COMMITTEE REPORT

SESSION:

Public ☒
Non-Public ☐

ACTION REQUESTED:

Decision ☐
Discussion/Direction ☐
Information ☒

TO:	**Academic Council**
DATE:	**March 26, 2024**
PRESENTED BY:	**Pamela Onsiong**
SLT LEAD:	**Brad MacIsaac**
SUBJECT:	**NEW – Debt Management Policy**

COMMITTEE MANDATE:

Under the Policy Framework and the University's Act, the Board of Governors has a "duty to consult" on "all academic, research, service and institutional policies".

We are submitting this report and the draft debt management policy to Academic Council to request discussion and comments.

BACKGROUND/CONTEXT & RATIONALE:

The University invests in capital infrastructure that are fundamental to achieving the University's mission as a higher education institution. Since capital projects will require a combination of financing sources, including grants and deferred contributions, internal reserves and external debt, debt is considered a perpetual component of the University's financial structure.

The University currently has a set of debt guidelines which it has complied with since 2016/17 as part of its due diligence and focus on minimizing risk and reducing its cost of capital. We are now formalizing these guidelines with this new Debt Management Policy. This policy will provide a framework for all University's external borrowing and leave the University assuming debt at levels that continue to promote its financial operations and sustainability.

OVERVIEW:

The University has a significant level of debt on its books, attributable to a $220.0M series of debentures which were issued by the University in October 2004 shortly after the university was first established in 2002. The proceeds of this debt issuance were used to finance capital projects including the construction of three academic buildings, a library and related infrastructure.

Since August 2011, 80% of this debenture debt (i.e. $13.5M of the $16.5M annual debt repayment) has been funded through a special grant from the Province. This grant will continue until the maturity of the debentures in October 2034.

In this policy, the University has established guidelines regarding the optimal amount of outstanding debts through the monitoring of the University's financial sustainability or debt ratios. These ratios are derived from the University's audited financial statements and notes, and for management reporting, are **adjusted** to account for the grant funding that is earmarked to service existing University debt.

All new debts must comply with the University's outstanding debt covenants, and such compliance must be documented as part of the Board-approved motion and documentation to apply for and the use of external debt.

Compliance with this policy will ensure consistent and transparent capital debt management. It is also intended to hold the University in good stead as it looks to reduce its cost of capital and its associated risks.

COMPLIANCE WITH POLICY/LEGISLATION:

The proposed policy and procedures comply with generally accepted accounting principles (GAAP) for not-for-profit organizations.

CONSULTATION AND NEXT STEPS:

Presented to:

- ✓ Policy Advisory Committee – Policy Assessment (February 2, 2024)
- Academic Council – Consultation (March 26, 2024)
- Administrative Leadership Team – Consultation (April 9, 2024)
- University on-line Consultation (March 18 – 29, 2024)
- Audit and Finance Committee – Policy Deliberation (April 11, 2024)
- Board of Governors – Policy Approval (April 18, 2024)

SUPPORTING REFERENCE MATERIALS:

- Draft Debt Management Policy

Item	xxx
Framework Category	Legal, Compliance and Governance
Approving Authority	Board of Governors
Policy Owner	Vice-President, Administration
Approval Date	DRAFT FOR APPROVAL
Review Date	
Supersedes	N/A

DEBT MANAGEMENT POLICY

PURPOSE

1. The purpose of this policy is to assist the University in ensuring that debt is used strategically to support the University in achieving its mission. It will increase transparency by creating alignment between use of proceeds and debt issuance, setting out the responsibilities for the approval and reporting of debt and establishing maximum limits on the amount of total external debt.

DEFINITIONS

2. For the purposes of this Policy the following definitions apply:

"Bridge Financing" means short-term or interim financing of a project until such time that permanent financing is obtained.

"Capital projects" means investments in capital assets equal to or in excess of $4.0M and which require Board of Governors approval.

"Debenture" means debt financial instruments issued by the University in October 2004, the proceeds of which were used to finance the original construction of the University.

"Derivative product" means a type of financial contract whose value is derived upon the value of an underlying asset.

"**Expendable Net Assets**" means internally restricted and unrestricted net assets.

"External debt" means the portion of a capital project that is funded by external borrowing, including commercial banks. External debt, including principal and interest, is usually paid in instalments over the term of the debt, and is included as a priority expense in the annual budget cycle.

"**Financial sustainability ratios**" means a set of metrics that measure the University's debt capacity and debt affordability.

"Grants and deferred contributions" means funds received from the Ministry or other granting agencies to cover specific capital projects. These grants are treated as deferred contributions and amortized using the same useful lives as the asset investment.

"Internal Reserves" means reserves arising out of operating surplus that have been approved by the Board of Governors to be internally restricted for specific projects.

