Ohio | Board of Regents

Ted Strickland, Governor
Eric D. Fingerhut, Chancellor

University System of Ohio

DIRECTIVE 2010-023
April 20, 2010

Re: CONSIDERATION OF A REQUEST BY THE UNIVERSTIY OF CINCINNATI TO PLEDGE STUDENT FEES IN SUPPORT OF A BOND ISSUANCE NOT TO EXCEED $62,250,000 TO BE USED TO FINANCE VARIOUS CAPITAL IMPROVEMENT PROJECTS ON THE INSTITUTION'S MAIN CAMPUS.

Ohio Revised Code §3345.11 enables a state university or college to issue general receipts obligation bonds in the manner provided by and subject to the applicable provisions of Ohio Revised Code §3345.12.

§371.60.20 of Am. Sub. H.B. 1 of the 128th General Assembly requires that any new pledge of student fees to secure bonds or notes of a state college or university be approved by the Chancellor of the Ohio Board of Regents.

Pursuant to Ohio Revised Code, The University of Cincinnati has demonstrated the following:

- The proposed projects are essential to fulfilling institutional goals.
- The University's Board of Trustees approved resolutions authorizing this bond issuance at their March 16, 2010 meeting.
- The University of Cincinnati has demonstrated that their proposal complies with §3345.11 and §3345.12.

Agency staff reviewed the request and posted its recommendations to the Regents' web site for purposes of providing a period of public comment before final approval by the Chancellor. The materials posted for comment and the request to pledge student fees are attached to this document.

Based on my review of staff recommendations, I hereby approve the Request to Pledge Student Fees by the University of Cincinnati in support of general receipts obligation bonds in an aggregate amount not to exceed $62,250,000.

This directive will take effect immediately.

Eric D. Fingerhut
Chancellor, Ohio Board of Regents

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The University of Cincinnati
April 2010 Fee Pledge Request - $62,250,000

I. Project Overview

The University of Cincinnati proposes to issue general receipts bonds to finance various capital projects on its main campus, including:

- Morgens Hall Renovation & Scioto Hall Decommissioning
- Phase II: Utility Energy Savings Projects
- Phase II: Roof Replacements
- Phases III & IV: Rieveschl Lab Renovations
- Jefferson Avenue Sports Complex

The University intends for this debt to be financed through a combination of a non-permanent and permanent debt that will be retired in 10 to 25 years.

Submission: March, 2010

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II. Project Financing and Costs

The University of Cincinnati requests the authority to pledge student fees in support of the issuance of general receipts obligation bonds in an aggregate amount not to exceed $62,250,000. Estimated project costs funded through the proposed debt issuance are presented below:

Project	Estimated Project Costs	Net Capitalized Interest	Provision for Bond Discount and Issue	Margin of Safety	Total Bond Authorization Requested
Morgens Hall Renovation & Scioto Hall Decommissioning	$20,000,000	$2,944,000	$291,000	$1,365,000	$24,600,000
Utility Energy Savings Projects - Phase II	$10,000,000	$500,000	$135,000	$865,000	$11,500,000
Roof Replacements - Phase II	$3,000,000	$0	$46,000	$204,000	$3,250,000
Rieveschl Lan Renovations Phase III & IV	$12,000,000	$0	$152,000	$748,000	$12,900,000
Jefferson Avenue Sport Complex	$10,000,000	$0	$0	$0	$10,000,000
Total Debt Issuance	*$55,000,000*	*$3,444,000*	*$624,000*	*$3,182,000*	*$62,250,000*

The University of Cincinnati estimates that the maximum annual debt service obligation for the proposed debt issuance will be $4,350,000, based on an annual interest rate no greater than 5.25% over a period of 10 to 25 years. Moreover, the related debt service and incremental operating costs relating to the capital projects will be supported through the use of undesignated general funds as well as pledged funds and auxiliary revenues (as identified in the project description section).

III. Fee Impact

This proposed debt issuance will have no direct impact on student tuition and fees. While the University of Cincinnati may use unrestricted student fee revenues to support the debt service and operating costs relating to this request, student fees are not expected to increase as a direct result of this action.

