THE UNIVERSITY OF TORONTO

THE GOVERNING COUNCIL

**REPORT NUMBER 132 OF THE BUSINESS BOARD**

**March 1, 2004**

To the Governing Council,
University of Toronto

Your Board reports that it met on Monday, March 1, 2004 at 5:00 pm in the Council Chamber, Simcoe Hall, with the following members present:

Ms Jacqueline C. Orange (In the Chair)
Mr. John F. (Jack) Petch, Vice-Chair
Dr. Thomas H. Simpson, Chair of the Governing Council
Professor Robert J. Birgeneau, President
Ms. Catherine J. Riggall, Interim Vice-President, Business Affairs
Professor Angela Hildyard, Vice-President, Human Resources and Equity
Ms Dominique Barker
Mr. Bruce G. Cameron
Dr. Claude S. Davis
Ms Mary Anne Elliott
Ms Susan Eng
Ms Françoise Dulcinea E. Ko
Ms Karen Lewis
Mr. George E. Myhal
Dr. John P. Nestor
Mr. Richard Nunn
Mr. Roger P. Parkinson
Mr. Timothy Reid
Professor Arthur S. Ripstein
Mr. Amir Shalaby
Professor Jake J. Thiessen

Mr. John Bisanti, Chief Capital Projects Officer
Ms Sheila Brown, Acting Chief Financial Officer
Dr. Jon S. Dellandrea, Vice-President and Chief Advancement Officer
Professor Vivek Goel, Interim Vice-President and Provost
Professor Ian Orchard, Vice-President and Principal, University of Toronto at Mississauga
Ms Christina Sass-Kortsak, Assistant Vice-President, Human Resources
Professor Ronald D. Venter, Vice-Provost, Space and Facilities Planning
Professor Safwat Zaky, Vice-Provost, Planning and Budget

Secretariat:

Mr. Neil Dobbs
Ms Susan Girard

**Regrets**:

Mr. Donald A. Burwash
Dr. Alice Dong
Dr. Paul V. Godfrey
Mr. Gerald A. Lokash
Ms Kim McLean
Dr. Susan M. Scace
Mr. Robert S. Weiss

**In Attendance**:

Mr. David Peterson, member, the Governing Council
Mr. Felix P. Chee, President and Chief Executive Officer, University of Toronto Asset Management Corporation
Mr. Andrew Drummond, Assistant Secretary of the Governing Council
Ms. Rivi Frankle, Assistant Vice-President, Alumni and Development
Ms Carole Moore, Chief Librarian
Mr. Allan Shapira, Hewitt Associates

ALL ITEMS ARE REPORTED FOR INFORMATION

**1. Report of the Previous Meeting**

Report Number 131 (January 19, 2004) was approved.

**2. Business Arising from the Report of the Previous Meeting**

The Chair reported that the Board's recommendation concerning the Health and Safety Policy had been deferred by the Executive Committee. A member of that Committee had requested assurance that the proposed policy had been amended pursuant to suggestions made at the Business Board. Another member had sought further information about the consultative process and the applicability of the policy to safety in field research. Professor Hildyard reported that the Business Board member's suggestion had been incorporated into the policy placed before the Executive Committee. Discussions had taken place with the member who had raised the other questions, and Professor Hildyard would be ready to report at the Executive Committee meeting on March 12.

**3. Vice-President, Human Resources and Equity: Annual Report, 2003**

Professor Hildyard highlighted her report by means of a PowerPoint presentation. She concentrated on aspects of Human Resources services that were of particular importance in the current academic planning process.

- There were over 11,000 staff-appointed and casual staff who worked in 194 buildings across three campuses. They were represented by the Faculty Association, three staff groups and 23 unions.

- Human Resources services were provided by 44 staff members in the central offices and another 57 staff in the divisional offices.

- There were a number of goals related to the Human Resources portfolio in *Stepping UP* including the appointment, tenure and retention of the best faculty, becoming the employer of choice for the staff, and ensuring strong academic and professional managerial leadership.

- For the faculty, Human Resources would assist in developing: programs to make the University an employer of choice, options for employment relationships at all stages of a career, and a culture of academic leadership.

- For staff, Human Resources would provide opportunities for acquiring new skills and education, create career trajectories to increasingly responsible positions, foster mutual respect between administrators and staff, and retain and recruit the best staff.

## 3. Vice-President, Human Resources and Equity: Annual Report, 2003 (Cont'd)

- Recent developments in Human Resources included the hiring of a new Assistant Vice-President, a new child care policy, a new Health and Wellbeing Unit, a course for Human Resources personnel on "academic life 101", and the launching of an employee on-line self-serve program.

