FOR APPROVAL **PUBLIC** **OPEN SESSION**

TO: Business Board

SPONSOR: Sheila Brown, Chief Financial Officer
CONTACT INFO: 416-978-2065, sheila.brown@utoronto.ca

PRESENTER: Same as above.
CONTACT INFO:

DATE: September 3, 2019 for October 7, 2019

AGENDA ITEM: 6

ITEM IDENTIFICATION:

Revisions: *University Funds Investment Policy*

JURISDICTIONAL INFORMATION:

The Business Board is responsible for financial policy, including policy delegating financial authority, and approval of financial transactions as required by the policy. With respect to investments, these responsibilities are further delineated as follows:

- Review and approval from time to time of the investment policies for University investment funds and amendments thereto;
- Review and approval from time to time of the return targets and risk tolerances for the investment of the University funds;
- Review from time to time of the asset allocation for the investment of University funds.

GOVERNANCE PATH:

1. **Business Board [for approval] (October 7, 2019)**

PREVIOUS ACTION TAKEN:

The *University Funds Investment Policy* was last approved by the Business Board at its meeting on June 15, 2017.

HIGHLIGHTS:

University funds include funds pooled in the Long-term Capital Appreciation Pool (LTCAP), the Expendable Funds Investment Pool (EFIP), and in a small number of specially invested trust funds. This policy includes the investment return target and the risk tolerance for LTCAP and

EFIP, and recognizes that specifically invested trust funds are subject to externally imposed investment requirements. This policy has been updated in two areas:

LTCAP: The "traffic light" risk framework's Active Risk Zones have been updated to be consistent with the Active Risk Zones in the Statement of Investment Policies and Procedures of the Pension Fund Master Trust, which were revised to reflect the current practice of using at least 10 years of data in the calculation of Active Risk, rather than the 5 years of data used previously.

EFIP: A medium-term investment portfolio has been added; amounts to be allocated to the short-term, medium-term and long-term investments have been set; and investment return objective and risk tolerances have been updated to reflect current investment markets.

LTCAP:

LTCAP consists primarily of the University's endowed funds (held in perpetuity) along with a number of other funds of a long-term nature. Investment returns generated through investment of these funds support annual spending allocations to faculties and divisions for expenditures in accordance with the terms and conditions of individual endowments and other funds.

In order to meet planned spending allocations to LTCAP unit holders, the investment return target is a real investment return of at least 4.0% over 10-year periods, net of all investment fees and expenses, while taking an appropriate amount of risk to achieve this target, but without undue risk of loss.

The investment return target of 4.0% real, net of all investment fees and expenses, and the risk tolerance are unchanged from the previous policy.

The policy risk tolerance and return target are operationalized by the President of the University, with input from the Investment Committee, by establishment of a passive policy portfolio known as the Reference Portfolio together with limits, ranges and restrictions, including those with respect to risk, allocation ranges, currency exposures and liquidity. The Reference Portfolio, as with any portfolio, includes a level of risk, which for the purposes of this policy is currently defined as volatility. The asset allocation in the Reference Portfolio includes a level of volatility risk that is viewed as appropriate to the nature of the LTCAP. Given the decision to allow an active management approach, it is prudent to establish an LTCAP-level risk limit within which UTAM has discretion to make and implement investment decisions with the objective of earning returns above the Reference Portfolio. This LTCAP-level risk limit is defined as the volatility of the Reference Portfolio plus an additional amount of active risk. Active risk is defined as the volatility of the actual portfolio minus the volatility of the Reference Portfolio. Acceptable levels of active risk are managed within a "traffic light" risk framework, with normal (green), watch (orange) and alert (red) zones. **By decision of the President, on the advice of the Investment Committee, the traffic light risk framework that gauges the acceptable risk levels has been revised to reflect the usage of a data set that includes at least 10 years of data, rather than the 5 years of data used previously. This is consistent with the *Statement of Investment Policies and Procedures* of the Pension Fund Master Trust.**

EFIP:

The Expendable Funds Investment Pool contains expendable funds which are pooled and invested until they are spent. It includes the University's unspent cash from operations, capital projects, ancillary operations, expendable donations, spending allocations from endowments and research grants. At April 30, 2019, about 60% of assets were in operating and ancillary funds, about 12% were held in capital funds, and about 28% were held in restricted funds. EFIP assets are currently invested as follows:

- assets held and managed by the University to meet operational cash flow needs within three months, with a target return of 30 day T-bills and a risk tolerance of minimal risk;

- assets invested by UTAM with a target return of one-year T-bills plus 0.50% (i.e., 50 bps) and a risk tolerance of minimal risk; and

- assets invested in internal loans (mostly long-term) primarily in support of capital projects and pension in accordance with the Debt Strategy approved by the Business Board in 2012, with a return target of an appropriate spread over Government of Canada bonds of similar duration, with a risk tolerance of minimal risk.

