OHIO BOARD OF REGENTS

Agenda Item 3.20 Consideration of a request by the Ohio State University to pledge student fees in support of a debt issuance not to exceed $88,700,000 to be used for multiple capital improvements and new projects.

RESOLUTION

WHEREAS, §89.11 of Am. Sub. H.B. 95 of the 125th General Assembly requires that any new pledge of student fees to secure bonds or notes of a state college or university must be approved by the Ohio Board of Regents; and

WHEREAS, the Ohio State University proposes to pledge student fees in support of general receipts bonds and commercial paper in an aggregate amount not to exceed $88,700,000 for the purpose of financing multiple renovations and new projects on campus; and

WHEREAS, to provide for financial flexibility, reduced costs, and administrative simplicity, the University proposes to issue short-term commercial paper to later be converted to long-term bonds; and

WHEREAS, the University has determined that the proposed renovations and projects are essential to meeting the needs of students and fulfilling institutional goals; and

WHEREAS, the University's Board of Trustees is expected to approve this proposed debt issuance at its meeting of July 8, 2005; and

WHEREAS, the proposed debt issuance complies with the requirements of Section 3345.11 and Section 3345.12 of the Ohio Revised Code.

NOW THEREFORE,

BE IT RESOLVED, contingent upon the approval of the Ohio State University Board of Trustees, and upon the recommendation of the Chancellor and with the concurrence of the Resources Committee of the Ohio Board of Regents, that the pledge of fees by the Ohio State University in support of general receipts bonds, notes, or commercial paper not to exceed an aggregate amount of $88,700,000 is hereby approved.

The Ohio State University
June 2005 Fee Pledge Request - $88.7 million

A. Project Overview

The Ohio State University requests consideration of a request to pledge student fees in support of a debt issuance to support 15 capital projects that include constructing new facilities, renovating existing facilities, and acquiring other capital assets. The estimated total cost of this proposal is roughly $636 million, which includes construction and acquisition costs, capitalized interest, financing costs, and other related costs. At this time, the University requests debt authority of $88.7 million. Some of the aspects of this request include:

1. Expanding the University's biomedical research capabilities.
2. Replacing the student union (first phase).
3. Expanding and improving student housing.
4. Constructing a new early childhood development center
5. Expanding and improving University medical facilities.
6. Upgrading several buildings and campus infrastructure.

Initial Submission to the Board: June 2005.

Revised Submission:

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B. Project Financing

The Ohio State University is in the process of planning several capital improvements and other related projects described herein, which have an estimated total cost of between $586 million and $686 million. The University proposes to issue a combination of long-term general receipt bonds and short-term commercial paper in an amount not to exceed $88.7 million to support these projects. The University plans to finance this debt with general operating funds, student housing and auxiliary revenues, fundraising income, and state capital appropriations.

The table below provides a breakdown of project costs, amounts to be financed, and revenue sources for each of the 15 projects included in this proposal.