- Specific initiatives for faculty included a family-care office, relocation assistance for new faculty, aid with spousal employment opportunities to help attract new faculty, reviews of mandatory retirement issues and health benefit issues, and professional development programs.

- For managerial and professional staff, new performance and job evaluation tools had been created, as well as new compensation and professional development programs.

- For unionized staff, there was an increased level of consultation, new job evaluation initiatives and professional development programs.

- The challenges for 2004 included reaching a first collective agreement with the Canadian Union of Public Employees (CUPE) for stipendiary instructors, renewing agreements for several trades, implementing new job evaluation and compensation policies for professional and managerial staff, developing such policies for confidential staff, improving staff communications, developing a health and well-being initiative and becoming the employer of choice.

In answer to a member's question about the compensation scheme for professional and managerial staff, Professor Hildyard explained that it would be based on merit. Each staff member would be asked to outline objectives and would be evaluated on whether they had been met. There would be a bonus scheme for those who went beyond the expected high level of service. She said that policies would be presented to the Board for consideration at the next meeting.

The Chair thanked Professor Hildyard for her report and presentation. The University was a very large and complex organization, and the Human Resources department was increasing its professionalism and developing new initiatives to support the President's vision of a great public teaching and research University.

## 4. Advancement: Fundraising Strategy and Programs: Guidelines

The Chair recalled that last spring, the Board had approved the repeal of a number of out-of-date policies in this portfolio, but it had asked that new guidelines on fundraising strategies be prepared. Those were now before the Board for approval. Dr. Dellandrea explained that the key elements of the new Guidelines were that:

**4. Advancement: Fundraising Strategy and Programs: Guidelines** (Cont'd)

- advancement continue to serve the academic priorities of the University as defined by the academic leadership through the academic planning process and by governance;
- all fundraising programs be fully compliant with relevant policies and guidelines;
- all fundraising programs be organized on a centrally co-ordinated, decentralized basis;
- the four-month holdback on interest earnings only of all donations be continued to offset programs costs;
- donor stewardship continue to be emphasized; and
- high-quality advancement staff be recruited and retained.

In answer to a member's question, Dr. Dellandrea said that the Guidelines were written to clarify the ground rules for advancement staff rather than as a document for donors. The latter's interests were covered in the Provost's Guidelines on Donations and the Provost's Statement on the Role of Advisory Bodies.

A member asked if there were any essential changes from the previous document. Dr. Dellandrea noted that in 1995, the academic planning process was just beginning. This document simplified the process of coordinating advancement activities with academic priorities.

A member posed a situation in which a division sought a multi-million dollar gift from a donor for a project not on the list of priorities. Dr. Dellandrea said that such a situation would not arise. No proposal to seek support could go forward without the Provost's approval and the Vice-President and Chief Advancement Officer was personally responsible for gifts over a million dollars.

A member commented that the previous policy required fundraising to bring in annually an amount equal to 10 percent of the University's operating budget. He noticed that new guidelines had no such stated objective. Dr. Dellandrea confirmed that there was no specific percentage goal in the proposed guidelines. Planning was underway to complete the next $1-billion campaign in the next 10 years.

The President commented that a significant part of the endowment supported student aid. Income from the endowment was about four percent of the operating budget. However, that did not replace the lack of funding increases from the government to compensate for the effects of inflation.

**4. Advancement: Fundraising Strategy and Programs: Guidelines** (Cont'd)

On motion duly moved and seconded,

YOUR BOARD APPROVED

The proposed Guidelines on Fund Raising Strategy and Programs at the University of Toronto, a copy of which is attached hereto as Appendix "A", replacing the Policy Statement on Fundraising Strategy and "Setting Priorities for Raising Private Funds" (both approved by the Business Board on April 17, 1995).

**5. Report on Gifts and Pledges over $250,000, November 1, 2003 to January 31, 2004**

The Board received for information the Report on Gifts and Pledges over $250,000 for the period November 1, 2003 to January 31, 2004.

**6. Financial Situation of the University: Background Briefing, Part IV – Endowments and Ancillary Operations**

Ms Brown displayed the University's income statement from the April 30, 2003 audited financial statements, recalling that revenues of $1,248.3-million were less than expenses of $1,412,7-million, leading to a net loss of $164.4-million for the 2002-03 year. That net loss was made up of three factors: $55.6-million of investment loss, $69.7-million of pension and other employee-future-benefits expense, and $39.1-million of other factors. The objective of this briefing was to help members understand two elements of these financial results: endowments and ancillary operations.