Due to the overall growth of the University's activities, the Expendable Funds Investment Pool has more than doubled in size over the last decade. Currently, investments made by the University and UTAM are short-term in nature while the investments in internal loans are mostly long-term in nature. A review has been done to assess whether historical patterns and future projections would support the addition of a medium-term investment portfolio and an increase in the allocation to internal loans, with the objective of generating additional investment income, while controlling the additional risk. The review was conducted in three stages.

Firstly, analysis of historical cash inflows and outflows was performed over a lengthy period to assess seasonal cash flow patterns and liquidity requirements. Projections included provision for possible future adverse deviations to assess the percentages of the EFIP balance that could be conservatively invested in medium-term investments and in internal loans. That analysis showed that more than half of the EFIP balance would not be required for immediate liquidity needs and could therefore be invested in a combination of medium-term investments and internal loans. Additionally, more than half of the EFIP balance would comprise of operating and ancillary funds; and therefore, all restricted funds would continue to be invested in short-term investments within EFIP. The key findings of this analysis were that:

- 25% of EFIP, as measured at April 30, could be invested in internal loans (mostly long-term), which is well below the 40% limit set out in the University's existing Debt Strategy;
- 30% of EFIP, as measured at April 30 could be invested in a medium-term investment portfolio with an investment strategy reflecting an investment horizon of about 3 to 5 years without impeding the University's ability to meet its ongoing cash requirements; and

- 45% of EFIP as measured at April 30 would continue to be invested in a short-term portfolio managed by UTAM and in short-term funds managed by the University Administration, with in-year fluctuations of EFIP balances to be also invested in the short-term category. Additionally, funds designated for the medium-term portfolio and internal loans, awaiting to be invested, will be included in the short-term category.

Secondly, the investment return target and risk tolerances for the short-term portfolio managed by UTAM were reviewed and an investment return target and risk tolerance for the proposed medium-term portfolio was selected.

Short-term investment return and risk targets:

There are a number of drawbacks with the current investment return target for the short-term portfolio managed by UTAM that is stated as 1 year T-bills plus 50 bps with a risk tolerance of "minimal risk". First, this target is not an investible target, and second, achieving an additional 50 bps over 1-year T-bills with minimal risk is unrealistic in today's low interest rate environment. Since the current target is not investible it does not reflect what is available in the capital markets for a given level of risk (i.e., the 50 bps does not change with changing market conditions). Therefore, the short-term investment return target must be changed to an investible index that reflects both the returns currently available in the markets and a risk tolerance of "minimal risk".

The investment return target for the short-term investment portfolio was recommended to be 50% of the 1-month Canadian Bankers' Acceptance (BA) rate plus 50% of the FTSE Short Term Universe Index (a Canadian short-term bond index) with the risk tolerance remaining as minimal risk. The use of an investible index as a target rather than an investible index (i.e., 1-year T-bills) plus a fixed percentage spread (i.e., 50 bps) ensures that the target return will adjust with changes in market conditions over time. The recommended investible index is consistent with a risk tolerance of "minimal risk".

Medium-term investment return and risk targets:

Several possible investment strategies were considered for the medium-term investment portfolio, to assess whether meaningful additional investment returns could be generated within a risk level that the University would be willing to tolerate. It was determined that a public only fixed income portfolio with a medium-term investment horizon (e.g., 3 to 5 years) would best meet these objectives.

The investment return target for the medium-term portfolio was recommended to be the FTSE Corporate BBB Index (a Canadian Corporate Bond Index) with a low risk of losses over a 3 to 5 year period (i.e., "avoidance of permanent impairment of capital") but with mark-to-market fluctuations tolerated over shorter horizons as its risk tolerance. As with the investment return target for the short-term portfolio, the use of an index rather than a fixed percentage target return was made to enable the target to adjust with changes in interest rates over time and to ensure that the target was investable. This target introduces some additional risk to the portfolio, which was addressed in the third stage of the review.

Internal Loans:

The investment return target is unchanged at an appropriate spread over Government of Canada bonds of similar duration. The risk tolerance is unchanged at minimal risk.

