UNIVERSITY OF TORONTO

FINANCIAL SERVICES

TO:	Audit Committee and Business Board
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DATE:	May 29, 2013 for June 12, 2013 and June 13, 2013
AGENDA ITEM:	Audit Committee, Item 8. Business Board, Item 3.

ITEM IDENTIFICATION:

Debt Policy Limit, Debt Allocations, Outstanding Debt Issued and Status of the Long Term Borrowing Pool to April 30, 2013

JURISDICTIONAL INFORMATION:

The Business Board approves the financing of capital projects.

PREVIOUS ACTION TAKEN:

The Business Board approved a new debt strategy on November 5, 2012. The Business Board had approved external debt of $712.7 million and internal debt of $200.0 million over the period of January 2001 to February 2009; and in January 2011, it approved an additional $150 million internal debt reserved for pensions. 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 April 8, 2013.

HIGHLIGHTS:

This report provides the Business Board with an update on the total debt limit (as per new debt policy approved in November 2012) based on the financial results of April 30, 2013. It compares the updated total debt limit to the total debt allocated by the Business Board and the outstanding debt undertaken by the University as at April 30, 2013. It also provides an update on the actual debt burden ratio and viability ratio based on financial results at April 30, 2013 as compared to the policy ratios. Finally, it provides an update of the status of the long-term borrowing pool ("LTBP"), which is the University's internal sinking fund that accumulates funds for repayments of debentures issued. A summary of these results is provided in the table below. Appendix I attached is the regular status report on debt to April 30, 2013.

Summary of Debt at April 30, 2013 **(in millions of dollars)**				
	Total	External	Internal	
			Other	Pension
Total debt limit	1,400.0	1,050.0	200.0	150.0
Approved debt allocations	1,114.2	764.2	200.0	150.0
Remaining unallocated	285.8	285.8	-	-
Actual debt outstanding	1,001.8	721.0	174.1	106.7
Policy debt burden ratio	5.0%			
Actual debt burden ratio	3.7%	2.5%	0.8%	0.4%
Viability ratio - Total debt limit (desired higher than 0.80)	0.85			
Viability ratio - Actual oustanding debt	1.19			

Background

The debt strategy approved by the Business Board on November 5, 2012 included the following elements:

- the total debt limit is calculated based on a 5% debt burden ratio (interest plus principal repayment divided by total expenditures adjusted for depreciation and non-funded pension expense);

- debt includes all long-term external and internal borrowed funds (with fungibility between them) obtained by any means and excludes letters and lines of credit and all short-term and medium term internal financing for purposes such as fund deficits;

- the internal debt component is limited to 40% of the Expendable Funds Investment Pool ("EFIP"), defined as internal debt outstanding divided by audited April 30 EFIP balance plus internal debt outstanding;

- the viability ratio (expendable resources divided by debt) is used as a secondary monitoring ratio, so that if the viability ratio related to the debt policy limit is below 0.8, consideration will be given to moderating the debt policy limit;

- credit ratings will continue to be excluded from policy determination because they are subject to many external factors, including changes in rating agency methodologies over time;

- borrowing method (e.g. private placement or other method) continues to be determined by the senior officer responsible for financial matters;

- principal and interest repayments related to bullet debenture borrowing will continue to 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; and

- borrowing will continue to be 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.

Update to April 30, 2013 (see appendix II for calculations):

- The debt burden ratio based on actual outstanding debt was 3.7% ($87.1 million of total interest and principal divided by $2.4 billion of expenditures), which is 1.3% lower than the policy debt burden ratio of 5%. The viability ratio based on actual debt outstanding was 1.19, which is higher than the desired lower threshold of 0.80.

- Based on actual expenditures at April 30, 2013, a 5% policy debt burden ratio resulted in a total debt limit of $1.4 billion. Had the University issued a total $1.4 billion debt at April 30, 2013, the viability ratio would have been 0.85, which is higher than the desired lower threshold of 0.80.

- Total debt outstanding of $1,001.8 million consisted of:

    - $721.0 million of external debt (reported as $726.0 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), of which $710.0 million represents debt issued through debentures series A to E, $10.3 million represents debt issued prior to 2001 and $0.7 million represents an interest free loan from the City of Toronto.
    - $280.8 million of internal debt of which $106.7 relates to pensions. The internal component of the debt represents 20.1% of EFIP, about half of the maximum limit of 40%.