- **Endowments: characteristics**. Endowments were funds in which the original capital was retained in perpetuity, with only the investment earnings being spent. At the University of Toronto, there were several thousand individual endowments, each managed separately to serve their particular purposes. Almost all of those endowment funds were, however, managed together for investment purposes in the Long-Term Capital Appreciation Pool (L.T.CAP), a unitized pool that could be likened to a mutual fund for the individual endowment funds.

- **Value and purposes of endowments**. As at April 30, 2003, the University's endowments were valued at $1,062.3-million. They included endowments in support of the following purposes: chairs and professorships, $314.4-million; student aid, $427.3-million; academic programs, $143.8-million, and research, $176.8-million.

- **Preserving the capital value of the endowments and endowment spending**. The key issue in the financial management of the endowments was achieving the right balance between (a) the need to provide sufficient current income from the funds to support their

6. **Financial Situation of the University: Background Briefing, Part IV – Endowments and Ancillary Operations** (Cont'd)

purposes, and (b) the need to preserve the real value of the funds so that they could provide sufficient income to support their purposes indefinitely into the future. Achieving that balance required balancing the investment earnings to be sought with an appropriate level of risk to ensure the long-term preservation of the capital. This also required an annual allocation for spending that was less than the long-term investment earnings target, with the remainder of the earnings being reinvested to preserve the value of the endowments against erosion by inflation.

Until 2003-04, the University had paid out to the beneficiaries of the endowments 5% of the average value of the units in the L.T.CAP over the previous 48 months. The final payout under this system had been made on April 30, 2002, amounting to $9.36 per L.T.CAP unit, for a total payout of $57-million. To achieve that payout policy, the University had sought a real investment return of 5.0%, that is a nominal return of 5.0% plus the increase in the Consumer Price Index. While the risk tolerance required to achieve that payout rate had not been articulated quantitatively, it had been implied through the L.T.CAP's asset mix of 80% equities and 20% fixed-income securities.

Beginning in the 2003-04 budget year, the endowment payout had been reduced, also enabling the University to reduce the risk to be assumed in investing the endowment funds. The objective remained to preserve the inflation-adjusted value of the endowment capital. To do so the payout would be about 4% of the baseline market value of the L.T.CAP units, which would be changed with inflation. The payout each year would be within a corridor of at least 3% of the baseline market value and no more than 5%, with one-time-only adjustments to the payout made to remain within the corridor. Under the new policy, the payout as at April 30, 2003 had been $6.60 per unit for a total payout of $43-million. This change in the payout policy had allowed a reduction in the investment-return objective to a real return of 4.0% (a nominal return of 4.0% plus the increase in the Consumer Price Index). The risk tolerance expressed in the investment policy was an average standard deviation over ten years not to exceed 10.0%. Responsibility for selecting an appropriate asset mix to achieve the return objective within the risk tolerance was delegated to the University of Toronto Asset Management Corporation (UTAM).

Ms Brown displayed a graphical analysis of the payout and preservation-of-capital history of the entire endowment pool from 1992, with projections continuing to 2010, based on the new payout and investment policies. In the strong markets continuing until the spring of 2000, the investment return on the endowment had been more than sufficient to cover the payout, and the amount reinvested had been more than sufficient to preserve the value of the endowment against inflation. In the poor market conditions that followed, however, that cushion had evaporated rapidly, with the value of the endowment as at April 30, 2003 falling just below the cumulative value of the capital adjusted for inflation. With the new payout policy and improved investment markets,

6. **Financial Situation of the University: Background Briefing, Part IV – Endowments and Ancillary Operations** (Cont'd)

it appeared that the planned payout of $6.73 per unit on April 30, 2004 would leave sufficient capital to deal with the effects of the 2% rate of inflation.

- **Endowment restrictions**. Whether donations could be spent or whether they were to be placed in an endowment was often specified by the donor. That was an important fact for accounting purposes, because a different accounting treatment was given to the endowment funds (a) where the donor had specified that the donation be an endowment and (b) where the Governing Council had decided to place donations and other funds into endowment. (In addition, of course, the specific purpose of the spending from the endowment income might or might not be specified by a donor.) The University's income statement reflected only investment income or losses on internally restricted endowment funds. For investment income or loss on funds specified by donors as endowments ("externally restricted endowments"), the outcome was treated only as an addition to or reduction of the University's assets and capital on its balance sheet. Similarly, the externally restricted endowment donations themselves were not accounted for as income on the income statement; they were direct additions to the assets and capital on the balance sheet. This accounting treatment was specified by the Canadian Institute of Chartered Accountants' Generally Accepted Accounting Principles (GAAP) for non-for-profit organizations.