IV. Project Description

The following provides project descriptions for the five projects identified in The University of Cincinnati's $62,250,000 debt authority request:

Morgens Hall Renovation & Scioto Hall Decommissioning ~ $24,600,000

The primary purpose of this project is to renovate Morgens Hall and decommission Scioto Hall. The renovations to Morgens Hall include the remediation and complete replacement of the mechanical and plumbing systems, replacement of building façade as well as roof improvements. The scope of the work for Scioto Hall includes the decommissioning of building services to minimize utility consumption in the unoccupied areas of the building. The renovation and decommissioning projects were approved by the University of Cincinnati's Board of Trustees as part of its FY 2009-2010 Capital Budget during their June 23, 2009 meeting. The projects are currently in the design phase; construction is anticipated to commence in the spring of 2011 with an estimated completion date of summer 2013.

The University of Cincinnati estimates that $24,600,000 in total debt authority is sufficient to fund the $20,000,000 in project costs, estimated debt issuance costs and capitalized interest. Moreover, UC estimates the average annual debt service for this project to be $1,700,000; which will be repaid over 25 years with Campus Services and Housing revenues.

Utility Energy Savings Project, Phase II ~ $11,500,000

The primary purpose of this project is to fund a series of projects designed to improve existing utility plant efficiencies, improve efficiencies of existing major building systems and upgrade existing facilities with new or updated building systems. The projects are specifically designed to facilitate a reduction in energy usage and facilitate the university's compliance with the requirements of Ohio H.B. 251 as well as the American College & University Presidents' Climate Commitment. The annual energy savings is estimated to be between $1.4 and $1.6 million. The second phase of the Utility Savings Project was approved by the university's Board of Trustees during its June 24, 2008, meeting as part of the Capital Budget process for FY 2008-09. The designs for the project are currently underway with construction expected to commence during the summer of 2010 and an anticipated completion date in October 2011.

The University of Cincinnati estimates that $11,500,000 in total debt authority is sufficient to fund the $10,000,000 in project costs, estimated debt issuance costs and capitalized interest. Moreover, the institution estimates the average annual debt service to be $1,400,000; which will be repaid over 10 years with undesignated general funds supported from anticipated energy savings in the same amount.

Roof Replacement Project, Phase II ~ $3,250,000

The primary purpose of this project is to replace or improve numerous roofs on various buildings throughout campus. Current roof structures at Blegen Library, Swift Hall, the Cardiovascular Center and Memorial Hall were prioritized as the most in need of repair. Additional roof repairs will be added as the project budget allows. The new roofs were designed to improve energy efficiency and sustainability to the respective buildings. The life expectancy of the new roofs is expected to be 20 to 25 years. The university intends for each of the roofing projects to be approved through an appropriate approval process based on their project costs.

The University of Cincinnati estimates that $3,250,000 in total debt authority is sufficient to fund the $3,000,000 in project costs and related debt issuance costs. Moreover, the institution estimates the average annual debt service for this project to be $250,000; which will be repaid over 20 years with undesignated general funds.

Rieveschl Lab Renovations Project, Phases III & IV ~ $12,900,000

The primary purpose of the Rieveschl Lab project is to continue the strategic updates of the University's oldest basic science education facility. Specifically, the project includes the renovation of approximately 5,000 square feet of existing teaching laboratory space including:

- Abatement,
- Fire suppression,
- New mechanical, electrical, plumbing, lighting and lab utilities, and
- New finishes, laboratory casework and fume hoods.

The Rieveschel Lab renovations were approved by the University of Cincinnati's Board of Trustees during their June 23, 2009, meeting as part of the Capital Budget for FY 2009-2010. The design is currently underway with abatement scheduled to begin in the fall of 2010. In addition, construction is anticipated to begin in the spring of 2012 with a completion date scheduled in the fall of 2013.

The University of Cincinnati estimates that $12,900,000 in total debt authority is sufficient to fund the $12,000,000 in project costs and related debt issuance costs. Moreover, the institution estimates the average annual debt service costs for this project to be $1,000,000 beginning in 2014; which will be repaid over 20 years with undesignated general funds.

