

TO: Business Board
FROM: Janice Oliver
FOR: Meeting of January 21, 2002
AGENDA ITEM: 4 (b)

ITEM IDENTIFICATION: University of Toronto at Scarborough Residence-Phase 4

SPONSOR: Janice Oliver, Assistant Vice-President, Operations & Services
Call 978-4322 for further information

JURISDICTIONAL INFORMATION:

Pursuant to section 4.1(b) of its Terms of Reference, the Business Board is asked to concur with recommendations to complete 'major projects, plans or programs outside the normal course of business that require the balancing of expense and revenue'. It is the Board's duty to examine the financial plan for the project and to satisfy itself that revenue will be sufficient to balance the expense of constructing and operating the residence.

Pursuant to Section 5C of the Policy on Capital Planning and Capital Projects, the Business Board is charged to assess the "cost effectiveness of the project, the extent to which full funding is committed or obtainable, and whether there are any significant outstanding and unresolved issues with respect to the project".

PREVIOUS ACTION TAKEN:

In November 2000, Business Board concurred with the Academic Board and University Affairs Board recommendation to Governing Council that the project be approved.

Business Board also authorized the expenditure of \$1.2 million for the design and site development work of the project.

ACTION SOUGHT:

Subject to the understanding that the rates of the University of Toronto at Scarborough Residency Ancillary Operation will be increased sufficiently to ensure that the operation continues to recover its own cost,

That the Vice President, Business Affairs be authorized

- (i) to expend up to \$14.9 million for the construction of the Scarborough Residence-Phase 4.
- (ii) to arrange such interim and long-term financing as required.

HIGHLIGHTS:

The proposed residence, which is designed to be 4 storeys high, providing 201 bedrooms in 54 suites and housing the residence administration offices, will add 7905 square meters to the existing UTSC residence ancillary operation.

The projected cost is \$14.9 million, an increase of \$1.2 million over the original proposal. The increase is due to the inclusion of the residence administration offices and further escalation in the market (\$800,000), the cost of bringing utilities to the site from the nearest public street (\$150,000), and the replacement of lost parking (\$250,000).

FINANCIAL IMPLICATIONS:

All U of T ancillary operations operate like businesses, having responsibility to cover all costs. The four objectives for all ancillaries are: 1) to operate without a subsidy from the operating fund; 2) to provide for all costs of capital renewal, including deferred maintenance; 3) to generate sufficient surplus to cover operating contingencies; and, after the first three requirements have been met, and where possible, 4) to contribute net revenue to operating budgets.

The need for residence expansion has presented a financial challenge, in that the costs of building new residences have risen faster than residence rates. To maintain financial health with room rates at an affordable level, the four objectives were modified for this project as outlined in the attached business case, and the financial viability of the combined residence ancillary operation evaluated accordingly.

Based on this evaluation, the combined residence ancillary at UTSC is financially viable. The projected construction cost of \$14.9 million will be funded as part of the residence operation. It is projected to break even annually in year 5 and cumulatively in year 8 as required, as the result of a subsidy arrangement of \$101,880 annually for eight years, the capital renewal allowance for the new residence commencing in year 6 and residence rate increases as described in the attached.

It is particularly important to note that the UTSC residence ancillary rates are approved annually by the University Affairs Board. Implicit in the Business Board approval is the understanding that residence rates will be increased each year by no less than the percentages projected in the business case in order to maintain the financial viability of the residence operation.



University of Toronto

Office of the Assistant Vice-President, Operations and Services

December 20, 2001

MEMORANDUM TO: Members of the Business Board

FROM: Janice Oliver, Assistant Vice-President, Operations & Services

RE: **UTSC Residence Phase 4**

Background - Governance Approvals

In October 2000 the University of Toronto at Scarborough (UTSC) submitted the Planning Report for Phase 4 of its residence system to governance. The plan contemplated a 7559 gross square meter building costing \$13.7 million, providing space for 203 students. The residence was to be a suite-style with each suite containing 4 bedrooms, 2 bathrooms, living and kitchen areas. The capital cost of the project (\$13.7 million) was based on the costs of the Erindale Phase 6 Residence, inflated to a June 2001 tender. The project was to be 100% financed with a 25-year mortgage. Interest and principal payments were to be made from the ancillary's budget, along with funding from the Academic Priority Fund up to \$204,000 per year for a period of 8 years. The funding model had the total UTSC residence system in a positive cash flow by year 5 and a cumulative break-even position by year 8. It did however assume that the requirement to set aside 1.5% of the capital cost of the building be waived in the first 5 years of operation of the residence.