  Ms Brown illustrated this accounting treatment for the April 30, 2003 financial statements. Realized and unrealized investment losses on the endowment for the 2002-03 year had amounted to $142.5-million, arising from the downturn in the markets during the year. An amount of $43.0-million had been allocated for spending. The outcome was a negative re-investment amount, or a decline in the value of the endowment, of $185.5-million. The income statement recorded a loss of $30.7-million on internally restricted endowments. This was 20% of the investment loss, representing the 20% of the endowments that were internally restricted. The rest of the decline was recorded only on the balance sheet, in the section reporting the University's capital. The balance sheet showed a loss of $111.8-million on externally restricted endowments, which was 80% of the loss, reflecting the 80% of the endowments that were externally restricted. This section also showed the decline of $43.0-million in the value of the endowment arising from the year's allocation for spending.

- **Ancillary operations**. Members of the Board would be familiar with the business ancillary operations: the real estate division, the University of Toronto Press, the University of Toronto Innovations Foundation, the University of Toronto Asset Management Corporation and the newest ancillary operation, the University of Toronto Schools. Members would be less familiar with the service ancillaries, which reported to the University Affairs Board. There were the various residence operations, the food and beverage services, the conference services, the parking operations and Hart House. All of those ancillaries operated like businesses, with the objective of at least breaking even

6. **Financial Situation of the University: Background Briefing, Part IV – Endowments and Ancillary Operations** (Cont'd)

after reflecting all costs. It was interesting that certain other university operations that were similar were not designated as ancillaries, for example the extra-curricular athletics operations.

The ancillary operations' financial planning and financial statements followed principles appropriate for businesses. For example, the financial statements of the incorporated ancillaries had always recorded an expense for depreciation – something the University's financial statements had only begun to do in 1998. The operations were required to pay for overhead costs. They had multi-year operating and capital budgets, updating those budgets and long-term budget projections annually. They developed reserves for operations and capital renewal, and they had little or no deferred maintenance.

- **Ancillary operations: key issues**. The service ancillaries were struggling with the effects of the University's large-scale enrolment growth. To deal with enrolment increases, they had undertaken new construction or major maintenance and renewal projects, and they were struggling to absorb the costs of those projects, often budgeting losses for the next few years. On the St. George Campus, the residence ancillaries were dealing with a soft housing market, which had given rise to problems filling residence beds and achieving projected rate increases. On the other hand, the residence operations at Mississauga and Scarborough were facing real problems to meet the demand for student housing.

  The issues faced by the business ancillaries were different from the service ancillaries. They too were required to break even. The University of Toronto Press operated in low-margin businesses, sometimes with obsolete equipment. The University of Toronto Innovations Foundation had to recover its costs from earnings derived from royalties or equity stakes in companies developing University inventions. It hoped to benefit, as had some other technology-transfer operations, from a "gusher" – an invention that would provide a very large source of income.

- **Ancillary operations: financial position and results**. While the University's financial statements were now unified, the University did still maintain its system of fund accounting, accounting separately for the operating fund, the capital fund, the restricted fund group and the ancillary operations. Ms Brown displayed the assets, liabilities and capital of the ancillary operations fund for the fiscal years from 1998 to 2003. The assets and liabilities had grown dramatically, reflecting the construction of new facilities such as parking garages and residence buildings and the debt incurred for that construction.

  With respect to revenues and expenses, the ancillary operations as a whole had been succeeding in earning sufficient revenues to cover their expenses, yielding a very small net income. The projection for the current year, however, was for a small net loss, with the service ancillaries struggling with (a) the costs of the early years of debt service for their new construction, and (b) the additional operating costs for their new facilities.

6. **Financial Situation of the University: Background Briefing, Part IV – Endowments and Ancillary Operations** (Cont'd)

In response to a question, Ms Brown said that the service ancillary operations did not, in general, pay rent for their land or other facilities, but they did cover their operating, maintenance and capital-renewal costs. The parking ancillary on the St. George Campus had until 2001-02 made a transfer to the operating budget, representing an imputed ground rent, but the operation had then had to deal with borrowing costs associated with a new facility and had been unable to continue to make the transfer.

Ms Brown displayed the current year's surplus or deficit for the ancillary operations group, showing the effects of transfers, largely to reserves for future capital needs, which had been made in five of the past six years.

Finally, looking at the University's income statement for the year ended April 30, 2003, the results of the ancillary operations group had reduced the University's net loss by $1.3-million.

In response to a member's question, Ms Brown said that about $300-million of the planned $620-million debt in the capital projects report was attributable to the ancillary operations. The President observed that the ancillary operations had achieved real success in completing so many new buildings to accommodate the sudden enrolment expansion arising from the double cohort. That was a real tribute to Professor Venter, Mr. Chee, Mr. Bisanti, Ms Brown, Ms Riggall and colleagues in the Business Affairs portfolio and in the academic divisions.