	Ohio State University, June-July 2005	Total Project Cost	New Debt Financing	% to be Financed with New Debt	Funding Sources
Projects:					
1	Archer House renovation and conversion	$5,000,000	$5,000,000	100%	Student Affairs/Housing revenues
2	Biomedical Research Facility addition	$9,000,000	$9,000,000	100%	General fund revenues
3	Cannon Drive Substation transformer	$6,000,000	$6,000,000	100%	General fund revenues
4	Digestive Diseases Center	$22,000,000	$8,000,000	36%	Medical Center revenues; state capital appropriations
5	Early Childhood Development Center	$11,600,000	$1,500,000	13%	General fund revenues; proceeds from fundraising
6	Fawcett Center renovation	$8,000,000	$8,000,000	100%	Student Affairs/Housing revenues
7	Kinnear Road Infrastructure	$5,000,000	$5,000,000	100%	General fund revenues
8	Lincoln Tower renovation (Phase I)	$27,500,000	$1,000,000	4%	Student Affairs/Housing revenues
9	Mansfield Admin. & Classroom Bldg.	$7,800,000	$6,500,000	83%	General fund revenues; proceeds from fundraising
10	Marion Campus Student Services Bldg.	$6,100,000	$1,100,000	18%	State capital appropriations; general fund revenues
11	North Hot Water Heating Loop	$2,500,000	$2,500,000	100%	General fund revenues
12	Ohio Union replacement (Phase I)	$100,000,000	$1,000,000	1%	Student Affairs and Ohio Union revenues
13	Project Cancer - Medical Center (Phase I)	$350,000,000	$10,250,000	3%	Med. Center income; fundraising; indirect cost recoveries
14	Scott Laboratory construction	$72,500,000	$12,000,000	17%	State capital appropriations; fundraising; general funds
15	South/West Campus Land Acquisition	$2,850,000	$2,850,000	100%	General fund revenues
	Subtotal	**$635,850,000**	**$79,700,000**	**13%**	
	Margin of safety/contingencies	--	$9,000,000	--	
	Total debt authority requested	**--**	**$88,700,000**	**--**	

The University proposes issuing general receipt debt consisting of a combination of bonds and commercial paper, which includes converting commercial paper (previously approved by the Regents in 2003) to bonds. By first issuing short-term commercial paper that will be subsequently converted to long-term bonds, the University reports that it has enjoyed savings in excess of $8 million in the seven years that it has exercised this practice.

The long-term debt issuance will be split between fixed and variable rate bonds. The fixed interest rate is estimated to be 3.75% to 4%; the variable interest rate is currently 2.75%. The debt service schedule for this proposal will not exceed 25 years, and could be no more than 20 years.

The University expects this debt issuance to increase its annual debt service obligation by approximately $2 million. This amount will increase marginally once the commercial paper portion of this issuance is converted to long-term debt in 18 to 36 months. However, because it is likely that OSU will refund a portion of its current outstanding debt, OSU is likely to experience a net reduction in debt service expenditures of approximately $300,000 per year.

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C. Fee Impact

This proposed debt issuance will have no direct impact on student tuition and fees. While the University may use unrestricted student fee revenues to service the debt and pay for related operating costs, student fees will not increase as a direct result of this fee pledge.

In the future, however, Ohio State will most likely implement a new student fee to help cover the debt service and operating costs for the new student union when this project is completed in 2009. (Phase I of this project is described in section D.12 of this document.)

Ohio State anticipates that this fee would be exempt from any limitation on fee increases that might be imposed in the future by the state legislature. Ohio State will outline the specifics of this fee in 2007 when the University formally requests Regents approval for the remaining debt authority needed for this project.

The Ohio State University
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D. Project Description

1. **Archer House Conversion, $5 million:** Renovation of Archer House, which is currently used for office space, into a residence hall and support space. The residence will house 103 undergraduate students. Estimated completion: 2006.

2. **Biomedical Research Facility Addition, $9 million**: This project will construct approximately 20,000 assignable square feet for the University Lab Animals Resources Department. This space will connect to the the Biomedical Research Facility. Estimated completion: 2006.

3. **Campus Electric Capacity Expansion, $6 million**: Installation of a third transformer at the Cannon Drive Substation increasing capacity and providing redundancy. Estimated completion: 2007.

4. **Digestive Deseases Center, $8 million:** Renovation of space in Wiseman Hall to provide research lab and support space. Renovation and addition to Doan Hall to provide clinical and related educational and support space. Estimated completion: 2006.

5. **Early Childhood Development Center, $1.5 million:** Design, construction and equipping a building at Weinland Park to house the Early Childhood Development Center. The 47,840 square foot facility will serve approximately 80 children and will include space for the College of Human Ecology. Estimated completion: 2005.

6. **Fawcett Center Renovation, $8 million:** Renovate Fawcett Center to create 34,600 square feet of office space and to bring the facility into compliance with fire codes. Estimated completion: 2007.

