Appendix 1

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UNIVERSITY OF TORONTO

UNIVERSITY FUNDS INVESTMENT POLICY

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1. DESCRIPTION OF UNIVERSITY FUNDS

1.1. Long-Term Capital Appreciation Pool (LTCAP)

The LTCAP, formerly known as the Consolidated Investment Pool (CIP), consists of the university's endowed trust funds or other funds of a permanent or long-term nature. In addition, external funds may be invested in the LTCAP including funds of affiliated organizations and funds where the university is a beneficiary.

1.2. Expendable Funds Investment Pool (EFIP)

The EFIP consists of expendable funds, which are pooled for investment purposes until the funds are required for expenditure.

1.3. Specifically Invested Trust Funds

The specifically invested trust funds consist of both endowed and expendable funds which cannot be pooled for investment purposes because of constraints or conditions attached to the funds.

2. LONG-TERM CAPITAL APPRECIATION POOL (LTCAP)

2.1. General Description of the Fund and Governance

The LTCAP represents the pooling of invested assets accumulated by or donated to the University for endowed purposes.

The Governing Council has delegated management of the LTCAP assets to the University of Toronto Asset Management Corporation in accordance with the Service Agreement dated May 1, 2000 between The Governing Council and the University of Toronto Asset Management Corporation (UTAM). The investment decisions of UTAM and its Board of Directors are subject to the overall policy direction of the Business Board as reflected in this policy and in amendments the Board may make from time to time.

3. THE NATURE OF LTCAP LIABILITIES

The LTCAP provides funding to the faculties and departments of the university to be used for endowed purposes in accordance with the terms of each endowment or trust. The LTCAP is subject to the capital preservation policy currently in place and as may be amended from time to time, and as such the distribution and reinvestment rates must be harmonized on an inflation-adjusted basis.

4. INVESTMENT POLICIES AND GOALS OF THE LTCAP

4.1. Investment Policy, Objectives and Risk Tolerance

The University of Toronto has engaged the University of Toronto Asset Management Corporation (UTAM) to manage the LTCAP. As a client of UTAM, it is important that the University delivers to its fund manager a concise statement of return objectives as well as risk tolerance, and that these two components are congruous. The purpose of this policy is to establish both of these objectives with regard to the Long-Term Capital Appreciation Pool (LTCAP).

The purpose of the LTCAP is to provide cash flows that will grow each year at a minimum of the rate of inflation in order to preserve the purchasing power of the fund and provide the same or better level of support for future generations. 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 contribution from endowed assets. In addition, the University's Policy for the Preservation of Capital of Endowment Funds identifies the following:

a) The need to maintain the inflation-adjusted value of endowment capital; and

b) The need to provide a stable flow of expendable income for the purposes of each fund.

4.2. Return Expectations and Risk Tolerance

In order to meet the planned payouts, the return objective is a 4.0% real, inflation-adjusted return over a 10-year period. This return objective is net of all fees and levies. For purposes of this return objective, the level of University levies should be set at 0.4% to 0.5% of assets.

To keep risk at a reasonable level, UTAM shall manage the asset portfolio to achieve a target standard deviation of 10.0% or less in nominal terms.

4.3. Asset Mix

UTAM shall establish the asset mix investment mandates and then select investment managers to be responsible for the management of the portfolios in accordance with those mandates. Funds will normally be allocated to external managers in accordance with those mandates. Funds will normally be allocated to external managers, or when determined to be advantageous, may be allocated to internal management.

Performance benchmarks against market indices and peer universes will be established for the fund. The details of these benchmarks will be described in the service agreement between the University and UTAM. Portfolio diversification, categories and subcategories of investments, use of derivatives, and investment restrictions will be accountabilities of UTAM and a requirement that UTAM develop, approve and review these policies will be incorporated into the service agreement between the University and UTAM.

Each investment manager shall adhere to this policy and shall follow the investment policies and goals with the care, diligence and skill that a person of ordinary prudence would use in dealing with the property of another and shall use all relevant knowledge and skill that the investment manager possesses or ought to possess. Investment managers are expected to be in compliance with the standards of professional conduct and code of ethics established by the Association for Investment Management and Research (AIMR).

