OHIO BOARD OF REGENTS

Agenda item 3.11 Consideration of a request by the University of Toledo to pledge student fees in support of a bond issuance not to exceed $14,000,000.

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 University of Toledo proposes to pledge student fees in support of general receipts obligation bonds and/or bond anticipation notes in an amount not to exceed $14,000,000 for the purpose of financing a land acquisition and two capital projects; and

WHEREAS, the University has determined that the proposed project is essential to fulfilling institutional goals; and

WHEREAS, the University's Board of Trustees is expected to consider a resolution authorizing this bond issuance at its meeting of October 27, 2004; and

WHEREAS, this proposal complies with the requirements of Ohio Revised Code §3345.11 and §3345.12.

NOW THEREFORE,

BE IT RESOLVED: Contingent upon the approval of the University of Toledo Board of Trustees, and upon the recommendation of the Chancellor and with the concurrence of the Resources & System Efficiency Committee of the Ohio Board of Regents, that the pledge of fees by the University of Toledo in support of general receipts obligation bonds and/or bond anticipation notes in an aggregate amount not to exceed $14,000,000 is hereby approved.

The University of Toledo
November 2004 Fee Pledge Request - $14,000,000

A. Project Overview

The University of Toledo proposes to issue bonds to finance three capital projects:

- Central utilities upgrades
- Telecommunications infrastructure upgrade
- Real property acquisition

The University intends to issue 1-year bond anticipation notes that will be rolled over into 12- to 20-year general receipts obligation bonds when the University plans to issue a larger, more comprehensive bond issuance.

Initial Submission to the Board: October 2004

Revised Submission:

The University of Toledo
November 2004 Fee Pledge Request - $14,000,000

B. Project Financing and Costs

The University of Toledo requests the authority to issue 1-year bond anticipation notes that will be rolled over into 12- to 20-year general receipts obligation bonds in an aggregate amount not to exceed $14 million, to provide financing for three separate capital projects. The combined estimated project cost is estimated to be $15.3 million, for which the University has available $1.55 million in available resources.

The 1-year bond anticipation notes will have a 2.5% interest rate, and the longer-term general receipts obligation bonds will have an estimated interested rate of 5% and an estimated annual debt service payment of $1.2 million. According to the pro-forma provided by the University, the annual debt service and operating costs will be supported by energy savings and maintenance cost recoveries, deferred capital funds, available fund balances, and rental revenues.

A breakdown of the estimated project costs is presented below:

	Central Utilities	Telecomm. Infrastructure Upgrade	Research Space Acquisition	Total
Project Costs (Capital Only)				
Construction:	$6,960,194	$0	$0	$6,960,194
Moveable Equipment:	$0	$563,000	$0	$563,000
Architects and Engineers:	$340,000	$150,000	$0	$490,000
Land Acquisition/Preparation:	$0	$0	$2,650,000	$2,650,000
Capitalized Interest:	$0	$0	$0	$0
Contingency:	$534,782	$800,000	$0	$1,334,782
Other Costs (itemize):				$0
Administrative Fees	$160,024	$146,250	$0	$306,274
Installation	$0	$570,500	$0	$570,500
Pre-Bid Costs	$5,000	$0	$0	$5,000
Property Acquisition Costs	$0	$0	$100,000	$100,000
System & Software	$0	$2,300,000	$0	$2,300,000
Total Project Costs:	**$8,000,000**	**$4,529,750**	**$2,750,000**	**$15,279,750**
Project Resources (Capital Only)				
Gifts, Grants, etc. (non-state only)	$0	$0	$0	$0
State Capital Appropriations:	$0	$0	$0	$0
Transfers from Existing Resources	$0	$1,000,000	$0	$1,000,000
Other Revenue (itemize):				
Deferred Capital	$550,000	$0	$0	$550,000
Total Project Resources:	**$550,000**	**$1,000,000**	**$0**	**$1,550,000**
Amount to be Financed	**$7,450,000**	**$3,529,750**	**$2,750,000**	**$13,729,750**

The University of Toledo
November 2004 Fee Pledge Request - $14,000,000

C. Project Description

Central Utilities - $8,161,237

This project will bring central utilities, both steam and chilled water, south of the Ottawa River to serve both new and existing residence halls. The project will include the installation of a new absorption chiller in the Field House and both new chilled water and steam piping running south across the river to initially serve the Academic House, the International House, Parks Tower, the Crossings, and the FY 2006 Housing project. The project also incorporates portions of the facilities master planning project, such as a new pedestrian bridge over the Ottawa River just south of Wolfe Hall. The bridge will carry the needed utility lines under its structure and over the river, and at the same time enhance pedestrian circulation from the residence halls south of the river to the academic buildings on Centennial Mall. The new bridge is in keeping with the master planning principle of "celebrating" the river, and works well with the current master planning scenarios. The project will be phased over the next year; including connection to the FY 2006 Housing project now under construction and scheduled to open in fall of 2005.