Thirdly, the impact of the new investment portfolios on the operating budget was considered, with the following results:

- The decrease in the target return for short-term investments is expected to reduce the annual investment income budget by about $6 million.
- The addition of the medium-term portfolio has the potential to increase the annual investment income budget by $10 million to $13 million on average once the allocation is fully invested. However, additional annual volatility is expected as compared to the current strategy of investing predominantly in cash and money market vehicles.
- The increased allocation of EFIP to internal loans has the potential to increase the annual investment income budget by $5 million to $9 million on average once the allocation is fully invested. The University would benefit from internal flows from divisions paying the interest on internal loans, which would have otherwise been flowed to third party lenders if such loans had been sourced externally.

Overall, these changes have the potential of bringing additional income of between $10 and $15 million annually to the investment income budget, once the target allocations are fully invested. Although the average investment income is expected to be higher with the revised investment strategy, higher annual volatility (ranging from plus and minus $25 million to $30 million) is also expected due to the introduction of the medium-term investment portfolio based on an analysis of historical returns. These annual fluctuations would be too large for the operating budget to absorb on a year-by-year basis. To deal with the annual volatility, a simple 5-year smoothing mechanism will be put in place together with this new strategy. Each year, the operating budget will absorb 1/5th of the cumulative difference between the actual income and the budgeted income from EFIP. Please note that the smoothing only deals with the operating budget and has no impact on the investment income reported in the annual audited financial statements, which is marked to market and reported in its totality each year.

Specifically invested trust funds:

There are no changes to this section.

General:

This section of the policy includes conflict of interest guidelines and custody responsibilities. There are no changes to this section.

FINANCIAL IMPLICATIONS:

See highlights.

RECOMMENDATION:

BE IT RESOLVED

THAT the Business Board approve the *University Funds Investment Policy*, dated October 7, 2019, attached as Appendix C to the Memorandum from Sheila Brown, Chief Financial Officer, dated September 3, 2019, replacing the *University Funds Investment Policy* dated June 21, 2017.

DOCUMENTATION PROVIDED:

- Appendix A: *University Funds Investment Policy*, June 15, 2017
- Appendix B: track changes version to the proposed revised policy showing the changes from the current policy.
- Appendix C: *University Funds Investment Policy*, October 7, 2019

Appendix A

UNIVERSITY OF TORONTO

University Funds Investment Policy

June 15, 2017

To request an official copy of this policy, contact: The Office of the Governing Council
Room 106, Simcoe Hall
27 King's College Circle University of Toronto Toronto, Ontario
M5S 1A1
Phone: 416-978-6576
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E-mail: governing.council@utoronto.ca
Website: http://www.governingcouncil.utoronto.ca/

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Preamble

The financial assets ("University funds") of The Governing Council of the University of Toronto ("the University of Toronto" or "the University") are grouped and managed for investment purposes in two pools: the Long-term Capital Appreciation Pool (LTCAP), which holds endowment funds and other funds held for the long term, and the Expendable Funds Investment Pool (EFIP), which holds the University's expendable cash. There are also a small number of specifically invested trust funds with investment terms and conditions that preclude their pooling into LTCAP or EFIP.

Roles

Each of the Governing Council, the Business Board, and the President or designate have roles, as outlined in the Business Board Terms of Reference, with respect to investment of University funds.

The Business Board of Governing Council is responsible for:

- Financial policy, including policy delegating financial authority, and approval of financial transactions as required by the policy. With respect to investments, these responsibilities are further delineated as follows:
    - Review and approval from time to time of the investment policies for university investment funds and amendments thereto.
    - Review and approval from time to time of the return targets and risk tolerances for the investment of the University funds.
    - Review from time to time of the asset allocation for the investment of University funds.
    - Review of annual reports or more frequent reports as the Board may from time to time determine on the investment of University funds, such reports to include, without limitation: (i) reports on investment risk and return; and (ii) reports on fees and expenses incurred.
    - Approval of the delegation of authority to a University-controlled asset management corporation (or other entity established for a similar purpose) for the management of the investment of University funds.

The President of the University or designate is responsible for:

- With the advice of the Investment Committee, approval of asset allocation for the University funds.
- Negotiation and settlement of a detailed investment management agreement between the University and a University-controlled asset management corporation, pursuant to the approved delegation of authority to the corporation (or other entity) for the management of University funds.

