# LOYOLA UNIVERSITY OF CHICAGO

## Debt Policy

Debt is viewed as a continuing component of the balance sheet of Loyola University of Chicago ("LUC", "Loyola" or the "University"). In support of its mission and strategic objectives, Loyola may utilize various forms of debt financing to pay for costs associated with acquisition and construction of capital assets and to provide for liquidity and cash flow requirements. This Debt Policy sets forth guidelines applicable to the issuance and administration of debt, the issuance of which is subject to review by the University's Finance Committee and approval of the University's Board of Trustees.

### A. Debt Administration and Oversight

The University's Chief Financial Officer is responsible for management of the University's debt portfolio according to this Debt Policy and consistent with other applicable University polices and board resolutions. Management of debt-related matters and any oversight or reporting requirements in this policy may be delegated by the Chief Financial Officer to the University's Treasurer. Prior to the incurrence of debt (including all short and long-term obligations, guarantees, and other material debt instruments, excluding bank liquidity lines of credit), the Chief Financial Officer will present the proposed transaction to the Finance Committee and seek its recommendation for approval by the Board of Trustees.

The Chief Financial Officer or the Treasurer will report at least annually to the Finance Committee on the status of the University's debt portfolio and on any plans regarding debt. This review will include, among other topics, An assessment of the University's maintenance of certain credit metrics consistent with an investment grade credit rating. (Exhibit I)

### B. Principles Governing Use of Debt

Unless otherwise determined by the Board of Trustees:

- The University may incur long-term debt for general corporate purposes, which include those things which further the corporate mission, including to acquire and construct capital assets.
- Under appropriate circumstances, short-term debt may be issued to finance cash flow or other operational needs. It may also fund capital projects expected to be refinanced with long-term debt, so long as a plan for such a refinancing is approved at the time of the short-term financing.
- Debt will not be incurred unless projected debt service requirements (principal and interest payments, including any net swap payments) and operating costs associated with any new capital improvements financed by the debt can be accommodated within the University's future operating budget.

- The University will seek to maintain financial metrics generally consistent with an investment grade rated University.
- The University will seek to maintain a debt portfolio that balances the useful life of capital assets or projects financed with debt, interest rate risk, and the long-term cost of capital.
- The University's debt portfolio will be evaluated in the context of all of its assets and liabilities. Diversification within the debt portfolio will be used to balance risk and liquidity.
- Capital and operating leases are financing tools that may be utilized, where appropriate, to help achieve the University's objectives concerning the use of debt.

## C. Debt Capacity

In general, the University's debt capacity will be evaluated and determined by consideration of the following factors:

- Legal authorizations and limitations.
- Current and pro forma financial operating performance and liquidity.
- Credit considerations, including the University's Debt Policy objective to maintain financial metrics consistent with an investment grade rated higher education institution.
- Debt capacity considerations among financing partners.

The University will comply with any applicable debt covenants and Board-imposed limitations for determining the feasibility of new indebtedness.

The University's debt capacity and/or debt affordability is in part a function of current and pro forma operations, balance sheet size, capital planning, investment objectives, and liquidity levels, among other factors. While a target range may be considered, annual debt service as a percentage of the operating budget can be expected to vary over time as the University makes judgments about its highest priorities and needed investments.

Credit considerations encompass a broad array of factors that affect how the University is viewed by financial and capital markets. Many of these factors may be analyzed by credit rating agencies in determining the University's credit rating, which is an important reflection of the University's operating, management and financial strengths, and a significant determinant of both its access to and cost of capital.

## D. Bond Ratings

The University currently has long-term bond ratings from the nationally recognized bond rating agencies Moody's Investors Service and Standard & Poor's Financial Services. The University is committed to ensuring that actions within its control are prudent and appropriate to maintain a rating that is consistent with this Debt Policy.

There is a high correlation between an institution's credit rating and its cost of borrowing. This Debt Policy assumes an objective to maintain long-term bond ratings in an investment grade category.

**E. Projects That May be Considered for Debt Financing**

The University will utilize long-term debt financing generally for capital projects, unless otherwise approved by the Board. In general, this will include:

- Capital projects where it is unlikely that sufficient donor funding for the project will be secured.
- Capital projects where all or the majority of the project is to be funded through gifts and contributions; however, the timing of payment of those gifts and pledges may not match cashflows during or that extend beyond the construction period.
- Capital projects which are projected to generate sufficient cash flow to cover operating expenses that substantively cover the full costs of debt service.

