interest expense as a % of Ancillary revenues	4.5%	5.3%	6.6%	12.2%	14.1%	14.2%	13.6%	13.7%	12.4%	11.8%
Interest as a % of revenues	0.5%	1.2%	1.2%	1.3%	1.6%	1.6%	1.6%	1.7%	1.8%	1.5%

Principal and Interest on External and Internal Debt:

Borrowing, whether internally or externally financed, is covered by the internal financing program, which requires formal loan agreements with regular principal and interest payments for set periods, with interest charged at fixed rates linked to market rates at the issue date of the loan agreement. Therefore, evaluating the principal and interest payment load on the University must take this into account.

The $962.6 million in borrowing allocated by the Business Board to January 31, 2011 has been distributed as follows: $663.0 million to academic buildings and other requirements and $299.6 million to ancillary operations. The actual and estimated principal and interest repayment on this allocated borrowing is projected to be $79.1 million per annum distributed as follows: $53.8 million per annum to the operating fund, representing 3.4% of the 2010 operating fund revenues, and $25.3 million per annum to ancillaries, representing 17.7% of the 2010 ancillary revenues.

Given that interest rates are fixed and that revenues are expected to continue to increase, the percentages will fall over time on this amount of allocated borrowing.

The current borrowing does not place any limits on debt service or debt repayment percentages.

External debt service is partly dependent on total debt and partly dependent on interest rates. Since interest rates are fixed, debt service on currently outstanding debt will fall over time as a percent of revenues and expenses.

Allocation of debt to individual projects or divisions is based on their ability to repay that specific loan, while the aggregation of individual assessments provides the overall assessment of ability to repay debt.

The various measures that have been put in place are deemed to be sufficient control over debt service and debt repayment and no specific limits are considered necessary.

Conclusion

This review has considered the current borrowing strategy and has found the following.

The current strategy continues to be prudent. It is projected to make available between $71.8 million and $160.6 million in additional borrowing capacity by 2015 under current accounting rules, above the $962.6 million allocated by the Business Board to January 31, 2011.

An additional $150 million in EFIP could prudently be invested long-term without impairing cash flows and would therefore be available for borrowing. (This amount is over and above the $71.8 million to $160.6 million noted above.) Given the pension funding and financing requirements identified in *Ensuring a Sustainable Pension Plan for the University of Toronto* (Business Board, January 31, 2011) it makes sense to designate this additional $150 million as a pension borrowing capacity, separate and apart from the borrowing capacity otherwise defined under the current strategy. As with the existing $200 million internal borrowing capacity, if this additional $150 million invested by EFIP were needed for short-term expenditures, the borrowing would have to be re-financed externally.

In light of a potential decline in net assets, we would likely need to consider changing the constraints around the maximum borrowing capacity to sustain the University's momentum in what will otherwise be a period of some belt tightening.

Finally, it is also important to note that, apart from the uncertainties continued in the assumptions used to project net assets, the accounting rules could change in future, affecting net assets.