Jefferson Avenue Sports Complex ~ $10,000,000 (Interim Financing)

The primary purpose of the Jefferson Avenue Sports Complex is to provide the Department of Athletics with new fields to be used for football practice, competitive women's lacrosse and other programs supported by Athletics that also benefit the campus at large. The new complex will add one full field, a half field, an access road to facilitate easy access to the main campus, and provide a temporary bubble to cover the field during the winter months. Associated infrastructure upgrades and site preparation work is included within the scope of this project. The Jefferson Avenue Sports Complex project was approved at the November 17, 2009 Board Meeting. The design for the project is currently underway with construction expected to commence during in the spring of 2010. All construction is expected to be complete by the winter of 2011 and will ultimately be funded entirely by the Athletics Department, using a combination of pledged gifts and future game contracts. The funds will be received over a period of time which necessitates the borrowing of cash in advance of the receipt of gifts and game contracts; a process known as "interim financing".

This debt authority is sufficient to provide the cash required for project expenditures prior to the receipt of gifts pledged and game contracts. The $10,000,000 in debt authority will be renewed annually until all gifts and/or game contract payments are received. Gifts pledged and game contract payments will be sufficient to support the estimated project costs as well as the estimated financing costs, in the interim. Annual debt service is estimated at $400,000 (20 years at 5%) considering gifts received to date and guaranteed game revenues.

V. Financial Ratio Analysis

Through the 1997 enactment of Senate Bill 6, the 122nd General Assembly established a standardized method for monitoring the financial health of Ohio's state-assisted colleges and universities. Subsequently, the administrative rules used to guide the implementation of S.B. 6 identified three financial ratios to evaluate an institution's fiscal health. The rules also established threshold factors for ranges of ratios, and created a weighted score of the threshold factors, termed the *composite score*, which provides a summary statistic to evaluate an institution's financial stability. The ratios and composite score are described in greater detail below, including how The University of Cincinnati performed when these measures are applied to its FY 2006, FY 2007, FY 2008 and FY 2009 audited financial statements—the most up-to-date financial data available.

*NOTE: The FY 2009 data shown in *italics* reflect the ratios and composite score when approximately $72,850,000 in new debt is added to the calculations. This amount equals the estimated FY 2009 debt issuances of approximately $10,600,000 and $62,250,000 in net new debt requested here. Also, $5,250,000 in related debt service expenses have been added to the calculations. Other factors not taken into account here include the impact of the new debt on the University's expendable net assets, the future retirement of existing debt obligations, and future changes in revenues and expenses.

1. Viability Ratio

The viability ratio is defined as expendable net assets divided by plant debt. This ratio is a measure of an institution's ability to retire its long-term debt using available current resources. A viability ratio in excess of 100% indicates that the institution has expendable fund balances in excess of its plant debt. Pursuant to this analysis, a viability ratio of 60% or greater is considered good, while a ratio below 30% might be a cause for concern. The University of Cincinnati's viability ratios for FY 2006, FY 2007, FY 2008 and FY 2009 are as follows:

FY 2006	FY 2007	FY 2008	FY 2009	*FY 2009**
24.0%	21.1%	24.5%	24.3%	*22.8%*

2. Primary Reserve Ratio

The primary reserve ratio is defined as expendable net assets divided by total operating expenses. This ratio is one measure of an institution's ability to continue operating at current levels without future revenues. Pursuant to the S.B. 6 analysis, a ratio of 10% or greater is considered good, while a ratio below 5% would be a cause for concern. The University of Cincinnati's primary reserve ratios for FY 2006, FY 2007, FY 2008 and FY 2009 are as follows:

FY 2006	FY 2007	FY 2008	FY 2009	*FY 2009**
24.3%	23.1%	27.4%	26.8%	*26.7%*

3. Net Income Ratio

The net income ratio represents the change in total net assets divided by total revenues. This ratio is an important measure of an institution's financial status in terms of current year operations. A negative net income ratio results when an institution's current year expenses exceed its current year revenues. A positive net income ratio indicates that the institution experienced a net increase in current year fund balances. The University of Cincinnati's net income ratios for FY 2006, FY 2007, FY 2008 and FY 2009 are as follows:

FY 2006	FY 2007	FY 2008	FY 2009	*FY 2009**
+4.4%	+9.7%	-4.9%	-43.5%	*-44.2%*

As outlined in the Management's Discussion and Analysis section of the University's 2009 Financial Report, the net assets of the University declined in FY08 and FY09 as there are significant transactions included in the non-operating revenues (expenses) that are influenced significantly by the economy and investment markets. These items include: Fluctuations in the market value of investments; additions to permanent endowments and state capital appropriation revenue. A new strategic asset allocation policy was implemented on October 1, 2009 that will improve the ability of the endowment to sustain spending while maintaining its real, inflation-adjusted value. The University is committed to continuing its strategic vision while continuing to build upon its financial strength.

The negative net income ratio for FY09 is due mainly to a $330,000,000 decrease in the fair value of investments. As of the third quarter for FY10, the university has estimated conservatively a $100,000,000 increase in the fair value of investments. When comparing FY09 to FY10, for total operating/non-operating revenue, a positive delta of $430,000,000 is projected.

The university has strategically aligned its FY10 budget to offset any potential reductions in future fiscal years' funding streams.

4. Composite Score

The ratios are translated into a single composite score by assigning individual scores to ranges of ratios, weighting the individual scores, and summing the weighted scores. The primary reserve score is weighted more heavily than is the viability ratio, which in turn is weighted more heavily than the net income ratio. This scoring process effectively emphasizes the need for campuses to have strong expendable fund balances, manageable plant debt, and a positive operating balance.

The minimum acceptable composite score is any score above 1.75. Institutions with composite scores at or below this level merit special monitoring, and would be placed on fiscal watch if the ratio analysis yielded a composite score at or below this level for two consecutive years. The highest possible score is a 5.0. The University of Cincinnati's composite scores have been above the minimum threshold:

FY 2006	FY 2007	FY 2008	FY 2009	*FY 2009**
2.60	2.80	2.50	2.30	*2.30*

VI. Financial Outlook and Bond Rating

According to its FY 2009 audited financial report, The University of Cincinnati's financial position remains strong, having reported total assets of $2,964,366,000 and liabilities of $1,339,995,000. Net assets, which represent the value of the University's assets after liabilities are deducted, decreased by $301,144,000 in FY 2009 to $1,624,371,000 or 54.8% of total assets.

The University's existing debt has received relatively high marks from independent bond-rating agencies. In December 2009, The University of Cincinnati's Moody's Investors Services affirmed the institution's *A2* rating with a stable outlook. In addition, Standard & Poor's affirmed the University's long-term debt rating of *A+* with a stable outlook.

These ratings indicate that the University's ability to meet its debt obligations is considered strong, as shown in Moody's and S&P's scale below.

Long-Term Bonds				
Moody's			**S & P**	**Description**
Aaa1	Aaa2	Aaa3	AAA	Best quality with little or no investment risk.
Aa1	Aa2	Aa3	AA	High quality with low investment risk.
A1	A2	A3	A	High quality with moderate investment risk.
Baa1	Baa2	Baa3	BBB	Good quality with some investment risk.
Ba1	Ba2	Ba3	BB	Medium quality with some investment risk.
B1	B2	B3	B	Medium quality with higher investment risk.
Caa1	Caa2	Caa3	CCC	Low quality and susceptible to default.
Ca1	Ca2	Ca3	CC	Low quality and highly vulnerable to default.
C1	C2	C3	C	Lowest quality and extremely vulnerable to default.
-	-	-	D	In payment default (S&P rating only).

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VII. Institutional Plant Debt

The table on the following page depicts how long-term plant debt at Ohio's public colleges and universities has changed at the statewide level over the past five years. Between FY 2005 and FY 2009, statewide plant debt increased 35.4% or approximately $1.17 billion. A major contributing factor to this growing level of debt is the need for institutions to address critical capital and maintenance needs on campus. As the state's capital investment in Ohio's campuses has diminished in recent years, the need has grown for campuses to issue local debt.

While statewide institutional debt increased by $445.6 million or 11.0% in FY 2009, The University of Cincinnati's plant debt decreased by $376,000 or 0.03%.