Among the matters that arose in discussion were the following.

**(a) Accounting for investment returns on endowment funds**. Ms Brown shared a member's concern that the requirement for different accounting for investment returns on externally and internally restricted endowment funds could sometimes be misleading. In many cases, the dichotomy was a false one. For example, the University had established one of the major endowments – the Connaught Fund – from the proceeds of the sale of the Connaught Laboratories, the original maker of insulin. Nonetheless, the endowment of the funds and the use of the income to support research represented a trust arrangement. Another member was concerned that in years such as 2003 when the endowment fund incurred an investment loss, the financial statements did not fully reflect that loss, with the majority of the loss not being recorded on the income statement. That could, for example, impede the University's efforts to make its financial results clear as part of its efforts to seek greater public funding. It could also lead to an unrealistic picture of the University's financial results internally, risking calls for greater spending than appropriate given the extent of investment losses. Ms Brown understood the member's concern. With respect to external readers, including government, the accounting rules applied to all not-for-profit institutions in Canada, and government officials would therefore be able to understand the University's investment results. With respect to University readers of the financial statements, she agreed that it was particularly important that they have a realistic understanding by looking at the income statement and the balance sheet together. The

**6. Financial Situation of the University: Background Briefing, Part IV – Endowments and Ancillary Operations** (Cont'd)

member stressed that this realistic understanding was particularly important in the decision-making about payouts from the endowment and reinvesting earnings to maintain its value against erosion from the earlier investment losses and inflation. The Chair suggested that this matter be addressed specifically at the next meeting in the briefing on operating planning and budgeting.

**(b) Donor support of endowments**. In response to a member's question, Ms Brown and Ms Frankle said that about 60% of donations supported endowments, with the remaining 40% providing expendable funds, including funds for expenditure on capital projects.

**7. Investments: Pension Fund Master Trust Investment Policy**

Ms Riggall proposed approval of the revised Pension Fund Master Trust Investment Policy.

- **Form of the Statement of Investment Policies and Procedures**. The Pension Fund Master Trust Investment Policy currently in place had been approved by the Business Board on April 7, 2003. That single document was an appropriate one for the period before the clarification of the details of the relationship between the Governing Council of the University, which was plan sponsor and administrator, and the University of Toronto Asset Management Corporation (UTAM), the investment manager for the Pension Fund Master Trust (the pension fund). The new statement of investment policy and procedures consisted of three documents, which reflected the division of responsibility between UTAM as the investment manager and the Governing Council, as its client. The three documents included: (a) the proposed University Pension Fund Master Trust Investment Policy, which was before the Board for specific approval, (b) the Service agreement with UTAM, which had been approved in April 7, 2003, with Schedule "C" containing the revised performance benchmarks approved on November 12, 2003; and (c) the UTAM Pension Fund Master Trust Investment Policy, which had been approved by the UTAM Board on February 16, 2004. The Business Board was also being asked to approve that group of documents which, taken together, would represent the pension fund's statement of investment policy and goals, as required by the regulatory authorities. The key change in this new way of handling this approval was that the Governing Council would specify the return expectation and risk tolerance and act on the basis of UTAM's advice in approving the asset mix and other investment matters.

- **Return expectation and risk tolerance**. A review of the liability of the pension plans had revealed that it would be appropriate for the Pension Fund Master Trust to have the same return objective and risk tolerance as the University's endowment: a real (after-inflation) return of 4% per year and a standard deviation of 10% or less over ten-year periods. In previous versions of the policy, three return objectives had been stated: the achievement of a real return of 4% per year, performance exceeding that of a composite

**7. Investments: Pension Fund Master Trust Investment Policy** (Cont'd)

benchmark of securities indices, and performance exceeding that of the median fund of an appropriate performance-measurement service. Risk had been expressed as that acceptable to a prudent person, but no quantitative risk tolerance had been stated. With the proposed new University policy having specified the return objective and risk tolerance, the rest was left to the UTAM policy.

- **Other changes to the University policy**. The policy clearly delegated responsibility for asset mix to UTAM. It also delegated to UTAM other elements of investment strategy such as the categories of investments to be used, the voting of proxies, and the use of securities lending, if appropriate. The proposed policy contained expanded conflict-of-interest provisions. It added rules governing related-party transactions. It added a statement of responsibilities of the external fund managers and other external professionals such as the actuaries and the custodians.

