



UNIVERSITY OF
TORONTO

FINANCIAL SERVICES

TO: Audit Committee and Business Board

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DATE: May 31, 2012 for June 13, 2012 and June 14, 2012

AGENDA ITEM:

ITEM IDENTIFICATION:

Borrowing Capacity and Status of the Long Term Borrowing Pool to April 30, 2012

JURISDICTIONAL INFORMATION:

The Business Board approves the financing of capital projects.

PREVIOUS ACTION TAKEN:

The Business Board approved external borrowing of \$712.7 million over the period of January 2001 to February 2009. It also approved a borrowing strategy on June 17, 2004 which was most recently reviewed in April 2012. In January 2011, the Business Board also approved a \$150 million internal pension borrowing capacity, separate and apart from its maximum borrowing capacity. Prior to 2001, the University had approved outstanding long-term debt of \$61.2 million. Regular updates have been provided to the Board, most recently on May 3, 2012.

HIGHLIGHTS:

This report provides the Business Board with an update on the borrowing capacity and the long-term borrowing pool (LTBP). It updates the borrowing capacity to reflect the April 30, 2012 financial results and compares the borrowing capacity to approved borrowing. It also reports on the long-term borrowing pool, which is the University's internal sinking fund that accumulates funds for repayments of external borrowing.

Summary of Borrowing Capacity at April 30, 2012 (in millions of dollars)

	<u>External</u>	<u>Internal</u>	<u>Total</u>
Maximum Borrowing Capacity	746.6	200.0	946.6
Approved Borrowing (net)	770.0	200.0	970.0
Outstanding Borrowing	722.6	168.0	890.6
Separate Borrowing Capacity for Pension		150.0	150.0
Outstanding Borrowing for Pension		112.6	112.6

Background

The borrowing strategy approved by the Business Board on June 17, 2004 included several elements:

- that the internal borrowing capacity limit of \$200.0 million of internal loans from EFIP for the current capital plan and other requirements be maintained, along with the recognition that some or all of this sum may need to be refinanced externally at some time, if future cash flow patterns would change.
- that the maximum external borrowing capacity limit be 40% of net assets averaged over 5 years;
- that principal and interest repayments related to bullet debenture borrowing be placed in the LTBP, or other sinking fund mechanism, and, together with investment income, be used to pay periodic interest payments to lenders, and to pay issue and ongoing administrative costs, with the expectation that the net sum from these additions and draw downs will be sufficient to repay the bullet debentures at maturity.

Borrowing is managed within the University through an internal loan programme that blends both external and internal financing sources. Projects and divisions assume amortizing loans with fixed income repayment terms, and make regular principal and interest payments on these loans.

At April 30, 2011, external outstanding borrowing was \$524.1 million comprising: \$13.0 million of pre-2001 loans, \$1.1 million interest-free loan from the City of Toronto, \$160.0 million Series A debenture, \$200.0 million Series B debenture, \$75.0 million Series C debenture and \$75.0 million Series D debenture.

Update to April 30, 2012

During 2011-12, the University issued \$200 million of Series E debentures bearing an interest rate of 4.251% and with the principal amount to be repaid on December 7, 2051.

At April 30, 2012, actual borrowing outstanding was as follows:

- \$722.6 million external borrowing (reported as \$727.7 million in the financial statements due to the application of accounting rules which netted unamortized discounts and premium and adjusted swap contracts to market value).
- \$168.0 million internal borrowing (excluding pensions).
- \$112.6 million internal borrowing for pensions.

The LTBP accumulates funds for repayment of the debentures. At April 30, 2012, the LTBP assets amounted to \$101.2 million, consisting of principal repayments from internal loans of \$107.2 million and \$6.0 million of internally restricted deficit. The internally restricted deficit of \$6.0 million is mainly as a result of investment losses of

\$17.3 million incurred in 2009 which have been reduced with the positive returns of 2010 and 2011.

The internally restricted net assets mainly represent the difference between investment earnings from LTBP plus interest collected from internal loans and interest payments made to bond holders. With time, the principal repayments from internal loans together with investment income on these funds are expected to grow to fund the debenture payments at maturity dates. The income statement and balance sheet for the LTBP are attached as appendix A.

Looking forward:

Over the past few years, the regular annual review of the existing borrowing strategy, which was most recently presented to the Business Board on April 2, 2012, has projected a possible decline of the maximum external borrowing capacity under current accounting rules. At April 30, the total external borrowing capacity has declined from \$773.1 million at April 30, 2011 to \$746.6 million at April 30, 2012 under current accounting rules.

As noted in that April 2012 review, we will be changing our accounting practices effective April 30, 2013, which could change our balance sheet in a favourable way, yielding more borrowing capacity. However, we don't believe that it is appropriate to borrow more simply because changing accounting practices make our balance sheet look better. We want to continue to manage borrowing in a strategic way, as a scarce resource, in absolute terms and in comparison to our peers.

The April 2012 review also noted that the University has borrowed less than our external peers, that we have more or comparable resources to support debt issuance, and that debt service and debt repayments continue to be reasonable.

Our credit ratings continue to be strong investment grade credit ratings (Moody's Aa2, stable, S&P AA negative, and DBRS AA stable).

These results show that it may be reasonable to add very modestly to our borrowing capacity.

As we have already signaled to the Business Board, we are working on a detailed review of the current strategy and Business Board can expect to hear more on this in the coming months.

FINANCIAL AND/OR PLANNING IMPLICATIONS:

-None

RECOMMENDATION:

For information.

Long Term Borrowing Pool (LTBP)
For the year ended April 30

Income Statement
(in millions)

	<u>2012</u>	<u>2011</u>
Net investment income on LTBP investments	1.5	7.3
Interest income from internal loans	28.1	27.5
Fees and amortization of issue costs	(0.2)	(0.2)
Interest payments to bond holders	(32.2)	(29.6)
Change in internally restricted net assets	(2.8)	5.0
Internally restricted net assets, opening balance	(3.2)	(8.2)
Internally restricted net assets, closing balance	<u>(6.0)</u>	<u>(3.2)</u>

Balance Sheet
(in millions)

	<u>2012</u>	<u>2011</u>
Assets		
LTBP investments	210.0	85.8
Less: LTBP V funds not yet loaned	(110.1)	-
	<u>99.9</u>	<u>85.8</u>
Unamortized issue costs and premium(prepaid expenses)	1.3	2.9
	<u>101.2</u>	<u>88.7</u>
Liabilities		
Principal collected to date and payable to bondholders on various maturity dates	107.2	91.9
Net assets		
Internally restricted net assets	(6.0)	(3.2)
	<u>101.2</u>	<u>88.7</u>