7. **Kinnear Road Infrastructure, $5 million**: Improvements to various infrastructure and roadway projects including storm water drainage water pressure improvement, utilities upgrade and improved roadways. Estmated completion: 2007.

8. **Lincoln Tower Renovation (phase I), $1 million**: This project will return Lincoln Tower back to a complete student housing facility by renovating floors 1-15 from office space. The resulting 209,298 square feet will add an additional 600 beds for undergraduate student housing. Estimated completion: 2011.

9. **Manfield Campus Administrative & Classroom Bldg., $6.5 million**: Design, construction and equipping a building on the Mansfield Campus to provide space for the departments of Music, Education, Student Services and Business Office. There will also be a 150-seat auditorium. Estimated completion: 2007.

10. **Marion Campus Student Services Building, $1.1 million**: Design and construct a building of approximately 17,500 square feet to house student services and academic program offices. The project will also upgrade a parking lot. Estimated completion: 2005.

11. **North Hot Water Heating Loop, $2.5 million**: Replacement of 8.2-mile hot water heating loop and replacement of distribution piping, heat exchanges and pumps in the McCracken Power Plant. Installation of new gas fired boilers. Estimated completion: 2007.

12. **Ohio Union Replacement (phase I), $10 million**: Replacement of the existing Ohio Union with a new building of approximately 264,000 square feet. The building will contain meeting space, study space, offices, retail including food service and recreational facilities. Estimated completion: 2009.

13. **Project Cancer (phase I), $10.25 million**: Expansion of the James Cancer Hospital and Richard J. Solove Research Institute to include an additional 128 beds, approximately 300,000 square feet of outpatient facilities and approximately 300,000 square feet of wet and dry research facilities. Estimated completion: 2013.

14. **Scott Laboratory, $12 million** Demolition of Robinson Laboratory and construction of a 240,000 square foot, three building complex to house classrooms, laboratories and offices. Estimated completion: 2005.

15. **South/West Campus Land Acquisition, $2.85 million** Purchase of properties near or contiguous to the University's Columbus Campus to support the University's mission of teaching, research and public service. Estimated completion: 2007.

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E. 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 Ohio State University performed when these measures are applied to its FY 2001, FY 2002, FY 2003 and FY 2004 audited financial statements—the most up-to-date financial data available.

It is important to note that beginning in FY 2002, financial statements began being reported in a modified format as required by the Government Accounting Standards Board (GASB) statements 34 and 35 for public colleges and universities. The most significant change resulting from the new GASB 34/35 format is the inclusion of depreciated assets in the annual audited financial statements reported by public campuses. Accordingly, the procedures for calculating the S.B. 6 ratio analysis were adjusted to permit a comparable, consistent and effective methodology for measuring fiscal stability.

*NOTE: The FY 2004 data shown in *italics* reflect the ratios and composite score when $88.7 million in new debt and $2 million in new debt services expenses are 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 retirement and/or refunding of existing debt obligations, and future changes in revenues and expenses.

1. Viability Ratio

For FY 2001, the viability ratio is defined as expendable fund balances divided by plant debt. For FY 2001(B)*, FY 2002, FY 2003 and FY 2004 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. Ohio State's viability ratios for FY 2001, FY 2002, FY 2003 and FY 2004 are as follows:

FY 2001	FY 2002	FY 2003	FY 2004	*FY 2004**
190.8%	105.5%	167.2%	145.7%	*131.4%*

2. Primary Reserve Ratio

For FY 2001, the primary reserve ratio is defined as expendable fund balances divided by total expenditures and mandatory transfers. For FY 2001(B)*, FY 2002, FY 2003 and FY 2004 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. Ohio State's primary reserve ratios for FY 2001, FY 2002, FY 2003, and FY 2004 are as follows:

FY 2001	FY 2002	FY 2003	FY 2004	*FY 2004**
33.0%	38.0%	39.3%	42.5%	*42.5%*

3. Net Income Ratio

For FY 2001, the net income ratio represents net total revenues divided by total current revenues. For FY 2001(B)*, FY 2002, FY 2003 and FY 2004 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 expenditures/expenses exceed its current year revenues. A positive net income ratio indicates that the institution experienced a net increase in current year fund balances. Ohio State's net income ratios for FY 2001, FY 2002, FY 2003 and FY 2004 are as follows:

FY 2001	FY 2002	FY 2003	FY 2004	*FY 2004**
+0.40%	-3.1%	+8.4%	+12.2%	+*12.2%*

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 generally 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 below this level for two consecutive years. The highest possible score is a 5.00. Ohio State's composite scores have been well above the minimum threshold:

FY 2001	FY 2002	FY 2003	FY 2004	*FY 2004**
3.60	3.40	4.20	4.20	*4.20*

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F. Financial Outlook & Bond Rating

According to Ohio State University's most recent audited financial report, the University's financial health remains sound. In FY 2004, the University's total expendable net assets increased by $207 million, primarily due to the issuance of long-term bonds, which shifted the negative equity associated with construction activity from net assets to capital assets. The University also reported a $244 million net investment gain in FY 2004. Additionally, Ohio State reported that it continues to work toward diversifying its revenue base, reducing operating costs, and effectively managing financial risks.

The Ohio State University's existing bond-related debt has received favorable marks from independent bond-rating agencies. Ohio State's existing long-term debt most recently received ratings of *Aa2* from Moody's Investors Services and *AA* from Standard & Poor's. Based on these ratings, the University's capacity to meet its financial obligations is considered strong. Additionally, OSU's short-term debt has received the highest possible ratings of MIG1 and SP-1+ from Moody's and S&P, respectively. The tables below illustrate Moody's and S&P's rating scale.

Long-Term Debt				
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).

Short-Term Debt		
Moody's	**S & P**	**Description**
MIG 1	SP-1+	Best quality with very strong debt service capacity.
MIG 2	SP-1	High quality with strong debt service capacity.
MIG 3	-	Good quality but may have narrow protection.
MIG 4	SP-2	Adequate quality with some risk of vulnerabilty.
SG	SP-3	Speculative quality and capacity for debt service.

The Ohio State University Board of Trustees took several steps during FY 2004 to help preserve OSU's strong credit ratings, including:

- Setting guidelines limiting the amount of new debt that may be issued;
- Establishing a $400 million cap for bonded projects; and
- Implementing a 12-month freeze on bonding for new projects.

VII. Institutional Plant Debt

The table on the following page depicts how long-term plant debt at Ohio's public colleges and universities has consistently increased at the statewide level over the past five years. Over the past five years, between FY 1999 and FY 2004, aggregate net plant debt increased by 166% or $1.9 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 locally issue debt.

At Ohio State University, net growth in long-term plant debt increased by 158% or $499 million over the past five years. In response to a December 2003 survey of campuses, the Ohio State reported that 61% of its outstanding debt essentially pays for itself—that is, the debt and operating costs are supported by auxiliary revenues directly related to the capital projects for which debt was issued—and 39% is supported by general receipts.

