FINANCE AND ADMINISTRATION - DEBT POLICY

BOT 6.7

Date of Last Update:
June 25, 2021

Approved By:

- Board of Trustees

Responsible Office:
Office of General Counsel

POLICY STATEMENT

6.7 Debt Policy

1. Purpose - The purpose of this debt policy is to ensure the appropriate mix of funding sources for capital improvements is utilized and to provide guidance on the strategic use of debt as a funding source.

2. Objectives - The objectives of the debt policy include the following:

a. Prudent utilization of debt to provide a low cost source of capital to fund long-term capital investments in order to achieve the University's mission and strategic objectives.

b. Manage the University's overall debt level in order to maintain the highest acceptable credit rating with appropriate access to capital. The minimum acceptable underlying rating for a University issue is the "A" rating categories by a nationally recognized rating organization.

c. Limit risk within the University debt portfolio by balancing the goal of attaining the lowest cost of capital with the goal of managing interest rate risk.

d. Without attempting to "market time" specific transactions, manage outstanding debt over time to achieve a low cost of capital and to take advantage of interest rate cycles and refunding opportunities.

e. Assure projects financed have a feasible plan of repayment and that secondary pledges are utilized prudently.

3. Funding Capital Projects - The University will use the following guidelines in making decisions about financing options and use of debt, although they are not intended to be

all-inclusive:

a. Other sources of funding. In assessing the possible use of debt, other financing and revenue sources will be considered such as: State appropriations/bonds, philanthropy, project-generating revenues, grant revenues, including administration cost reimbursement, expendable reserves, and other sources.

b. Plan of construction and repayment. Every project for financing must have a defined, supportable plan of costs (construction and incremental operating) approved by management.

4. Debt Management Practices

a. Debt Capacity - Debt capacity shall be consistent with the "A" rating categories as assigned by a nationally recognized rating organization. Core financial ratios that are strongly correlated with "A" rated public higher education peers will be monitored to ensure oversight of leverage levels. The three ratios that will be most closely monitored, which are strongly correlated to the rating level, are:

1. Unrestricted Net Assets to Debt
2. Unrestricted Net Assets to Operations
3. Maximum Annual Debt Service to Operations

b. Structure and Maturity - Debt will be structured so as to be consistent with a fair and equitable allocation of costs to current and future beneficiaries or users of the asset(s) being financed with the proceeds of debt.

The amortization and maturity of debt shall be established based on (1) statutory or governmental restrictions, including tax regulations (2) the types of assets financed, and (3) projected availability of cash flows to meet debt service requirements.

Debt shall be issued only for a time period that is consistent with the life of the project for which the debt was issued, generally not to exceed 30 years. Tax-exempt debt must meet the "120 percent of useful life" test set forth in federal tax law. This test requires that weighted average term of tax-exempt borrowings be limited to not more than 120 percent of the estimated usefully life of the asset(s) being financed with the proceeds of the issue. As market dynamics change, maturity structures should be reevaluated. Call features should be structured to provide the highest degree of flexibility relative to cost and to be consistent with market requirements.

Subject to compliance with federal tax law, the use of bullet maturities or balloon principal payments is not precluded by this policy if it can be demonstrated that the

retirement of such bullet maturities or making such balloon principal payments have been adequately and appropriately considered.

c. Fixed and Variable Rate Debt - Variable-rate debt may be used as a component of its debt portfolio in order to:

1. Take advantage of prepayment and restructuring flexibility,

2. Benefit from historically lower average rate interest costs,

3. Provide a "match" (or natural hedge) to the University's short-term liquid investment balances,

4. Enhance the ability to undertake optimal financial structure management,

5. Enhance the ability to undertake risk management strategies, and

6. Potentially provide an economically more attractive funding alternative than cash.

7. While variable rate debt can provide for relatively lower costs of capital than fixed rate debt, variable rate debt also introduces additional risk (including the risk of inability to acquire and maintain required liquidity facilities) and potential volatility with the debt portfolio. The University will seek to manage the debt portfolio over time in a manner that will achieve a range of between 25%-60% of the portfolio in variable rate debt instruments, taking into account the impact of related derivative products. Forty percent (40%) will be considered the neutral portfolio.

The portfolio allocation to variable rate debt will: (1) be analyzed on an after-derivative basis, (2) have an appropriate relationship to short-term liquid assets, and (3) take into consideration rating and other implications. The allocation of variable rate debt may be managed or adjusted through the issuance of new debt or refunding of outstanding debt and through the use of interest rate swaps and other derivative products such as caps and collars.

d. Taxable Debt - The University may use taxable debt for projects that cannot be financed using tax-exempt debt. The University will allocate its capital funding sources in a manner that will minimize the need for taxable debt to keep its cost of borrowing as low as possible.

e. Method of Sale - Bonds shall normally be sold through a "negotiated sale" with the senior underwriter for a specific series of bonds. Notwithstanding, any particular bond issue may be sold through a competitive bidding process rather than a negotiated sale, if

circumstances are such that a competitive sale may produce a more optimal result for the University in the current market conditions. Private placements will be considered for debt issuance where the size is too small or the structure is too complicated or not appropriate for public debt issuance.

f. Bond Insurance and Other Credit Enhancement - Bond insurance and other credit enhancement opportunities (e.g. bank liquidity facilities and letter of credit) may be considered and utilized if they are deemed cost effective and do not place onerous covenants upon the University.

g. Refunding and Restructuring of Debt - Periodic reviews of all outstanding debt will be undertaken to determine refunding opportunities. Refunding will be considered (within federal tax law constraints) if and when there is a net economic benefit of the refunding or the refunding is essential in order to modernize covenants essential to the University's financial or operating position.

h. Derivative Products - Derivatives may take the form of interest rate swaps, options on swaps and other hedging mechanisms such as caps, floors, collars and rate locks. Derivative products can be an important interest rate management tool which, when used properly, can increase the University's financial flexibility, provide opportunities for interest rate savings, alter the pattern of debt service payments, create variable rate exposure, and limit or hedge variable rate payments. It is essential that the character of and risk associated with these transactions be evaluated and clearly understood prior to entering into a debt-related derivative. In connection with the use of swaps and derivative products, the University will adhere to the University's Interest Rate Management Agreements Policy.

i. Bond Proceeds Investment - Bond proceeds shall be invested appropriately to achieve the highest return available under arbitrage limitations while providing appropriate flexibility relative to the University estimated construction schedule. When sizing bond transactions, consideration shall be given to funding on a net basis.

j. Selection of Service Providers - The selection of service providers associated with the individual debt transactions shall be made by the Treasurer.

5. Debt Compliance and Reporting

a. Continuing Disclosure Compliance - The University will meet the ongoing disclosure requirements in accordance with SEC Rule 15c2-12. The University will submit all reporting required with respect to outstanding debt to which such Rule is applicable.

b. Arbitrage Rebate Compliance - The University will comply with arbitrage

requirements on invested tax-exempt bond proceeds. Arbitrage calculations will be performed as needed and rebate payments to be remitted to the IRS periodically as required.