Such of the funds invested in LTCAP and/or EFIP that the University desires to have invested by the University of Toronto Asset Management Corporation ("UTAM"), together with a small number of specifically invested trust funds, are invested by UTAM on behalf of the University in accordance with the Delegation of Authority from the University to UTAM and in accordance with an investment management agreement between the University and UTAM. UTAM, which was formed in April 2000, is a separate non-share capital corporation

whose members are appointed by the University of Toronto. Its primary mandate is to manage, or see to the management of, the investment funds that are delegated to it by the University of Toronto.

The Investment Committee reports to the President of the University and provides expert advice to the University Administration, collaborating extensively with the University Administration and with UTAM management on investment objectives and investment activities. The Investment Committee approves proposals from UTAM management staff for execution of investment strategy, and provides monitoring and oversight of investment performance. The Investment Committee recommends investment risk and return objectives to the University Administration. Its concurrence is sought by the President in proposing risk tolerance and investment return targets which are then put forward for approval by governance.

Risk Tolerance and Return Targets

This policy specifies the risk tolerance and investment return targets for LTCAP and EFIP, which are operationalized by the President of the University or designate.

Long-term Capital Appreciation Pool (“LTCAP”)

The Long-term Capital Appreciation Pool is a unitized fund which pools, for investment purposes, the University’s endowed trust funds along with some other funds of a permanent or long-term nature. In addition, small amounts of external funds may be invested in LTCAP in those situations where the University is a beneficiary. The purpose of LTCAP is to generate investment returns net of all investment fees and expenses that will preserve purchasing power and provide the same or better level of support for future generations of unit holders as those provided today[1]. 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 spending allocation from these funds.

In order to meet planned spending allocations to LTCAP unit holders, the investment return target is a real investment return of at least 4.0% over 10-year periods, net of all investment fees and expenses, while taking an appropriate amount of risk to achieve this target, but without undue risk of loss.

The return target and risk tolerance are operationalized by the President of the University, with input from the Investment Committee, through the President’s approval of LTCAP’s asset allocation and the investment management agreement between the University and UTAM. Asset allocation is defined as the division of a portfolio’s assets among a variety of asset classes in accordance with long-term policy goals and includes ranges, restrictions and limitations of various kinds on investments. Currently, the President does so, with input from the Investment Committee, by establishment of a passive policy portfolio, known as the Reference Portfolio, together with limits, ranges and restrictions, including those with respect to risk, allocation ranges, currency exposures, and liquidity. Taken together, these are viewed as being sufficiently large to permit

[1] The University’s *Policy for the Preservation of Capital of Endowment Funds* identifies the need to maintain the inflation-adjusted value of endowment capital; and the need to provide a stable flow of expendable income for the purposes of each fund.

UTAM management the flexibility to achieve its value-added objective but not so large as to put the portfolios at undue risk of significant underperformance relative to the Reference Portfolio. The Reference Portfolio provides a means of comparing the outcomes of passive management of investments, to an allocation that is made pursuant to an active management approach, which is the approach currently used by UTAM. The Reference Portfolio, as with any portfolio, includes a level of risk, which for the purposes of this policy is currently defined as volatility. The asset allocation in the Reference Portfolio includes a level of volatility risk that is viewed as appropriate to the nature of the LTCAP. Since active management also includes a level of volatility risk, three zones of active risk are identified, with a target zone (green), a zone that requires notification and analysis (orange), and a zone that requires mitigation steps (red). This can be described as a "traffic light" risk framework approach.

This approach is described in more detail in the following narrative and table:

> The Reference Portfolio represents a simple, low-cost, passive portfolio which is believed to be appropriate to LTCAP's long-term horizon and associated return and risk profile. By design, the Reference Portfolio is not exposed to active management decisions and thus is expected to be reviewed only periodically. Given the current environment, it is believed that the Reference Portfolio may have difficulty achieving the 4% real return objective and therefore successful active management decisions need to be implemented to achieve the return objective. The Reference Portfolio provides a transparent replicable benchmark against which to compare an active management approach, although over shorter periods of time the Reference Portfolio's real return may deviate from the longer term expectation. Given the decision to allow an active management approach, it is prudent to establish an LTCAP-level risk limit within which UTAM has discretion to make and implement investment decisions with the objective of earning returns above the Reference Portfolio. This LTCAP-level risk limit is defined as the volatility of the Reference Portfolio plus an additional amount of active risk. Active risk is defined as the volatility of the actual portfolio minus the volatility of the Reference Portfolio. The table below outlines the current "traffic light" risk framework.