Telecommunications Infrastructure Upgrade - $4,529,750

To meet the growing voice communication demands of students, faculty and staff, the University plans to upgrade its telecommunications capabilities. The infrastructure the University's telecommunications rely on was originally designed and implemented in the mid-1980's and expanded in the mid-1990's to meet the current and anticipated demands expected during those times. The University reports that the infrastructure has since come under serious strain to keep pace with new and diverse demands as well as the general growth in students, faculty and staff.

University and state capital investments in new and renovated facilities, including residence halls, have resulted in a sharp increase in the number of telephones on campus. The University's existing phone switch devices are nearly out of physical capacity to add more telephones in contiguous and manageable ranges. They are also well beyond the recommended hardware lifecycle and are beyond vendor maintenance. There are also no backup or failover capabilities in these devices. A failure in one could render much of campus without telephone communications. This presents significant risk to the University.

The University proposes to upgrade the campus telecommunications infrastructure and reposition the system for convergence with the campus data network when the network is upgraded to handle Voice over IP (VoIP) and other real-time applications. In accordance with a recent consultant's study, the goal is to upgrade existing NEC telecom equipment where possible and acquire new NEC equipment where necessary to create a hybrid VoIP enabled telecom system.

The project will be completed over the next year in anticipation of the FY2006 Housing project now under construction and scheduled to open in Fall of 2005.

Research Space Acquisition - $2,750,000

Due to an increasing need for research space and a commitment to engage with the community to develop the Research & Technology Corridor, the University has identified 2.68 acres of real property, including a research/office building of approximately 36,910 gross square feet for purchase. The property is adjacent to the University's College of Engineering and, most likely, will be the home of alternative energy and alternative fuel research by the University's Physics Department and Engineering College. The University also intends to lease space to private companies performing similar research in the interest of creating synergies between parties and providing for improved educational opportunities.

Pending Controlling Board approval, closing will take place on or about January 1, 2005. The University is currently developing several space utilization strategies that include external tenants who currently inhabit portions of this property.

The University of Toledo
November 2004 Fee Pledge Request - $14,000,000

D. 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 Toledo performed when these measures are applied to its FY 2001, FY 2002 and FY 2003 audited financial statements—the most up-to-date financial data available—and preliminary (unaudited) FY 2004 financial statements.

It is important to note that beginning in FY 2002, all campus's financial reports are prepared 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 are based on preliminary (unaudited - DRAFT) financial statements provided by the University of Toledo. The FY 2004 data shown in *italics* reflect the ratios and composite score when $14 million in proposed new debt and $1.2 million in related debt service 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 future retirement 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, and FY 2003 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 Toledo's viability ratios for FY 2001, FY 2002, FY 2003 and FY 2004 (preliminary) are as follows:

			PRELIMINARY	
FY 2001	FY 2002	FY 2003	FY 2004*	*FY 2004**
42.1%	58.0%	44.7%	52.6%	*48.6%*

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, and FY 2003 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 Toledo's primary reserve ratios for FY 2001, FY 2002, FY 2003, and FY 2004 (preliminary) are as follows:

			PRELIMINARY	
FY 2001	FY 2002	FY 2003	FY 2004*	*FY 2004**
18.9%	24.3%	25.6%	28.3%	*28.2%*

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, and FY 2003 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. The University of Toledo's net income ratios for FY 2001, FY 2002, FY 2003 and FY 2004 (preliminary) are as follows:

			PRELIMINARY	
FY 2001	FY 2002	FY 2003	FY 2004*	*FY 2004**
+5.6%	-2.2%	+4.7%	5.5%	*5.1%*

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. The University of Toledo's composite scores for FY 2001, FY 2002, FY 2003 and FY 2004 (preliminary) have been above the minimum threshold:

			PRELIMINARY	
FY 2001	FY 2002	FY 2003	FY 2004*	*FY 2004**
3.10	2.30	3.40	3.60	*3.60*

The University of Toledo
November 2004 Fee Pledge Request - $14,000,000

E. Financial Outlook and Bond Rating

Standard & Poor's recently reported that higher education institutions are likely to face more challenges in the future due to increased costs and physical plant needs. This uncertain outlook is also attributable to a change in students' educational needs and a changing demographic base. S&P believes this could affect the higher education sector's credit quality in the municipal market, which could cause institutional bond ratings to become more volatile. The S&P report also described the amount of investment needed to renew and upgrade technology in older higher education facilities as "staggering". [1]

The University of Toledo's existing debt has received relatively high marks from independent bond-rating agencies. UT's long-term debt was assigned a rating of *A* by S&P. Moody's Investors Services most recently assigned UT a bond rating to of *A2*.

These ratings indicate that UT's ability to meet its debt obligations is considered relatively strong. The table below illustrates Moody's and S&P's rating scale. Both companies generally use the same principals, criteria, and rating system. Moody's sometimes applies numerical modifiers to each rating category, with a modifier of 1 indicating the higher end of the category; a modifier of 2 indicating a mid-range ranking; and a modifier of 3 indicating the lower end of the category. Similarly, S&P's ratings may be augmented by a plus or minus sign to show the relative standing within these categories.