Institution	Long-Term Plant Debt					
	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004
UNIVERSITIES						
BOWLING GREEN	$35,400,000	$32,035,000	$83,415,000	$79,255,000	$91,215,000	$84,410,000
CENTRAL STATE	$3,780,127	$3,572,922	$3,346,920	$3,192,444	$2,703,429	$2,535,821
CLEVELAND STATE	$16,420,347	$16,153,641	$12,393,540	$10,849,215	$55,977,422	$53,754,446
KENT STATE	$63,143,000	$81,774,000	$234,407,000	$290,735,000	$285,773,000	$282,832,000
MCOT	$2,883,387	$2,184,779	$1,229,464	$6,392,000	$8,837,000	$8,730,000
MIAMI UNIV.	$44,949,785	$49,018,070	$45,061,353	$53,168,773	$47,994,898	$92,833,435
NEOUCOM	$0	$0	$542,430	$1,583,286	$1,397,190	$1,237,841
OHIO STATE	**$315,216,350**	**$365,192,650**	**$378,145,912**	**$581,106,000**	**$586,233,000**	**$814,606,000**
OHIO UNIVERSITY	$79,696,363	$84,103,403	$132,049,339	$126,677,123	$133,002,202	$175,592,164
SHAWNEE STATE	$3,672,175	$3,599,407	$3,406,398	$3,200,000	$2,910,000	$2,600,000
UNIV. AKRON	$36,007,772	$59,014,572	$89,002,729	$191,864,557	$211,208,546	$226,729,516
UNIV. CINCINNATI	$365,895,000	$375,212,000	$577,365,000	$567,181,000	$647,688,000	$893,004,000
UNIV. TOLEDO	$93,722,220	$88,467,721	$121,691,439	$119,376,000	$172,577,000	$167,367,000
WRIGHT STATE	$15,669,753	$14,438,988	$13,232,584	$11,575,625	$18,570,323	$29,584,121
YOUNGSTOWN ST.	$19,096,590	$17,840,681	$16,368,157	$14,992,226	$14,263,619	$13,492,373
COMMUNITY COLLEGES						
CINCINNATI ST.	$771,204	$592,494	$423,417	$0	$49,173,132	$47,580,000
CLARK STATE	$0	$68,172	$47,234	$22,011	$0	$72,800
COLUMBUS ST.	$14,263,821	$14,108,529	$13,221,412	$12,330,217	$11,434,658	$24,105,000
CUYAHOGA	$0	$0	$4,083,210	$12,564,559	$59,095,229	$65,222,373
EDISON STATE	$0	$800,000	$800,000	$738,589	$68,676	$604,972
JEFFERSON	$0	$0	$0	$0	$0	$2,170,485
LAKELAND	$6,493,734	$6,445,224	$2,900,237	$2,441,594	$1,976,978	$5,674,098
LORAIN	$12,340,038	$9,806,212	$7,230,062	$5,426,817	$3,952,163	$9,560,074
NORTHWEST ST.	$0	$0	$0	$123,260	$106,207	$73,705
OWENS STATE	$136,892	$141,049	$206,317	$0	$0	$0
RIO GRANDE	$0	$0	$0	$0	$0	$0
SINCLAIR	$0	$0	$0	$0	$0	$0
SOUTHERN ST.	$259,010	$138,968	$155,855	$122,950	$168,506	$3,245,886
TERRA STATE	$0	$0	$49,805	$42,710	$35,171	$839,738
WASHINGTON ST.	$0	$0	$0	$0	$0	$0
TECHNICAL COLLEGES						
BELMONT TECH	$0	$0	$0	$126,878	$97,927	$66,728
COTC	$337,831	$305,307	$270,726	$231,348	$186,826	$401,059
HOCKING	$1,871,748	$1,873,504	$4,311,120	$5,213,938	$497,794	$516,117
JAMES RHODES ST	$0	$0	$0		$0	$3,087,383
MARION TECH	$0	$0	$0		$0	$0
ZANE STATE (MATC)	$0	$0	$0	$0	$182,571	$341,385
NORTH CENTRAL	$775,048	$703,213	$744,479		$375,474	$300,562
STARK STATE	$143,311	$308,942	$259,870	$763,399	$620,993	$620,080
STATEWIDE TOTAL	$1,132,945,506	$1,227,899,448	$1,746,361,009	$2,101,296,519	$2,408,322,934	$3,013,791,162

(a) FY 2002 was first year of reporting under new GASB 34/35 requirements.

(b) FY 2003 figures are preliminary. The FY 2003 analysis is still under review and is subject to revision.

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