- **Asset-mix changes**. In the previous policy, the University had specified the asset mix: 60% equities and 40% fixed-income securities. In the new arrangement, UTAM decided the asset mix, which was specified in the UTAM policy as follows:

| | | |
|---|---|---|
| Equities (40%) | | |
| Canadian | 10% | |
| U.S. | 15% | |
| Non-North American | 15% | |
| Fixed income (30%) | | |
| Universe | 10% | |
| Long bonds | 10% | |
| Real-return bonds | 10% | |
| Alternatives (30%) | | |
| Real assets | 10% | |
| Private equity | 10% | |
| Absolute return | 10% | |
| Total | | 100% |

- **Foreign content**. Both the old and the proposed new policies, of course, adhered to the requirement of the Income Tax Act, restricting foreign content to 30% of the book value of the pension fund's assets. The proposed new policy also stated that the actual foreign content exposure might exceed 30%. Using structures that complied with all relevant legal and Income Tax Act requirements, actual foreign content exposure might range up to about 50%. The objective was to seek the better returns available in the 97% of world equities from markets outside of Canada.

Among the matters that arose in discussion were the following.

**(a) Alternative investments**. Mr. Chee was invited to respond to a number of questions about investments other than those in publicly traded securities. For private-equity investments,

**7. Investments: Pension Fund Master Trust Investment Policy** (Cont'd)

UTAM selected private-equity funds. It did not make direct investments. UTAM was not large enough to make direct investments. It had only one managing director to oversee investments in this very labour-intensive area. Real assets would include investments in real estate and in oil and gas production and timberland. Currently, all private-equity and real-asset investments required review and approval by the UTAM Board. UTAM was currently developing a protocol for such investments, which would limit them to externally managed funds.

Mr. Chee said that UTAM did invest in absolute-return hedge funds, although the level of such investments in the pension fund had not yet been brought up to the benchmark weight of 10%. He personally was responsible for overseeing such investments. While UTAM did currently hold investments directly in a number of hedge funds, future investments would be limited to funds of hedge funds.

In response to a question, Mr. Chee said that UTAM did not invest directly in income trusts as alternative assets. Rather, they were regarded as publicly traded equity investments, and the external equity managers were free to include them in their portfolios.

A member asked whether the 30% to be invested in alternative asset classes (private equity, real assets and absolute-return hedge funds) represented a departure. Was it appropriate to restrict such investments? Mr. Chee responded that investing 30% in alternative asset classes was not now atypical. Major pension funds such as the Ontario Teachers' Pension Fund and the Ontario Municipal Employees Retirement System (OMERS) were moving more and more into this area. He did not see the need to restrict such investments in the policy. The University had been investing in hedge funds for some time, but those investments had formed part of the equity category rather than being identified as a separate asset class.

A member observed that the major pension plans in Ontario were investing increasingly in infrastructure projects. Were such investments included in UTAM's asset mix for alternative asset classes? Mr. Chee replied that he would very much like to include such investments in the pension fund. However, the $2-billion fund could not make direct investments comparable to those of the Ontario Teachers' Pension Plan, for example, with its assets of nearly $70-billion. Such investments represented bets on the outcome of individual projects, which could safely form only a small proportion of the total investments of a fund. Therefore, UTAM would have to participate in such investments as one of several investors in private equity funds, if such investments were made by the external managers of those funds.

**(b) In-house and external management**. UTAM did manage fixed-income portfolios in house – a capacity that it had developed only about one year ago. UTAM relied on external portfolio managers for all other investments. UTAM's role was to actively manage the overall funds.

**(c) Establishment of risk tolerance**. In response to a member's question, Mr. Chee said that the risk tolerance was the outcome of a study of the liability of the pension plan. The objective was to select an asset mix that would provide the best possible return within an acceptable level of risk. That included an acceptable level of loss in any given year as well as a long-term loss of

**7. Investments: Pension Fund Master Trust Investment Policy** (Cont'd)

purchasing power. The study had been completed in conjunction with the University's actuaries, and the outcome translated into the conclusion expressed in the proposed policy: a real return objective of 4% per year with a maximum average volatility over ten years of 10%. This referred to the fund as a whole and not to individual asset classes, where long-term returns and volatility would be expected to be greater in some asset classes (such as equities) and less in others (such as fixed income).

**(d) Foreign investments**. A member of the Governing Council referred to the expectation that, with the aid of structures that complied with legal and tax requirements, "actual foreign content exposure may range up to about 50%." He questioned whether it was advisable for UTAM to lock itself into so high a proportion of foreign investments and foreign currency exposure. Would more flexibility be appropriate? Mr. Chee replied that UTAM management had discretion to move to 5% of total assets above or below the benchmark weight for any asset category. That discretion was not, however, used to make bets on particular markets. Rather, it was used as a guide to provide flexibility in timing the rebalancing the portfolio to move it back to the benchmark weight. Currency exposure was actively managed by an external currency-hedging manager, who had been successful in protecting the University's funds from a substantial part of the effect of the recent decline in the U.S. dollar. Mr. Chee did agree that currency exposure was a major issue.