Active Risk Zone	Active Risk (in basis points)
Target Zone ("Normal")	$-50 \leq Active\ Risk \leq 100$
Notification and Analysis Zone ("Watch")	$100 < Active\ Risk \leq 125$
Mitigation Zone ("Alert")	$Active\ Risk > 125$

The President, pursuant to his approval authority, and with the advice of the Investment Committee, may periodically revise the active risk framework (including, without limitation, the "traffic light" risk framework and the definition of active risk), while ensuring that the total risk in LTCAP is consistent with the risk tolerance and investment return targets identified in this policy.

UTAM will provide a periodic investment performance report to the Business Board not less frequently than annually that will compare actual investment results for LTCAP to the risk tolerance and investment return targets, and to the Reference Portfolio results.

Expendable Funds Investment Pool ("EFIP")

The Expendable Funds Investment Pool ("EFIP") contains expendable funds that are pooled and invested until spent. It includes the University's unspent cash from operations, capital projects, ancillary operations, expendable donations, expendable payouts from endowments, and research grants.

EFIP has several 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 primarily in support of capital projects and pension, and longer term assets that are managed by UTAM. The return objective and risk tolerance for each category of EFIP funds is as follows:

Category	**Return Objective**	**Risk Tolerance**	**Asset Allocation**
Assets managed by U of T	30 day T-bill return.	Minimal risk.	University Administration shall establish investment mandates and select investment vehicles. Assets normally held in bank accounts or short-term institutional money market pooled funds.
Internal loans	Appropriate spread over Government of Canada bonds of similar duration.	Minimal risk.	University Administration shall issue internal loans using EFIP funds, or using externally borrowed funds, in accordance with the Business Board-approved Debt Strategy.
Assets managed by UTAM	One-year T-bill return plus 50 bps.	Minimal risk.	University Administration shall approve the asset allocation. UTAM shall implement investment strategy in accordance with its mandate.

For EFIP funds managed by UTAM, portfolio diversification, categories and subcategories of investments and investment restrictions and other elements of investment strategy will be recommended by

UTAM to the University Administration for approval. UTAM will provide a periodic investment performance report to the Business Board no less frequently than annually with respect to EFIP investment results.

Specifically Invested Trust Funds

The assets of specifically invested trust funds shall be invested to adhere to the investment requirements specifically imposed on the University by contractual agreement, whether by a donor, by condition of an estate, or by external administrative arrangement.

General

Conflict of Interest Guidelines

Anyone involved directly or indirectly with the investment of University funds (“the Affected Persons”) shall promptly declare 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 responsibility regarding the investment of University funds. Declarations shall be made to the next level of accountability (e.g. depending on the circumstances, and without limitation, to the supervisor, UTAM President, University of Toronto President, Business Board Chair, or Chair of Governing Council).

Any such disclosure shall include, but is not limited to, any material ownership of securities, or any material ownership of any kind, either by an Affected Person or a member of the Affected Person`s immediate family, which could impair, or could reasonably be viewed as impairing, their ability to render unbiased advice, or to make unbiased decisions affecting the investment of the University funds. For clarity, financial interests that are in the ordinary course of personal affairs, and that are not reasonably viewed as material, fall outside the disclosure obligation. If the Affected Person has any doubt as to whether a conflict of interest may exist, including whether a particular interest may reasonably be viewed as material, disclosure should be made.

Further, no Affected Person shall make any personal financial gain (direct or indirect) because of his or her fiduciary position. However, normal and reasonable fees and expenses incurred in the discharge of their responsibilities are permitted upon notification in advance and in writing to the University.

No Affected Person shall accept a gift or gratuity or other personal favour, other than one of nominal value, from a person with whom the Affected Person deals in the course of performance of his or her duties and responsibilities regarding the investment of University funds.

No Affected Person who has or is required to make a disclosure as contemplated in this policy shall participate in any discussion, decision or vote relating to any proposed investment or transaction in respect of which he or she has made or is required to make a disclosure.

Custody

The University Administration appoints the custodian and delegates operational oversight of the custodian to UTAM. The custodian/trustee will:

- Maintain safe custody over the University funds.
- Execute the instructions of the University, of UTAM and of the investment managers.
- Record income and provide monthly financial statements to the University and to UTAM as required.
- Meet with the University and UTAM as required.