Business Board reviewed the proposal and concurred with the Academic Board and University Affairs Board recommendation to Governing Council for approval of the project. Business Board also authorized the expenditure of \$1.2 million for the design and site development work portion of the project.

Project As Designed

In December 2000 Montgomery Sisam Associates Inc. and Daird Sampson Neuert Architects Inc. in joint venture were retained as architects for the project. In discussion with UTSC, the program was revised to incorporate a change of scope to include residence administration in the new building. The UTSC Master Plan 2001, which was completed after the submission for the Phase 4 residence, indicated that the Student Village Centre where the residence offices are currently housed, was to be demolished. UTSC therefore decided to move in advance of the Master Plan and incorporate the residence administration offices within the design of Phase 4.

The design for the residence includes the program requirements for telephone, cable and data outlets in the bedrooms and living rooms, as well as telephone drops in the study rooms and offices. The residence as designed is 4 storeys high and provides 201 bedrooms in 54 suites and 192 net assignable square meters for Residence Administration staff. The gross floor area is 7905 square meters.

The design was reviewed by the University Design Review Committee and their comments with respect to massing, lighting and landscape have been incorporated.

Capital Cost Estimate

The total project cost based on a quantity surveyor's estimate of the 90% contract drawings is \$14.9 million. The increase is broken down as follows: \$800,000 to incorporate the residence

administration offices and further escalation in the market; \$150,000 to bring utilities to the site from the nearest public street, and \$250,000 for the replacement of lost parking. The project is at tender. Authorization is being sought to expend the \$14.9 million assuming a successful tender close.

Business Case

The capital project for the UTSC Residence, which is projected to cost \$14.9 million, will be funded as part of the residence operation. The financial analysis, which follows, addresses the ability of the combined residence operation to fund the new residence capital construction cost and ongoing operational costs while remaining financially healthy.

All U of T ancillary operations operate like businesses, receiving their revenues and having responsibility to cover all costs, including direct and indirect costs, costs of capital construction and costs of infrastructure maintenance. The four objectives for all ancillaries are:

1. to operate without a subsidy from the operating fund;
2. to provide for all costs of capital renewal, including deferred maintenance;
3. to generate sufficient surplus to cover operating contingencies; and, after the first three requirements have been met;
4. to contribute net revenue to operating budgets.

The need for residence expansion has presented a financial challenge, in that the costs of building new residences have risen faster than residence rates. To maintain room rates at an affordable level, an annual subsidy of \$1.7 million has been allocated from the academic priorities fund (APF) in support of residence expansion and other changes have been made to the objectives for this ancillary as follows.

In the case of the first objective, a subsidy will be provided for a maximum of eight years through the APF from the University's operating budget to a college's residence ancillary budget to cover a portion of the borrowing cost. The combined ancillary operation will be required to break even annually in year 5 and cumulatively in year 8, and the subsidy amount will be calculated to achieve those break-even targets. Should special circumstances warrant, the University will continue to assist a college with principal and interest payments after eight years.

In the case of the second objective, the normal capital renewal provision for new residence buildings will be deferred until the sixth year they are in operation.

The third objective will remain unaltered, i.e., the residence ancillary will continue to be responsible for funding operating and maintenance contingencies in the residences.

The first three objectives must be met before the fourth can be invoked, i.e., transfers from the residence and conference ancillaries to the divisional operating budget can only occur when the residence and conference ancillaries combined meet the first three objectives. During the current residence expansion program, the first three objectives will only be met after

1. the annual subsidy provision has ended;
2. the annual 1.5% provision for capital renewal is being set aside; and
3. operating contingencies have been provided for by means of net surpluses.

In the intervening period, it is expected that the residence and conference ancillaries will retain within their ancillary budgets the funds normally transferred to their college operating budget and use these funds to support the expansion program. This expectation has been factored into the financial plans which colleges have submitted for their program of residential expansion and into the calculation of the maximum subsidy available to each division from the APF.

During the residence expansion program, colleges are expected to continue to strive to maximize their cash flows through revenue and expense management. Each year during which a central subsidy flows to a college, the actual amounts generated by the residence and conference ancillaries combined will be compared to the amounts required in the subsidy model. Colleges will be allowed to transfer to their operating budgets any amount in excess of the amount required by the subsidy model to generate annual break-even of the ancillary in year 5 and cumulative break-even in year 8.