**F. Other Considerations Regarding the Use of Debt**

1. Term of Debt

The University will determine the appropriate final maturity and the specific amortization schedule of a proposed debt issue by evaluating its overall debt portfolio. Considerations will include the life of the assets being financed, interest rate costs, risk assessment, general market conditions, and the University's future financial plans. The University has a practice whereby principal is funded by a general asset reserve over the life of the debt issuance to assure that the principal payments will not duly impact the operations of any one fiscal year. It is the University's intentions to continue to fund principal through this asset reserve in compliance with this debt policy.

2. Refinancing and Restructuring of Debt

The Chief Financial Officer and the University's licensed financial advisor, in consultation with the University's external financing partner, will periodically review all outstanding debt to determine if refinancing opportunities exist. Refinancing or restructuring of current debt may be done to benefit the University's financial, operational, or strategic position.

3. Use of Tax-Exempt versus Taxable Debt

In determining whether to use tax-exempt or taxable debt for a given capital project, the University should analyze both alternatives. Considerations in this analysis may include the following:

- Tax law limitations on use of tax-exempt financing.
- Rate, costs, and speed of issuance.
- Market conditions.
- Project use and operating flexibility.

4. Use of Call Options

The University will consider the use of call options to provide flexibility in its debt portfolio. In considering the use of non-callable bonds, bonds with substantive call penalties, or make whole calls, the University will be expected to evaluate factors such as the value of the call, the cost of the call, and the total debt service under these options to overall payments under scenarios involving more traditional, callable structures. The use of callable, non-callable debt, make whole call or debt with call penalties may be undertaken for other reasons, even if it does not necessarily provide the lowest possible debt service for the University.

5. Internal Loans

Internal loans may be considered when the available operating or external resources are either insufficient or when an internal borrowing solution confers strategic benefits vis-s-vis traditional borrowing approaches. Internal loans should be funded from immediately available funds of the University that do not have donor restrictions that would be violated.

To use an internal loan, the Chief Financial Officer will provide to the Finance Committee a written justification for the use of this financing approach. Included in the justification should be a) a description of the borrowing need, the amount requested, and the interest rate to be applied; b) the time frame over which funds will be expended and the debt amortized; c) the other borrowing options that have been considered; and d) why an internal loan is favored over other more traditional options.

## G. Acceptable Approaches for Debt Structure

1. Mix of Fixed and Variable Rate Debt

The University may structure its overall debt portfolio using a combination of fixed and variable rate debt to provide a balance between interest rate risk and the cost of capital.

Variable rate debt allows the University greater diversification in its debt portfolio and may reduce its overall interest costs. In addition, variable rate debt typically can be pre-paid more readily, which can provide greater flexibility in debt management. However, the use of variable rate debt also increases interest rate risk as a result of market fluctuations, can expose the University to the interest rate effects of tax law changes and may present liquidity risk for the most traditional variable products (and potential counterparty risk if the University purchases external liquidity).

The amount of variable rate debt maintained by the University can and should vary depending on market conditions. When financings are being considered in a low interest rate environment, it may be prudent to secure fixed-rate or synthetically fixed-rate financing. In high interest rate environments, variable rate financings may be preferable because:

- Publicly placed variable rate debt typically includes any-time call flexibility for traditional structures, allowing for the University's ability to refinance into fixed rate modes in future and more attractive interest rate periods.
- Variable rate debt has lower historical average rates than fixed rate debt.

- Variable rate borrowing levels can trend in the same direction as market-wide interest rate indices, such as Fed Funds or SOFR.

Risks of publicly issued variable rate debt include:

- Interest rate risk: Rate resets are subject to market forces and may increase borrowing cost over the budgeted rate or the rate of fixed rate debt.
- Put risk: Traditional variable rate debt is puttable in daily/weekly reset modes – the University must have enough available liquidity (required to demonstrate this to rating agencies) to fund the investor put option. This can be in the form of internal liquidity or externally purchased liquidity from a bank provider.
- Bank risk (*pricing*). If external liquidity is purchased from a bank to support the bonds to provide liquidity support for the put feature on any variable bonds, the University is exposed to price changes at the end of each term of the liquidity support.
- Bank risk (*credit risk*). If external liquidity is purchased from a bank to support the liquidity requirement, the bonds are exposed to credit risk of the bank (an outside party). Any material credit risk to banks (e.g. downgrades) will expose the University's bonds to potential changes in rate, thus leading to interest rate risk.
- Remarketing risk. The risk that bonds cannot be placed to investors at any acceptable rate.