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Sheila Brown, Chief Financial Officer

June 15, 2017

Appendix B

UNIVERSITY OF TORONTO

University Funds Investment Policy

October 7, 2019~~June 15, 2017~~

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Active Risk Zone	Active Risk (in basis points)
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Mitigation Zone (“Alert”)	$Active\ Risk > \cancel{125}175$

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~~Category~~	~~**Return Objective**~~	~~**Risk Tolerance**~~	~~**Asset Allocation**~~
~~**Assets managed by U of T**~~	~~30 day T-bill return.~~	~~Minimal risk.~~	~~University Administration shall establish investment mandates and select investment vehicles. Assets normally held in bank accounts or short-term institutional money market pooled funds.~~
~~**Internal loans**~~	~~Appropriate spread over Government of Canada bonds of similar duration.~~	~~Minimal risk.~~	~~University Administration shall issue internal loans using EFIP funds, or using externally borrowed funds, in accordance with the Business Board-approved Debt Strategy.~~
~~**Assets managed by UTAM**~~	~~One-year T-bill return plus 50 bps.~~	~~Minimal risk.~~	~~University Administration shall approve the asset allocation. UTAM shall implement investment strategy in accordance with its mandate.~~

EFIP is composed of:

- Short-term funds held by the University to meet operational cash flow needs within three months;
- Short-term and medium-term portfolios managed by UTAM; and
- Long-term funds invested by the University in internal loans.

The amounts allocated to short-term, medium-term and internal loans are determined annually based on the EFIP balances at April 30, as follows:

- 45% is allocated to the short-term category, representing funds available to be spent on a short-term basis, with an investment strategy reflecting an investment horizon of less than 3 years, and with any intra-year fluctuations in the total EFIP balance to be allocated to the short-term category. Additionally, funds allocated to medium and long-term investments, which have not yet been invested, will also be invested in the short-term category. Within the short-term category, funds required for operational cash flow needs within three months are held by the University, and the remaining balance is invested by UTAM.

- 30% is allocated to a medium-term portfolio to be managed by UTAM, representing funds that are not expected to be spent in the short-term, with an investment strategy reflecting an investment horizon of about 3 to 5 years.

- 25% is allocated for the long-term, representing funds that are expected to be used for internal loans (mostly long-term loans with terms of 25 years) under the University's internal borrowing programme[2]. Funds provided to the University that have restricted terms for their use are not invested in long-term investments, but are invested in short and medium term portfolios.

The investment return targets and risk tolerances are as follows:

	Investment Return Objective	**Risk Tolerance**	**Asset Allocation**
Short-term Investments – managed by U of T to meet cash flow needs within 3 months	30 day T-bill return	Minimal risk.	University Administration shall establish investment mandates and select investment vehicles.
Short-term portfolio – managed by UTAM	50% 1 month Canadian Bankers' Acceptance (BA) rate plus 50% FTSE short-term Universe	Minimal risk.	University Administration shall approve the asset allocation. UTAM shall implement investment strategy in accordance with its mandate.
Medium-term portfolio – managed by UTAM	FTSE Corporate BBB Index	Low risk of losses over a 3 to 5 year period (i.e., avoidance of permanent capital impairment) with mark-to-market fluctuations tolerated over shorter time horizons.	University Administration shall approve the asset allocation. UTAM shall implement investment strategy in accordance with its mandate.
Long-term investments in Internal loans under the University's internal borrowing programme	Appropriate spread of Government of Canada bonds of similar duration	Minimal risk.	University Administration shall issue internal loans using EFIP funds, or using externally borrowed funds, in accordance with the Business Board-approved Debt Strategy

[2] The University's Debt Strategy, approved by the Business Board in 2012, permits up to 40% of EFIP to be used for longer-term loans under the University's internal borrowing programme.

For EFIP funds managed by UTAM, portfolio diversification, categories and subcategories of investments and investment restrictions and other elements of investment strategy will be recommended by UTAM to the University Administration for approval. UTAM will provide a periodic investment performance report to the Business Board no less frequently than annually with respect to EFIP investment results.

Specifically Invested Trust Funds

The assets of specifically invested trust funds shall be invested to adhere to the investment requirements specifically imposed on the University by contractual agreement, whether by a donor, by condition of an estate, or by external administrative arrangement.

General

Conflict of Interest Guidelines

Anyone involved directly or indirectly with the investment of University funds (“the Affected Persons”) shall promptly declare 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 responsibility regarding the investment of University funds. Declarations shall be made to the next level of accountability (e.g. depending on the circumstances, and without limitation, to the supervisor, UTAM President, University of Toronto President, Business Board Chair, or Chair of Governing Council).