**(e) Determination of asset mix**. In response to a question, Mr. Chee said that the Governing Council, as pension plan sponsor and administrator, determined, through the proposed policy, the expected rate of return and the risk tolerance for the pension fund and then delegated to UTAM responsibility for determining an asset mix that would achieve the necessary rate of return within the stated risk parameters. The asset mix adopted in the UTAM policy was in its general outline similar to a traditional balanced fund, but included more sophisticated or "new wave" sub-categories of investments. A traditional balanced fund would include 50% equities and 50% bonds. The UTAM asset mix included 40% publicly traded equities plus 10% private equity investments. On the side comparable to the traditional 50% fixed income, the UTAM asset mix included 30% bonds, including 10% real-return bonds, but it also included 10% in real-asset investments and 10% in absolute-return hedge funds. The latter categories produced steady income streams like bonds but those returns tended to be somewhat better than bonds and the valuations of those instruments tended not to be correlated with those of the fixed-income market, reducing overall volatility.

**(f) Actuarial assumptions concerning plan liability and investment rate of return**. Invited to respond to a member's question, Mr. Shapira said that the rate-of-return assumption in the actuarial valuation and in the investment policy (4% plus inflation) were consistent with the discount rate used to determine the liability of the plans – the present value of the stream of payments that the plans would be required to make to pensioners.

## 7. Investments: Pension Fund Master Trust Investment Policy (Cont'd)

On motion duly moved and seconded,

YOUR BOARD APPROVED

(a) The proposed University of Toronto Pension Fund Master Trust Investment Policy, a copy of which is attached hereto as Appendix "B"; and

(b) Taken together,

(i) the proposed University of Toronto Pension Fund Master Trust Investment Policy,
(ii) the University of Toronto Asset Management Corporation Pension Fund Master Trust Investment Policy, a copy of which is attached hereto as Appendix "C", and
(iii) the Amended and Restated Service and UTAM Personnel Agreement made as of the 14th Day of May, 2003, including the amended Schedule C approved by the Business Board on January 19, 2004,

as the University of Toronto's Pension Fund Master Trust Statement of Investment Policies and Procedures, replacing the University of Toronto Pension Fund Master Trust Investment Policy (Statement of Investment Policies and Goals) approved by the Business Board on April 7, 2003.

## 8. Capital Projects Report

Mr. Bisanti reported the changes that had taken place in the capital projects report since the previous meeting. He explained that originally $8-million had been set aside in the University's $620-million borrowing capacity for phase 2 of the Economics building. However, the plan for the Economics building called for phase 2 to be funded entirely from fundraising efforts. Plans were to proceed with phase 1 now and to postpone phase 2 indefinitely. This freed up $8 million in the borrowed funds. It was proposed that the Library Storage Facility proceed using this financing. During his remarks, Mr. Bisanti commented that the administration saw the $620-million as a guideline and not as an exact limit on the borrowing capacity of the University.

## 9. Capital Project: Downsview: Library Storage Facility

Mr. Bisanti introduced Ms Carole Moore, the Chief Librarian, who was present for this item. He said that the Library had a current backlog of about one million volumes waiting for shelving. By 2020, that number could reach five million. It was proposed that a storage facility be built in phases, with the first phase accommodating two million volumes with additional

**9. Capital Project: Downsview: Library Storage Facility** (Cont'd)

phases being constructed every four or five years. He reported that a number of alternatives had been considered including purchases of old warehouses. The proposal before the Board was the best solution and it had been recommended for approval by the Planning and Budget Committee. It was proposed that it be built at Downsview near the Institute for Aerospace Studies and the University of Toronto Press facilities.

Several members suggested that the University might consider moving the facilities on the Downsview land and selling the land at a considerable profit. Professor Goel noted that land on the three campuses was not unlimited. The administration had considered building the storage facility at UTM or UTSC but there was insufficient space. It had also considered buying land for the warehouse but since there was land available at Downsview and there was no plan to sell that land, Downsview was considered the best solution.

A member asked how a change in the priority for the project had occurred. She noticed that the storage facility had been quite far down the list of projects and now it was recommended to proceed. Professor Venter said that *all* projects on the capital plan had the approval of the Provost as being consistent with the academic plan and having a high academic priority. That this project appeared on section 3 of the plan simply indicated that it had not yet received governance approval to proceed.