Likewise, fixed rate debt provides a different set of advantages and considerations for the University. Fixed rate is known as the most conservative form of debt that ensures a known debt service obligation for the University, which can assist management in planning and budgeting. In low interest rate environments, fixed rate debt can provide financing at relatively low cost for extended periods of time with all future risks transferred to investors at the time of bond sale. Considerations of fixed rate debt are the higher yields in the fixed rate market and less call flexibility compared to publicly-placed variable rate debt (fixed rate debt generally has a 10-year par call, compared to variable rate debt that traditionally has an anytime par call).

2. <u>Interest Rate Swaps and Other Derivatives</u>

The use of interest rate swaps and other derivative products may be appropriate interest rate management tools that can help the University meet important financial objectives. These instruments may hedge risk, increase the University's financial flexibility, provide opportunities for interest rate savings and/or help the University manage its balance sheet through better matching of assets and liabilities. Swaps may be integrated into the University's overall debt management guidelines and should not be used for speculation or leverage.

The University may use interest rate swaps and other derivative instruments if it is reasonably determined that the proposed transaction allows the University to:

- Optimize its capital structure, including its schedule of debt service payments.
- Achieve an appropriate asset/liability match.

- Reduce risk, including:
  - Interest rate risk
  - Tax risk
  - Liquidity renewal risk
- Provide greater financial flexibility.
- Generate interest rate savings.
- Manage exposure to changing markets in advance of anticipated debt issuances (through the use of anticipatory hedging instruments).

Among others, the University may utilize the following financial instruments on a current or forward basis, after identifying the objective(s) to be realized and assessing the risks.

- Interest rate swaps, including fixed, floating and/or basis swaps.
- Interest rate caps/floors/collars.
- Options, including swaptions, caps, floors, collars, and/or cancellation or index-based features.

This list is not intended to be a limitation on other derivative instruments that the University may consider and use. A longer discussion of swaps and derivatives, as well as their advantages and disadvantages, can be found in the University's Interest Rate Swap Policy.

3. Authorization

The Chief Financial Officer will consult a licensed financial advisor with experience in structuring hedging agreements prior to entering into these agreements and must receive approval from the Board of Trustees prior to entering into any swap or derivative product arrangement related to the University's debt. The University's Finance Committee will evaluate the recommendation of the Chief Financial Officer regarding the use of such instruments and will evaluate its appropriateness in meeting the University's financial objectives before making a recommendation to the Board of Trustees for approval.

## H. Payment of Debt Service

The University assumes that the operating budget will fund interest and swap cashflow payments, and the internal bank will fund principal payments on debt. Other sources may include permitted endowment revenue and pledge payments related to Capital Campaign or University Advancement activities.

Where the University identifies a capital project to be funded through the issuance of long-term debt, and if that debt service is to be funded entirely through operations and the internal bank, Loyola will undertake financial modeling to determine the capital project's impact on operations. The modeling will assess whether:

- Financing the project will allow the University to meet existing and the proposed financial covenants in loan and bond agreements;
- Net revenues produced by the project are sufficient on their own to cover debt service; or
- If the project does not on its own support its related debt service, it can be demonstrated that projected University-wide cash flow available for debt service is sufficient to cover incremental debt service, while meeting the financial metrics consistent with an investment grade rated institution.

Where the University identifies a capital project to be funded through the issuance of long-term debt and is supported by revenues to be generated by the new project, the projected revenues will flow through the operating budget. In evaluating debt on a new revenue-generating project, special attention will be given to projects that are replacing an existing revenue generating project that is planned to be decommissioned. The revenue generated on the new project should be evaluated to determine if it can replace revenue generated from the decommissioned facility, as well as satisfy the debt service on the new project.

In cases where the University issues tax-exempt debt for cash flow purposes based upon a schedule of pledge payments to be received, the University will utilize those pledge payments to pay off the debt, as required by IRS regulations.

## I. Reporting Requirements

The University's Chief Financial Officer will present to the University Finance Committee of the Board of Trustees no less than annually the following information:

- A schedule of existing debt highlighting the structure of each component of the debt, the next call date, if any, as well as the financial covenants associated with each facility. In the case of variable rate debt, renewal dates should also be highlighted.
- A report on derivative agreements entered into by the University, if any. Information provided will include, but not be limited to:
    - the amortization (if any) and maturity date of the derivative instrument,
    - its most recent marked-to-market valuation on the balance sheet,
    - whether and under what circumstances the derivative product is subject to early termination.
- A current calculation of the University's financial metrics in comparison to investment grade university rating agency medians and select peer institutions, as well as the most recent calculation of the financial covenants.
- An affirmation from the Chief Financial Officer or Treasurer that Loyola is in compliance with all financial and reporting covenants included in its debt documents, and that obligations under the University's tax-exempt post-issuance compliance policy and IRS regulations have also been met.