Any such disclosure shall include, but is not limited to, any material ownership of securities, or any material ownership of any kind, either by an Affected Person or a member of the Affected Person`s immediate family, which could impair, or could reasonably be viewed as impairing, their ability to render unbiased advice, or to make unbiased decisions affecting the investment of the University funds. For clarity, financial interests that are in the ordinary course of personal affairs, and that are not reasonably viewed as material, fall outside the disclosure obligation. If the Affected Person has any doubt as to whether a conflict of interest may exist, including whether a particular interest may reasonably be viewed as material, disclosure should be made.

Further, no Affected Person shall make any personal financial gain (direct or indirect) because of his or her fiduciary position. However, normal and reasonable fees and expenses incurred in the discharge of their responsibilities are permitted upon notification in advance and in writing to the University.

No Affected Person shall accept a gift or gratuity or other personal favour, other than one of nominal value, from a person with whom the Affected Person deals in the course of performance of his or her duties and responsibilities regarding the investment of University funds.

No Affected Person who has or is required to make a disclosure as contemplated in this policy shall participate in any discussion, decision or vote relating to any proposed investment or transaction in respect of which he or she has made or is required to make a disclosure.

Custody

The University Administration appoints the custodian and delegates operational oversight of the custodian to UTAM. The custodian/trustee will:

- Maintain safe custody over the University funds.
- Execute the instructions of the University, of UTAM and of the investment managers.
- Record income and provide monthly financial statements to the University and to UTAM as required.
- Meet with the University and UTAM as required.

Sheila Brown, Chief Financial Officer

~~June 15, 2017~~October 7, 2019

Appendix C

University Funds Investment Policy

October 7, 2019

Table of Contents

Preamble

The financial assets ("University funds") of The Governing Council of the University of Toronto ("the University of Toronto" or "the University") are grouped and managed for investment purposes in two pools: the Long-term Capital Appreciation Pool (LTCAP), which holds endowment funds and other funds held for the long term, and the Expendable Funds Investment Pool (EFIP), which holds the University's expendable cash. There are also a small number of specifically invested trust funds with investment terms and conditions that preclude their pooling into LTCAP or EFIP.

Roles

Each of the Governing Council, the Business Board, and the President or designate have roles, as outlined in the Business Board Terms of Reference, with respect to investment of University funds.

The Business Board of Governing Council is responsible for:

- Financial policy, including policy delegating financial authority, and approval of financial transactions as required by the policy. With respect to investments, these responsibilities are further delineated as follows:
    - Review and approval from time to time of the investment policies for university investment funds and amendments thereto.
    - Review and approval from time to time of the return targets and risk tolerances for the investment of the University funds.
    - Review from time to time of the asset allocation for the investment of University funds.
    - Review of annual reports or more frequent reports as the Board may from time to time determine on the investment of University funds, such reports to include, without limitation: (i) reports on investment risk and return; and (ii) reports on fees and expenses incurred.
    - Approval of the delegation of authority to a University-controlled asset management corporation (or other entity established for a similar purpose) for the management of the investment of University funds.

The President of the University or designate is responsible for:

- With the advice of the Investment Committee, approval of asset allocation for the University funds.
- Negotiation and settlement of a detailed investment management agreement between the University and a University-controlled asset management corporation, pursuant to the approved delegation of authority to the corporation (or other entity) for the management of University funds.

Such of the funds invested in LTCAP and/or EFIP that the University desires to have invested by the University of Toronto Asset Management Corporation ("UTAM"), together with a small number of specifically invested trust funds, are invested by UTAM on behalf of the University in accordance with the Delegation of Authority from the University to UTAM and in accordance with an investment management agreement between the University and UTAM. UTAM, which was formed in April 2000, is a separate non-share capital corporation

whose members are appointed by the University of Toronto. Its primary mandate is to manage, or see to the management of, the investment funds that are delegated to it by the University of Toronto.

The Investment Committee reports to the President of the University and provides expert advice to the University Administration, collaborating extensively with the University Administration and with UTAM management on investment objectives and investment activities. The Investment Committee approves proposals from UTAM management staff for execution of investment strategy, and provides monitoring and oversight of investment performance. The Investment Committee recommends investment risk and return objectives to the University Administration. Its concurrence is sought by the President in proposing risk tolerance and investment return targets which are then put forward for approval by governance.

Risk Tolerance and Return Targets

This policy specifies the risk tolerance and investment return targets for LTCAP and EFIP, which are operationalized by the President of the University or designate.

