Title: Debt Management Guidelines and Procedures **Policy: 1500**

Purpose

a. To provide guidance to Virginia State University in undertaking long-term debt obligations benefiting the University.

b. To provide a structured framework for the issuance of long-term debt obligations that supports the mission and strategic objectives of the Institution.

c. To provide an ongoing process for the University to evaluate the level of its annual debt service support and consolidated debt burden.

d. To document the exercise of due diligence in the execution and/or management of the University debt portfolio and use of its financial resources.

e. To assist the University in achieving and/or maintaining credit ratings necessary to be eligible for authority under the Restructured Higher Education Financial and Administrative Operations Act.

Authority, Responsibility, and Duties

a. The Board of Visitors of Virginia State University is authorized, in Title 23, Chapter 10 of the *Code of Virginia* to operate and manage the Institution. The Debt Management Guidelines and Procedures will be reviewed periodically and modified as necessary by the Board of Visitors.

b. The President, acting through the Vice President for Finance and CFO, shall be the primary person responsible for the development, implementation, and execution of the Virginia State University Debt Management Guidelines and Procedures. The Vice President for Finance and CFO shall be responsible to the President of Virginia State University in the implementation of these Debt Management Guidelines and Procedures.

c. The President, acting through the Vice President for Finance and CFO, will ensure that these Debt Management Guidelines and Procedures meet the debt guidelines promulgated by the Commonwealth of Virginia Treasury Board.

Definitions

a. **Annual Debt Service Cost** – The maximum annual debt service cost (principal and interest payments) payable within any fiscal year on the University's Direct Debt reduced by any amounts whereby the agreed upon funding source is from the University Foundations.

b. **Bond Counsel** – An attorney (or firm of attorneys) retained by the issuer to give a legal opinion that the issuer is authorized to issue proposed securities, the issuer has met all legal requirements necessary for issuance, and interest on the proposed securities will be exempt from federal and/or state income taxation. Typically, bond counsel advises the issuer on statutory requirements, prepares authorizing resolutions or ordinances, trust indentures, official statements, closing documents and other documents required for the issuance of securities, conducts validation proceedings and supports the issuer in the event of litigation.

c. **Capitalized Interest** – A portion of the proceeds of an issue set aside to pay interest on the securities for a specified period of time. Interest is commonly capitalized for the construction period of a revenue-producing project.

d. **Capital Lease** – Shall have the same meaning as the term is defined in the Commonwealth Accounting Policy and Procedures (CAPP) Manual.

e. **Call/Redemption** – A transaction in which the issuer returns the principal amount represented by an outstanding security (plus, in some cases, an additional amount or "premium"). Redemption can be made at maturity of the security, as a result of the issuer's call of the securities prior to their stated maturity date, or in the case of variable rate debt, as a result of the security holder's election to exercise a put or tender option privilege.

f. **Call Provisions** – The terms of the bond contract giving the issuer the right, or requiring the issuer to redeem or "call" all or a portion of an outstanding issue of bonds prior to their stated dates of maturity at a specified price, usually at or above par and stated as a percentage of the principal amount called.

g. **Debt Service Reserve Fund** – The fund in which moneys are placed which may be used to pay debt service if pledged revenues are insufficient to satisfy the debt service requirements. May be funded with bond proceeds, or it may only be partly funded at issuance and reach its full funding requirement over time. If allowed in the bond documents, a surety policy from a bond insurance company or other qualified provider may be used to satisfy the Debt Service Reserve requirement.

h. **Direct Debt** – Direct obligation of University incurred to fund Capital Projects reduced by the amount of Direct Debt whose agreed upon repayment source is from the University Foundations.

i. **Financial Advisor** – A consultant who advises the issuer on matters pertinent to the issue, such as structure, timing, marketing, fairness of pricing, terms and bond ratings.

j. **General Revenue Pledge** – Bonds or other obligations secured by the general operating revenues (rather than specific project revenues) of an institution of higher education. General operating revenues may include total gross university sponsored overhead, unrestricted endowment income, tuition and fees, indirect cost recoveries, auxiliary enterprise revenues, general fund appropriations and other revenues not required by law to be utilized for another purpose.

k. **Gross Funding** – Issuing the entire amount of the bond authorization with the intent to use any earnings on proceeds to pay additional project costs. Contrast with Net Funding.

l. **Moral Obligation Debt** – Refers to the structure under which the state or University pledges to consider replenishing a deficiency in the debt service reserve fund arising from the need to draw money from the fund when the underlying project revenues prove to be insufficient to service the debt.

m. **Net Funding** – A method of sizing the bond issue in which projected earnings on the bond proceeds are taken into account as a source of funds for project costs using anticipated spending schedules and an assumed rate of investment earnings. This results in a smaller overall issue size.

n. **Present Value** – The value at the current time of a cash payment or stream of payments which is expected to be received in the future, allowing for the fact that an amount received today could be invested to earn interest until the future date(s).