The member asked whether the University had to keep the volumes in specially climate controlled facilities. Was electronic storage not becoming a preferred option? Ms Moore said that the current plan was to continue to build the collections and to maintain the Library's pre-eminent position in North America. An electronic copy of a document was not a preservation copy since the long-term viability of any electronic process was not known. The University proposed to use the same configuration as employed at Harvard University. That University currently had eight modules. It was the most cost effective way of proceeding. There were 5-million volumes in Robarts Library which had been built to house 4.2-million. In response to a question about the operation of the proposed facility, Professor Venter said that the facility would have shelving 27 feet high and use mezzanine walkways; greater efficiencies were achievable with the increased height (and volume). Books would be stored in bins of predefined size and retrieved manually by library staff; non-library staff would not be allowed on the floor. Robotic aids had been considered and discarded as too expensive to acquire and maintain.

A member commented that if the University spent $1 million on design and determined that the project would cost more than planned, the University might be forced into proceeding although the cost of the project would exceed the $620-million borrowing capacity limit or guideline as termed by Mr. Bisanti. He asked whether the University would abandon the $620-million limit. Ms Riggall said that there would be a review of the $620-million figure because of the large demand for capital construction. The review would look at everything including raising the limit, selling assets, and fundraising potential. Up to $40-million of the borrowing capacity might not be required if fundraising efforts were to succeed in raising the full amount of donations projected for projects included in the report. That $40-million amount was included in the borrowing capacity, for reason of prudence, in the event that fundraising efforts

**9. Capital Project: Downsview: Library Storage Facility** (Cont'd)

did not succeed in full and it became necessary to borrow to complete the projects. A member said that the Board would probably spend the full $6-million projected cost of the proposed project. Mr. Chee, who had defined the formula used to estimate the University's borrowing capacity, said that the amount was within the University's ability to handle, but if the number were to be increased, the University should do so in a thorough and circumspect manner.

A member asked if there would be comments from the credit-rating agencies to help the University make the decision about whether to increase the borrowing capacity. Ms Riggall said that the credit agencies rated companies continually. If the University made a decision to take on further debt, the agencies would decide at that time about the credit ratings. In her opinion, a further increase of $20-million would probably not make any difference in the ratings. Ms Brown and several members noted that it was important to have a discussion of the principles surrounding this issue. What level of debt service could the University handle? What credit rating would the University accept? Could it accept a reduction in its credit rating? Ms Brown noted that credit reports were produced yearly and it would be difficult to advance those reports.

A member asked about the ongoing costs of maintaining the current number of volumes. Ms Moore assured the member that the warehouse model was the most cost effective model.

On motion duly moved and seconded,

YOUR BOARD APPROVED

Subject to Governing Council approval of the project and the allocation of operating funding to service the loan for the project,

THAT the Vice-President, Business Affairs be authorized:

(i) to expend up to $1,000,000 for design, site-development and other work to initiate the Library Storage Facility Project on the Downsview Campus, with financing to be amortized from the University's operating budget, and

(ii) to arrange such interim and long-term financing as required for the expenditure of up to $1 million, from either internal or external sources.

**10. Capital Project: University of Toronto at Mississauga - Residences, Phase VIII – Appropriation for Design**

Mr. Bisanti introduced the proposal to expend $300,000 for design fees for a proposed new residence on the Mississauga campus which would contain 418 beds and a dining room, making a meal plan possible. September 2006 was the projected completion date. The funds

**10. Capital Project: University of Toronto at Mississauga - Residences, Phase VIII – Appropriation for Design** (Cont'd)

for the design would come from UTM's operating budget. The cost per bed at $55,000 was expected to be considerably lower than the $78,000 per bed in phase VII construction.

In response to a question, Mr. Bisanti stated that the comparable cost at University College was $92,000 per bed. The difference could be explained by the facts that: (a) the U.C. residence would be a tower; (b) it would be built on a very small footprint with limited access; and (c) it would include an outer cladding required by the City in order to obtain building approval, given the high-profile nature of the site.

A member asked about residence rates. Professor Venter said that the average was about $600 a month for 8 months. Operating costs varied but all residence ancillaries were expected to break even. Mr. Bisanti said that the new residences were expected to break even in year 5 and cumulatively in year 8.

On motion duly moved and seconded,

YOUR BOARD APPROVED

Subject to Governing Council approval in principle of the project,

THAT the Vice-President, Business Affairs be authorized to expend up to $300,000 to initiate the design of Phase VIII of the University of Toronto at Mississauga student residences, using funding provided by the operating budget of the University of Toronto at Mississauga.

**11. Date of Next Meeting**

The Chair reminded members that the next regular meeting was scheduled for Wednesday, April 14, 2004 commencing at 5:00 p.m. in the Council Chamber.

The meeting adjourned at 7:25 p.m.

Secretary

Chair

March 10, 2004

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