FY 2005-2009 Long-Term Plant Debt

Institution	Long-Term Plant Debt				
	FY 2005	FY 2006	FY 2007	FY 2008	*2009*
UNIVERSITIES					
BOWLING GREEN	$109,000,000	$99,250,000	$89,345,000	$80,290,000	$78,255,000
CENTRAL STATE	$2,340,402	$2,177,250	$2,003,952	$1,862,693	$1,743,287
CLEVELAND STATE	$115,923,075	$113,522,226	$161,098,196	$163,591,508	$207,067,009
KENT STATE	$279,692,000	$276,441,000	$273,153,000	$277,532,000	$276,019,000
MUO (b)	$56,299,000	$53,827,000	See UT	See UT	See UT
MIAMI UNIV.	$168,613,252	$159,727,329	$235,357,582	$228,484,393	$224,325,090
NEOUCOM	$1,046,607	$878,345	$700,300	$2,291,713	$1,992,413
OHIO STATE	$877,540,000	$1,106,227,000	$1,118,091,000	$1,076,097,000	$1,360,245,000
OHIO UNIVERSITY	$167,529,147	$192,862,349	$182,914,606	$167,403,027	$192,718,265
SHAWNEE STATE	$2,270,000	$1,925,000	$19,550,000	$17,765,000	$17,515,000
UNIV. AKRON	$258,484,797	$255,328,236	$247,378,185	$421,931,710	$418,195,077
UNIV. CINCINNATI	**$877,453,000**	**$966,516,000**	**$1,074,333,000**	**$1,091,020,000**	**$1,090,644,000**
UNIV. TOLEDO	$176,779,000	$171,134,000	$269,554,000	$265,409,000	$252,924,000
WRIGHT STATE	$46,189,820	$42,513,677	$38,738,096	$35,624,887	$31,564,022
YOUNGSTOWN STATE	$13,268,653	$22,162,550	$20,397,972	$18,603,592	$38,990,037
COMMUNITY COLLEGES					
BELMONT TECH	$33,107	$0	$0	$0	$0
CINCINNATI STATE	$47,530,000	$47,923,408	$47,701,975	$47,455,542	$46,774,109
CLARK STATE	$46,400	$8,195,000	$8,175,000	$7,900,000	$7,900,000
COLUMBUS STATE	$22,700,000	$21,250,000	$19,830,000	$18,255,000	$16,620,000
COTC	$100,986	$2,112,219	$3,875,762	$3,470,979	$2,394,382
CUYAHOGA	$64,840,147	$62,974,601	$57,393,209	$79,449,916	$178,119,296
EDISON STATE	$532,347	$5,109,018	$4,975,254	$4,704,730	$4,422,095
HOCKING	$1,039,729	$5,025,450	$5,235,058	$6,384,650	$6,089,638
JAMES RHODES	$3,067,812	$3,018,241	$2,968,669	$2,914,098	$2,859,527
JEFFERSON	$2,023,978	$1,838,573	$1,623,724	$1,422,593	$1,211,968
LAKELAND	$5,535,996	$4,767,321	$4,044,695	$3,308,426	$11,096,151
LORAIN	$7,925,194	$7,472,149	$7,010,546	$6,529,973	$6,035,000
MARION TECH	$0	$0	$0	$0	$0
NORTH CENTRAL	$220,160	$182,119	$727,540	$97,879	$51,308
NORTHWEST STATE	$82,001	$35,594	$25,249	$59,860	$40,300
OWENS STATE	$749,152	$579,288	$401,212	$536,241	$276,495
RIO GRANDE	$0	$0	$0	$2,411,421	$2,256,498
SINCLAIR	$0	$0	$0	$0	$0
SOUTHERN STATE	$3,022,204	$2,839,083	$2,710,583	$5,577,394	$5,371,694
STARK STATE	$16,738	$6,137	$0	$0	$0
TERRA STATE	$655,721	$464,012	$264,285	$66,409	$0
WASHINGTON STATE	$0	$0	$0	$0	$0
ZANE STATE (MATC)	$285,586	$223,983	$156,401	$309,075	$654,117
STATEWIDE TOTAL	**$3,312,836,011**	**$3,638,508,158**	**$3,899,734,051**	**$4,038,760,709**	**$4,484,369,778**