- The LTBP accumulates funds for repayment of the debentures. At April 30, 2013, the LTBP assets amounted to $131.7 million, consisting of principal repayments of $131.5 million and $0.2 million of internally restricted net assets. Internally restricted net assets mainly represent the difference between investment earnings from LTBP (including interest collected from internal loans) and interest payments made to bond holders. The income statement and balance sheet for the LTBP are attached as appendix III.

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

RECOMMENDATION:
For information.

Appendix I

University of Toronto
Status Report on Debt to April 30, 2013

Financial Ratios in accordance with Policy	Total	Internal Component Pension Debt	Internal Component Other Debt	External Component
Debt burden ratios:				
Debt policy limit at April 30, 2013	**5.0%**			
Actual debt outstanding at April 30, 2013	**3.7%**	0.4%	0.8%	2.5%
Viability ratios:				
Debt policy limit at April 30, 2013	**0.85**			
Actual debt outstanding at April 30, 2013	**1.19**	11.21	6.87	1.66
Monitoring debt burden + pension special payments				
Actual debt outstanding at April 30, 2013 plus special pension payments as % of total expenditures	**6.3%**	3.0%	0.8%	2.5%

Debt Policy Limit April 30, 2013	Total in Millions	Internal Component Pension Debt	Internal Component Other Debt	External Component
Debt Policy Limit	**1,400.0**	150.0	200.0	1,050.0

Allocations	Total in Millions	Internal Component Pension Debt	Internal Component Other Debt	External Component
Opening balance at March 31, 2013	**1,114.2**	150.0	200.0	764.2
Approved by Business Board on April 8, 2013	**-**	-	-	-
Change of allocation on previously approved projects	**-**	-	-	-
Closing balance at April 30, 2013	**1,114.2**	150.0	200.0	764.2
Unallocated	**285.8**	-	-	285.8

Actual Debt Outstanding	Total in Millions	Internal Component Pension Debt	Internal Component Other Debt	External Component
Opening balance at March 31, 2013				
Debentures due 2031 to 2051	**710.0**			710.0
Other external debt	**12.6**			12.6
Internal debt	**271.5**	106.9	164.6	-
	994.1	106.9	164.6	722.6
Changes	**7.7**	(0.2)	9.5	(1.6)
Closing balance at April 30, 2013	**1,001.8**	106.7	174.1	721.0

Definitions:

Debt includes all long-term external and internal borrowed funds obtained by any means (e.g. debentures, bank loans) and excludes letters and lines of credit and all short-term and medium term internal financing for purposes such as construction financing and fund deficits.

Debt burden ratio, key determinant of debt policy limit, equals interest plus principal divided by total expenditures.

Debt policy limit is the maximum debt that can be taken on based on a debt burden ratio of 5%.

Viability ratio, to be taken into consideration in setting debt policy limit, equals expendable resources divided by debt. The debt strategy has set a preference of a viability ratio of 0.8 or greater.

Allocations include borrowing approved by Business Board, plus contingency for donations targets and pledges.

Actual debt outstanding is the sum of internal loans issued from internal debt plus actual external debt issuance.

Debt Burden Ratio (April 30, 2013)

$$\text{Debt Burden} = \frac{\text{Principal + Interest}}{\text{Total Expenditures}}$$

	(in Millions)			
	External Debt	Internal Pension	Internal other	Ext + Int Debt
Principal Payment	20.6	3.2	8.1	31.9
Interest Payment	38.9	6.5	9.8	55.2
Total Principal & Interest (April 30, 2013)	59.5	9.6	17.9	87.1
Total Expenses (April 30, 2013)	2,390.0	2,390.0	2,390.0	2,390.0
Less Depreciation	(141.2)	(141.2)	(141.2)	(141.2)
Plus Principal payments	20.6	3.2	8.1	31.9
Pension funding in excess of expense	116.1	116.1	116.1	116.1
Total Expenditures at April 30, 2013	2,385.5	2,368.1	2,373.0	2,396.8
Debt Burden Ratios:	**2.5%**	**0.4%**	**0.8%**	**3.7%**

Monitoring Debt Burden + pension special payments (April 30, 2013)

$$\text{Debt Burden} = \frac{\text{Principal + Interest + Special Payments for Pension}}{\text{Total Expenditures}}$$