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).

[1] *The Bond Buyer* (online edition): "S&P: Higher Education Institutions to Face Challenges in Future" by Adam Cataldo, August 19, 2004.

The University of Toledo
November 2004 Fee Pledge Request - $14,000,000

F. 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. Between FY 1998 and FY 2003, aggregate net plant debt increased by 145% or $1.4 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 the University of Toledo, net growth in long-term plant debt increased by 92% or $82.9 million between FY 1998 and FY 2003. In response to a December 2003 survey of campuses, the University of Toledo reported that 100% 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.

Institution	Long-Term Plant Debt					
	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
UNIVERSITIES						
BOWLING GREEN	$41,050,000	$35,400,000	$32,035,000	$83,415,000	$79,255,000	$91,215,000
CENTRAL STATE	$3,983,721	$3,780,127	$3,572,922	$3,346,920	$3,192,444	$2,703,429
CLEVELAND STATE	$16,543,399	$16,420,347	$16,153,641	$12,393,540	$10,849,215	$55,977,422
KENT STATE	$65,490,000	$63,143,000	$81,774,000	$234,407,000	$290,735,000	$285,773,000
MCOT	$2,946,693	$2,883,387	$2,184,779	$1,229,464	$6,392,000	$8,837,000
MIAMI UNIV.	$50,499,010	$44,949,785	$49,018,070	$45,061,353	$53,168,773	$47,994,898
NEOUCOM	$0	$0	$0	$542,430	$1,583,286	$1,397,190
OHIO STATE	$222,557,597	$315,216,350	$365,192,650	$378,145,912	$581,106,000	$586,233,000
OHIO UNIVERSITY	$49,448,971	$79,696,363	$84,103,403	$132,049,339	$126,677,123	$133,002,202
SHAWNEE STATE	$3,707,230	$3,672,175	$3,599,407	$3,406,398	$3,200,000	$2,910,000
UNIV. AKRON	$29,591,298	$36,007,772	$59,014,572	$89,002,729	$191,864,557	$211,208,546
UNIV. CINCINNATI	$340,715,000	$365,895,000	$375,212,000	$577,365,000	$567,181,000	$647,688,000
UNIV. TOLEDO	**$89,660,778**	**$93,722,220**	**$88,467,721**	**$121,691,439**	**$119,376,000**	**$172,577,000**
WRIGHT STATE	$14,191,357	$15,669,753	$14,438,988	$13,232,584	$11,575,625	$18,570,323
YOUNGSTOWN ST.	$19,933,000	$19,096,590	$17,840,681	$16,368,157	$14,992,226	$14,263,619
COMMUNITY COLLEGES						
CINCINNATI ST.	$1,254,220	$771,204	$592,494	$423,417	$0	$49,173,132
CLARK STATE	$306,496	$0	$68,172	$47,234	$22,011	$0
COLUMBUS ST.	$15,022,102	$14,263,821	$14,108,529	$13,221,412	$12,330,217	$11,434,658
CUYAHOGA	$0	$0	$0	$4,083,210	$12,564,559	$59,095,229
EDISON STATE	$220,000	$0	$800,000	$800,000	$738,589	$68,676
JEFFERSON	$0	$0	$0	$0	$0	$0
LAKELAND	$30,000	$6,493,734	$6,445,224	$2,900,237	$2,441,594	$1,976,978
LORAIN	$77,449	$12,340,038	$9,806,212	$7,230,062	$5,426,817	$3,952,163
NORTHWEST ST.	$991,860	$0	$0	$0	$123,260	$106,207
OWENS STATE	$12,947,278	$136,892	$141,049	$206,317	$0	$0
RIO GRANDE	$0	$0	$0	$0	$0	$0
SINCLAIR	$0	$0	$0	$0	$0	$0
SOUTHERN ST.	$371,229	$259,010	$138,968	$155,855	$122,950	$168,506
TERRA STATE	$5,121	$0	$0	$49,805	$42,710	$35,171
WASHINGTON ST.	$0	$0	$0	$0	$0	$0
TECHNICAL COLLEGES						
BELMONT TECH	$0	$0	$0	$0	$126,878	$97,927
COTC	$367,493	$337,831	$305,307	$270,726	$231,348	$186,826
HOCKING	$1,862,829	$1,871,748	$1,873,504	$4,311,120	$5,213,938	$497,794
JAMES RHODES ST	$0	$0	$0	$0		$0
MARION TECH	$0	$0	$0	$0		$0
ZANE STATE (MATC)	$0	$0	$0	$0	$0	$182,571
NORTH CENTRAL	$920,656	$775,048	$703,213	$744,479		$375,474
STARK STATE	$20,307	$143,311	$308,942	$259,870	$763,399	$620,993
STATEWIDE TOTAL	$984,715,094	$1,132,945,506	$1,227,899,448	$1,746,361,009	$2,101,296,519	$2,408,322,934