"Performance and Liquidity ratios" means financial ratios that track the trends in the University's net earnings and its financial strength and flexibility.

SCOPE AND AUTHORITY

3. Investments in capital infrastructure are fundamental to achieving the University's mission as a higher education institution. Since capital projects will require a combination of financing sources, including grants and deferred contributions, philanthropy, internal reserves and external debt, debt is considered a perpetual component of the University's financial structure.

4. This Policy sets out the general philosophy for use of debt by the University and introduces specific financial metrics to assess overall debt capacity and debt affordability. As the University evaluates future projects in conjunction with its annual operating budgets, the goals and principles outlined in this debt policy will be reflected in these decisions.

5. The Vice-President Administration, or successor thereof, is the Policy Owner and is responsible for overseeing the implementation, administration and interpretation of this Policy.

POLICY

The objective of the Policy is to optimize the strategic use of debt and to manage the overall cost of capital and debt while limiting the level of risk as determined by the University's risk appetite, as set out in the Risk Management Policy. Debt options, e.g. bridge financing, derivative products, long term fixed and variable rate debt, will all be considered to achieve the goal of risk reduction and reduced cost of capital.

6. General

6.1. Borrowing will only occur following the approval of the project by the Board of Governors. Such approval shall be subject to review of a written business case, which includes the total anticipated cost of the project and source(s) of funding for the project.

6.2. The need for external debt is reviewed and informed by the Campus Master Plan and strategic projects as approved by the President and Vice Presidents. External debt calls will be led by the Executive Director, Financial Planning and Reporting under the direction of the Vice President, Administration.

6.3. In determining different debt strategies and instruments, the University will assess its financial position, including its assets, liabilities and unrestricted cash flow, market conditions and impact on the University's adjusted financial ratios.

6.4. The University will manage its overall and any new debt obligations in a manner to maintain or improve the University's credit rating.

7. Establishment of Financial Sustainability Ratios

7.1. The University has established guidelines regarding the optimal amount of outstanding debt through monitoring of the University's financial sustainability ratios. These ratios measure the University's balance sheet resources and annual operations to determine debt capacity and debt affordability. Ratios are derived from the University's financial statements and notes, and are subject to annual reviews by Finance Management and the University's Audit and Finance Committee.

Financial ratios will be adjusted to account for grant funding that is earmarked to service existing University debt. These ratios are defined as:

Ratio 1 – Viability: **Expendable Net Assets-to-Debt Ratio**: this ratio measures **debt capacity.** It determines University balance sheet leverage by comparing expendable net assets to outstanding debt obligations.

Ontario Tech has established a viability ratio of 50%, or 0.5x (times) coverage. This indicates that the University has unrestricted and internally restricted financial resources to cover 50% of its adjusted debt.

Ratio 2 – Affordability: Interest Burden: this ratio determines **debt affordability** as it quantifies the maximum percentage of expenses (excluding amortization of capital assets) dedicated to repaying the University's current debt burden.

Ontario Tech has established a threshold of less than 4.0% of adjusted operating expenses to ensure sufficient funding for interest repayments is available.

Ratio 3 – Affordability: Debt to Revenue: this ratio divides total University debt by the total revenue and reflects the University's ability to manage its debt repayments.

Ontario Tech has established a threshold for debt to revenue of less than 50% which puts the University in a position to handle unforeseen expenses.

7.2. The evaluation of proposed projects will take into consideration their impact on these ratios over time.

7.3. Where the debt ratios do not meet the established targets, management will undertake a more comprehensive review, including the review of other ratios such as the University's performance and liquidity ratios, and provide a report with recommendations to the Board of Governors. This report will include an action plan on how the debt will be brought back to within the target range.

8. Annual Debt Obligations, Compliance and Reporting

8.1. During the University's annual operating budget process, management will incorporate the source of funding for interest and principal payments associated with outstanding debt. The University will fund payments through a combination of provincial grant funding (for the repayment of its debenture debt), and operating funds, exclusive of operating grants.

8.2. All new debt must comply with the University's outstanding debt covenants, and such compliance must be documented as part of the Board-approved motion and documentation to apply for and use external debt.

8.3. Debt ratios will be reviewed at the June Audit and Finance Committee, as part of the year-end review of the University's audited financial statements and financial ratios.

MONITORING AND REVIEW

9. This Debt Management Policy will be reviewed as necessary and at least every three years. The Vice-President, Administration, or successor thereof, is responsible to monitor and review this Policy.

RELATED POLICIES, PROCEDURES & DOCUMENTS

10. Contract Management Policy

Signing Authority Policy

Expenditure Signing Authority Procedures

Naming of Physical University Assets Policy

Gift Acceptance Policy

Gift Registry Procedures

Capital Asset Guidelines

Risk Management Policy