5. EXPENDABLE FUNDS INVESTMENT POOL (EFIP)

5.1. Investment Policy, Risk Tolerance and Objectives

While the purpose of EFIP is to pool for investment purposes capital that is predominately short term in nature, trend-line growth of the capital base over the past several years has created a substantial core balance that is expected to be sustained on an on-going basis. Therefore, a risk profile that is greater than what would be expected for funds with a short-term investment horizon is appropriate for a significant portion of the fund.

5.1.1. Short-Term Funds

The cash equivalent portion of EFIP must be maintained in assets with a duration comparable to 91-Day T-bills recognizing that these funds may be used immediately or sometime within a twelve month time horizon. An analysis of past cash flow patterns indicates that maintaining approximately 15% of the average balance of the total pool over a one year operating cycle in cash or cash equivalents is sufficient to meet short-term demands.

In order to further ensure that adequate liquidity is available, approximately 25% of the market value of EFIP at the peak of its annual cycle in September shall be invested in short-term bonds. Individual securities in the short-term bond component must have a minimum of an “A” rating. The total short-term bond component shall have a duration in the range of 1.5 to 4 years.

5.1.2. Long-Term Core Funds

EFIP may invest approximately 30% of the market value of EFIP as measured at the peak of its annual cycle in September of each year in the LTCAP. While the LTCAP provides an appropriate investment pool for long-term funds, there must be a high degree of certainty that EFIP funds invested in the LTCAP would never require an urgent, unplanned or significant liquidation in a period of less than five years. The five year investment horizon in important, in that it is generally considered the minimum investment horizon required for investments in the equity markets. Withdrawals of EFIP balances invested in the LTCAP will be limited to $25 million in any given year and any withdrawal in excess of this amount must be mutually agreed upon by the University of Toronto Asset Management Corporation and the Chief Financial Officer of the University of Toronto. The purpose of this investment is to provide for a higher rate of return and avoid the opportunity cost associated with holding large cash and cash equivalent balances.

Additionally, up to 30% of the market value of EFIP as measured at the peak of its annual cycle in September of each year may be invested in diversified equity accounts, pooled funds, exchange-traded funds or equivalents, absolute return strategies or market neutral strategies, or equivalent exposure through synthetic products. While it is recognized that there is a very low probability that these funds will need to be liquidated in any given operating budget cycle, this structure enables the ability to provide liquidity without adversely impacting the value of the LTCAP.

The purpose of this investment is to provide for a higher rate of return and avoid the lost potential returns associated with holding large cash and cash equivalent balances, while providing a structure that enables the generation of liquidity for re-balancing purposes of adjusting exposure back to appropriate levels.

5.2. Performance Benchmarks and Rate of Return Objectives

Performance benchmarks against market indices and peer universes will be established for the fund and its components. The details of these benchmarks will be described in the service agreement between the University and UTAM.

5.3. Variation on the investment policy for the expendable funds investment pool for a period to end no later than April 30, 2008

This section provides a time-limited variation on the investment policy for the expendable funds investment pool by giving the Vice-President, Business Affairs the following authority for a period of about five years, up to April 30, 2008:

a) to reduce the average annual short-term portion to the extent appropriate to meet current short-term cash flow requirements and to allow a somewhat larger proportion of funds to be invested long term;
b) to use swaps or other suitable means to convert some or all of the current long-term investments to fixed income for that portion of the expendable funds investment pool which is to be invested long-term and to make other long-term investments in fixed income to manage the pool's exposure to equities.

6. Specifically Invested Trust Funds

The assets of Specifically Invested Trust Funds shall be invested to achieve the maximum total rate of return through a combination of capital appreciation and current income consistent with any liquidity or other constraint specified and subject to any consultation required by contractual agreement, or by condition of the estate, or administrative arrangement.

7. General

7.1. Conflict of Interest Guidelines

Anyone involved directly or indirectly with the University's fund investments shall immediately disclose, at the time of its discussion of the policy or of matters related to the investment of University funds, 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 fiduciary responsibility to act in the best interests of the funds.

7.2. Custody

Custody requirements will be an accountability of UTAM and a requirement that UTAM develop, approve and review these requirements will be incorporated into the service agreement between the University and UTAM.

7.3. Policy Review

This statement shall be reviewed at least once a year and either confirmed or amended as necessary.

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Felix P. Chee
Vice-President, Business Affairs
March 2003