The proposed residence will add to the capacity of the existing UTSC residence ancillary operation. The projected cost is \$14,857,514, an increase of \$1,170,000 over the original proposal. The financial viability of the combined residence ancillary operation, based on the revised construction cost, has been evaluated against the four modified objectives. Here are the key assumptions:

1. **Borrowing and repayment:** the total projected construction cost, amounting to \$14,857,514, will be borrowed and the annual principal and interest repayment is projected at 8% annually, with a 25 year amortization.
2. **Operating costs** are projected to change as follows:
 - renegotiation of existing mortgages has resulted in an annual saving of \$25,000 per year, since the submission of the original proposal.
 - decrease of \$52,298 due to projected savings in utilities and major maintenance
 - re-assignment of \$34,449 in borrowing costs for the Student Village Centre to another operating unit.
 - the proposed new residence will provide internet services to the resident students for a fee. The annual cost is estimated at \$52,375. These costs will be partly subsidized from existing residence operations, with the balance being paid by the students. Students will be required to sign up for the service at the beginning of the year and will be required to pay the annual fee upfront.
3. **Residence revenue** is projected to increase, as follows:
 - residence rates are projected to increase by 7% in 2002-2003, bringing the initial monthly bed rate for the new residence to \$525, as compared to the \$515 planned in the original proposal. Residence rates are subsequently forecast to increase by 5% annually up to and including 2005-2006, 4% in 2006-2007, 3.5 % in 2008-2009 and 3% annually thereafter.
 - there is a projected increase of \$14,717 in the annual contribution from Conference Services.
4. **Capital renewal allowance:** begins in the 6th year of operation at 1.5%.
5. **Subsidy:** as a result of the changes described above, the annual subsidy to be provided from the APF for the first 8 years of operation of the new residence has decreased from the \$203,759 needed under the original proposal, to \$101,880 per annum.

A sensitivity analysis was performed in which additional construction and operational costs were introduced independently into the model to determine how much additional revenue, if any, would be required to maintain the financial targets within the model. Since the subsidy has been determined as the amount necessary to enable the financial model to break even annually after 5 years and cumulatively after 8 years, even a modest variation from assumptions will require corrective action. If construction costs increased by 10% over the current cost estimates, then additional net annual revenues of \$148,188 would be required to meet the financial targets.

It is particularly important to note that the UTSC residence ancillary rates are approved annually by the University Affairs Board. Implicit in the Business Board approval is the understanding that residence rates will be increased each year by no less than the percentages projected here in order to maintain the financial viability of the residence operation.

Based on the above analysis, and evaluating against the four modified objectives, the combined residence ancillary at UTSC is financially viable. It is projected to break even annually in year 5 and cumulatively in year 8 as required, as the result of a subsidy arrangement of \$101,880 annually for eight years, the capital renewal allowance for the new residence commencing in year 6 and residence rate increases as described above.

Standard criteria for this residence:	
Residence style:	Suite
Revenues:	
Winter occupancy rates, new residence	98.00%
Expenses:	
Rate of annual increase for the 1st ten years	2.26%
Mortgage rate used	8.00%
Amortization term in years	25
Compounding interest periods/year	12
Capital renewal provided for at a rate of	1.50%
Capital renewal reserve allocations to begin in year	6
Financial targets to be met by Total Ancillary (year)	
Breakeven, annual	5
Breakeven, cumulative	8

	Original	Revised
	Approved Model	Model
Variable criteria for this residence:		
Number of beds	203	201
Initial monthly bed rate for new residence	493	525
Residence opening date	Sep-2002	Sep-2003
Winter bed rates will increase at a rate of 5% until and at a rate of 3% thereafter	2007-08	
Winter bed rates will increase at a rate of 5% until and at a rate of 4% until and at a rate of 3.5% in and 3% thereafter		2005-06 2007-08 2008-09
Capital cost and financing requirements:		
Cost to build residence, original	\$13,687,514	\$13,687,514
Additional costs, anticipated		1,170,000
Revised cost to build residence	\$13,687,514	\$14,857,514
Downpayment provided by ancillary		
Amount to be mortgaged	\$13,687,514	\$14,857,514
Cost to build per bed	\$67,426	\$73,918
Annual mortgage payment	\$1,267,709	\$1,376,072
Subsidy to be paid for 8 years		
Amount of annual subsidy required to meet financial targets per standard above	203,759	101,880

Sensitivity analysis based on assumption of breakeven of 5/8 & the new subsidy requirement:

- The financial assumptions in the revised model would support the following with no change in financial targets or subsidy requirements:

Maximum capital cost increase if revenue/expenses unchanged	0.00%
Maximum decrease in operational net income if revised capital cost stable	0.00%
- If construction costs increased by 10% over the current cost estimates, then additional annual net revenues would be required to maintain the financial targets in the amount of \$148,188