- A list of upcoming decision points associated with the debt portfolio.

Approved by the Finance Committee on 12/11/2024.

Additional References:
- Interest Rate Swap Policy
- Tax-Exempt Bond Post-Issuance Compliance Policy

# EXHIBIT I

## Financial Metrics

This is not an exhaustive list of financial metrics. The list may change over time due to changes in industry and rating agency metrics, as well as changes to accounting standards.

### Leverage Ratio

$$\text{Leverage Ratio} = \frac{\text{Cash and Investments}}{\text{Outstanding Debt}}$$

The Leverage Ratio is an indicator of the ability to repay debt over time. It is a measure of total financial assets versus debt. Higher is better.

### Debt Coverage Ratio

$$\text{Debt Coverage Ratio} = \frac{\text{Net Income from Operations plus Interest, Depreciation, and Amortization}}{\text{Outstanding Debt}}$$

The Debt Coverage Ratio is a measure of the University's ability to repay existing and additional indebtedness and the debt's impact on available cash flow. The ratio shows whether operating cash flow is maintained relative to changes in the level of debt. Higher is better.

### Debt Burden Ratio

$$\text{Debt Burden Ratio} = \frac{\text{Total Debt Service}}{\text{Total Expenses}}$$

The Debt Burden Ratio measures the University's ability to repay the principal and interest associated with all outstanding debt and the impact on the overall budget. This ratio uses aggregate expenses as opposed to revenues because expenses typically are more stable. Lower is better.

# EXHIBIT II

## Financial Covenant

Debt Service Coverage
Calculation as of June 30, 2023

| | FY 2023 |
|---|---|
| Revenues[1] | $ 655,589 |
| Expenses[2] | $ 634,884 |
| Operating Income | $ 20,705 |
| *plus* | |
| Depreciation & Amortization | $ 57,893 |
| Interest Expense | $ 8,786 |
| **Income Available for Debt Service** | **$ 87,384** |
| | |
| Capitalized Lease Obligations (FY 22 Audit) | $ - |
| Scheduled Maturities of Debt (FY 22 Audit) | $ 11,153 |
| Interest Expense (FY 23 Audit) | $ 8,786 |
| **Debt Service Requirements[3]** | **$ 19,939** |
| | |
| **Debt Service Coverage Ratio[4]** | **4.38** |

[1] Defined as, for any period, (a) for the Borrower, the sum of (i) tuition and fees, net of scholarships, plus (ii) all other revenues classified as "Operating Revenues" in or derived from the audited financial statements of the Borrower and (iii) excluding all non-operating revenues, income derived from the sale of assets not in the ordinary course of business or any gain from the extinguishment of debt or other extraordinary item, or earnings which constitute Escrowed Interest or earnings on amounts which are irrevocably deposited in escrow to pay the principal of or interest on Indebtedness and (b) in the case of any other Person, gross revenues less sale discounts and sale returns and allowance, as determined in accordance with GAAP; but (c) excluding in any event, (i) any realized or unrealized gains or losses resulting from changes in the value of investment securities, and (ii) any gains on the sale or other disposition of fixed or capital assets not in the ordinary course; provided, however, that if such calculation is being made with respect to the Borrower and any Affiliate, such calculation shall be made in such a manner so as to exclude any revenues attributable to transactions between the Borrower and any such Affiliate.

[2] Defined as, for any period, for the Borrower, all expenses classified as "Operating Expenses" in or derived from the Audited Financial Statements of the Borrower; but excluding in any event, (a) any realized or unrealized gains or losses resulting from changes in the value of investment securities and (b) extraordinary expenses (including, without limitation, any losses on the sale or other disposition of fixed or capital assets not in the ordinary course and losses on the extinguishment of debt); *provided, however*, that if such calculation is being made with respect to the Borrower and any Affiliate, such calculation shall be made in such a manner so as to exclude any expenses attributable between the Borrower and any such Affiliate.

[3] Defined as, for any period being measured, Interest Expense for such period, *plus* the scheduled maturities of Indebtedness having an original term of more than one year (including but not limited to amortization of Capitalized Lease obligations) as reported in the Borrower's audited financial statements for the Fiscal Year prior to the period being measured.

4 Different financial institutions may have different minimum thresholds for the covenant.