	(in Millions)			
	External Debt	Internal Pension	Internal other	Ext + Int Debt
Principal Payment	20.6	3.2	8.1	31.9
Interest Payment	38.9	6.5	9.8	55.2
Total Principal & Interest (April 30, 2013)	59.5	9.6	17.9	87.1
Special Payments for Pension		63.0		63.0
Total Principal & Interest (April 30, 2013) + Special	59.5	72.7	17.9	150.1
Total Expenses (April 30, 2013)	2,390.0	2,390.0	2,390.0	2,390.0
Less Depreciation	(141.2)	(141.2)	(141.2)	(141.2)
Plus Principal payments	20.6	3.2	8.1	31.9
Pension expense in excess of funding	116.1	116.1	116.1	116.1
Total Expenditures at April 30, 2013	2,385.5	2,368.1	2,373.0	2,396.8
Debt Burden Ratios:	**2.5%**	**3.0%**	**0.8%**	**6.3%**

Viability Ratio (April 30, 2013)

$$\text{Viability Ratio} = \frac{\text{Expendable resources (see list below)}}{\text{Debt}}$$

	(in Millions)			
	External Debt	Internal Pension	Internal Other	Ext + Int Debt
Expendable resources (April 30, 2013):				
Unrestricted deficit	(129.7)	(129.7)	(129.7)	(129.7)
Internally restriced endowments	247.9	247.9	247.9	247.9
Deferred Contributions	372.7	372.7	372.7	372.7
Internally restricted cash reserves				
Operating fund reserves	485.7	485.7	485.7	485.7
SRA fund	124.3	124.3	124.3	124.3
Pension reserve	2.4	2.4	2.4	2.4
Departmental trust funds	74.1	74.1	74.1	74.1
Alterations and renovation funds	105.9	105.9	105.9	105.9
Other funds	19.1	19.1	19.1	19.1
Internal loan for Pension Funding	(106.7)	(106.7)	(106.7)	(106.7)
Total expendable resources at April 30, 2013	1,195.7	1,195.7	1,195.7	1,195.7

	External Debt	Internal Pension	Internal Other	Ext + Int Debt
Total Debt at April 30, 2013	721.0	106.7	174.1	1,001.8
Viability Ratios	**1.66**	**11.21**	**6.87**	**1.19**

Maximum Debt at 5% Debt Burden Ratio (April 30, 2013)

$$\text{Debt Burden} = \frac{\text{Principal + Interest}}{\text{Total Expenditures}}$$

	(in Millions)	
Total Expenses	2,390.0	
Less Depreciation	(141.2)	
Plus Principal payments	31.9	
Pension expense in excess of funding	116.1	
Total Expenditures	2,396.8	(a)
Debt Burden Ratio of	**5.0%**	(b)
Represents total Principal and Interest at 5% debt burden	119.8	(a) x (b)
Less 12 months of principal + Interest on outstanding debt	(87.9)	
Additional Principal + Interest that UofT can afford	31.9	

Additional debt that UofT can afford assuming that it will be borrowed at an interest rate of 5.5% with equal principal payments over 40 years:

Principal + Interest = Cost of Debt

$$\left(\frac{\text{Debt}}{\text{40 years}}\right) + \left(\text{Debt x 5.5\%}\right) = \text{\$31.9 million}$$

Therefore, additional debt equals to $398.2 million

In Summary:

Additional debt that UofT can afford	398.2
Plus actual outstanding external debt	721.0
Plus actual outstanding internal debt	280.8
Maximum debt that UofT can borrow at 5% debt burden ratio	1,400.0

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

Income Statement
(in millions)

	2013	2012
Net investment income on LTBP investments	13.9	1.5
Interest income from internal loans	30.4	28.1
Fees and amortization of issue costs	(0.2)	(0.2)
Interest payments to bond holders	(37.9)	(32.2)
Change in internally restricted net assets	6.2	(2.8)
Internally restricted net assets, opening balance	(6.0)	(3.2)
Internally restricted net assets, closing balance	0.2	(6.0)

Balance Sheet
(in millions)

	2013	2012
Assets		
LTBP investments	238.7	210.0
Less: LTBP V funds not yet loaned	(108.3)	(110.1)
	130.4	99.9
Unamortized issue costs and premium(prepaid expenses)	1.3	1.3
	131.7	101.2
Liabilities		
Principal collected to date and payable to bondholders on various maturity dates	131.5	107.2
Net assets		
Internally restricted net assets	0.2	(6.0)
	131.7	101.2