Long-term Capital Appreciation Pool ("LTCAP")

The Long-term Capital Appreciation Pool is a unitized fund which pools, for investment purposes, the University's endowed trust funds along with some other funds of a permanent or long-term nature. In addition, small amounts of external funds may be invested in LTCAP in those situations where the University is a beneficiary. The purpose of LTCAP is to generate investment returns net of all investment fees and expenses that will preserve purchasing power and provide the same or better level of support for future generations of unit holders as those provided today[1]. 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 spending allocation from these funds.

In order to meet planned spending allocations to LTCAP unit holders, the investment return target is a real investment return of at least 4.0% over 10-year periods, net of all investment fees and expenses, while taking an appropriate amount of risk to achieve this target, but without undue risk of loss.

The return target and risk tolerance are operationalized by the President of the University, with input from the Investment Committee, through the President's approval of LTCAP's asset allocation and the investment management agreement between the University and UTAM. Asset allocation is defined as the division of a portfolio's assets among a variety of asset classes in accordance with long-term policy goals and includes ranges, restrictions and limitations of various kinds on investments. Currently, the President does so, with input from the Investment Committee, by establishment of a passive policy portfolio, known as the Reference Portfolio, together with limits, ranges and restrictions, including those with respect to risk, allocation ranges, currency exposures, and liquidity. Taken together, these are viewed as being sufficiently large to permit UTAM management the flexibility to achieve its value-added objective but not so large as to put the portfolios at

[1] The University's *Policy for the Preservation of Capital of Endowment Funds* identifies the need to maintain the inflation-adjusted value of endowment capital; and the need to provide a stable flow of expendable income for the purposes of each fund.

undue risk of significant underperformance relative to the Reference Portfolio. The Reference Portfolio provides a means of comparing the outcomes of passive management of investments, to an allocation that is made pursuant to an active management approach, which is the approach currently used by UTAM. The Reference Portfolio, as with any portfolio, includes a level of risk, which for the purposes of this policy is currently defined as volatility. The asset allocation in the Reference Portfolio includes a level of volatility risk that is viewed as appropriate to the nature of the LTCAP. Since active management also includes a level of volatility risk, three zones of active risk are identified, with a target zone (green), a zone that requires notification and analysis (orange), and a zone that requires mitigation steps (red). This can be described as a "traffic light" risk framework approach.

This approach is described in more detail in the following narrative and table:

> The Reference Portfolio represents a simple, low-cost, passive portfolio which is believed to be appropriate to LTCAP's long-term horizon and associated return and risk profile. By design, the Reference Portfolio is not exposed to active management decisions and thus is expected to be reviewed only periodically. Given the current environment, it is believed that the Reference Portfolio may have difficulty achieving the 4% real return objective and therefore successful active management decisions need to be implemented to achieve the return objective. The Reference Portfolio provides a transparent replicable benchmark against which to compare an active management approach, although over shorter periods of time the Reference Portfolio's real return may deviate from the longer term expectation. Given the decision to allow an active management approach, it is prudent to establish an LTCAP-level risk limit within which UTAM has discretion to make and implement investment decisions with the objective of earning returns above the Reference Portfolio. This LTCAP-level risk limit is defined as the volatility of the Reference Portfolio plus an additional amount of active risk. Active risk is defined as the volatility of the actual portfolio minus the volatility of the Reference Portfolio. The table below outlines the current "traffic light" risk framework.

Active Risk Zone	**Active Risk (in basis points)**
Target Zone ("Normal")	$-50 \leq Active\ Risk \leq 150$
Notification and Analysis Zone ("Watch")	$150 < Active\ Risk \leq 175$
Mitigation Zone ("Alert")	$Active\ Risk > 175$

The President, pursuant to his approval authority, and with the advice of the Investment Committee, may periodically revise the active risk framework (including, without limitation, the "traffic light" risk framework and the definition of active risk), while ensuring that the total risk in LTCAP is consistent with the risk tolerance and investment return targets identified in this policy.

UTAM will provide a periodic investment performance report to the Business Board not less frequently than annually that will compare actual investment results for LTCAP to the risk tolerance and investment return targets, and to the Reference Portfolio results.

Expendable Funds Investment Pool ("EFIP")

The Expendable Funds Investment Pool ("EFIP") contains expendable funds that are pooled and invested until spent. It includes the University's unspent cash from operations, capital projects, ancillary operations, expendable donations, expendable payouts from endowments, and research grants.

EFIP is composed of:

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Sheila Brown, Chief Financial Officer

October 7, 2019