o. **Present Value Savings** – A method of calculating the aggregate amount of savings on a refunding transaction. In each semi-annual period, the present value of the debt service on the Refunding Bonds is subtracted from the present value of the debt service on the refunded Bonds using the arbitrage yield on the refunding bonds as the discount rate. The present value savings in each year are added together to result in the aggregate Present Value Savings.

p. **Present Value Savings Percentage** – The Present Value Savings divided by the principal amount of the Refunded Bonds.

q. **Refunding** – A procedure whereby an issuer refinances outstanding bonds by issuing new bonds. Bonds are usually refunded to either reduce the issuer's interest costs or to remove a burdensome or restrictive covenant imposed by the legal terms of the bonds being refinanced. The new bonds are called the "refunding bonds," while the bonds being refinanced are called the "refunded bonds." An Advance Refunding is a type of refunding where outstanding securities are refinanced by the proceeds of a new issue of securities more than 90 days prior to the date on which the outstanding securities become due or are callable. The proceeds of the new securities are deposited in escrow and invested in U.S. Government or federal agency securities, with principal and interest on the escrowed securities used to pay principal and interest on the refunded bonds up to and including the Redemption or Call. The Internal Revenue Code restricts the yield on such escrowed securities. A Current Refunding is a type of refunding where the proceeds of the new bonds are used within 90 days of closing to retire the refunded obligations. If the proceeds are not used immediately (i.e., on the day of closing) to retire the refunded obligations, it may still be necessary to establish a portfolio of escrow securities. However, the Internal Revenue Code does not impose the same yield restrictions on Current Refundings that they do on Advance Refundings.

r. **Terms and Structure** – As it relates to §2.2-2416 of the Code of Virginia, "terms and structure" is deemed to include the following: type of debt instrument/obligation, security, size, method and timing of sale, interest rate structure, principal amortization method, call provisions, number and level of credit ratings, investment of proceeds, credit enhancements, synthetic features, (e.g., caps, floors, forwards, swaps), disclosure, refunding parameters, method of selection of financing team, etc.

s. **True Interest Cost ("TIC")** – Also known as "Canadian Interest Cost." A method of computing the issuer's cost defined as that rate, compounded semi-annually, that is necessary to discount the amounts payable (on the respective principal and interest payment dates) to the purchase price received for the new securities, excluding accrued interest.

t. **Trustee** – A financial institution with trust powers that acts in a fiduciary capacity for the benefit of the bondholders in enforcing the terms of the bond contract.

u. **Underwriter** – A firm that purchases a new issue of municipal securities for resale.
The underwriter may acquire the securities either by negotiation with the issuer (e.g., RFP) or by award on the basis of competitive bidding.

v. **Underwriter's Counsel** – An attorney or law firm retained to represent the interest of the underwriters in connection with the purchase of a new issue of municipal securities. The duties of the underwriter's counsel may include review of the issuer's bond resolution or ordinance and documentation on behalf of the underwriter, review of the official statement to determine the adequacy of disclosure, negotiation of the agreement among underwriters and preparation of the due diligence opinion.

Policy Statements

a. Capital Projects

1. Only capital projects that directly benefit the University should be financed by the University.
2. All capital projects to be financed must be part of the University's approved Master Development Plan
3. Capital projects funded with revenues of the University (tuition and fees, unrestricted gifts, investment income, as well as existing assets) should be funded with long-term obligations.
4. Capital projects funded with restricted gifts and/or pledges should be considered for funding with comparable term obligations.
5. Working capital needs should not be financed except where economic conditions exist that provide unique benefits to the University from the execution of an interim financing.
6. Capital projects delivered through alternative financing approaches such as the Public-Private Education Facilities and Infrastructure Act of 2002 should satisfy conditions in the Debt Management Guidelines and Procedures of the University if the University is issuing long-term debt or executing a long-term capital financing lease.
7. All debt issuances should be coordinated with the University's capital planning process.

b. Approvals

1. All Debt Obligations and Synthetic Products undertaken by the University shall be first approved by the President, acting through the Vice President for Finance and CFO, of the University.
2. All Debt Obligations and Synthetic Products undertaken by the University shall be approved by the Board of Visitors of the University or its designee.
3. All capital projects undertaken by the University shall be specifically authorized by the Commonwealth of Virginia in accordance with State law, regulations or policy.

c. Capital Funding

Prior to the issuance of any amount of debt, the Vice President for Finance and CFO shall prepare an analysis detailing the funding source(s) for the debt repayment, documenting that all principal and interest payments on the proposed debt service can be funded for such debt.

1. If the security for any capital financing program is a general revenue pledge of the University, the total resources of the University shall be made available to pay this debt service.
2. If the proposed funding source is from future gifts from the Foundations or other individual donors, then the Vice President for Finance and CFO shall ensure:
   - At least 70% of the gifts shall have been pledged at the time of the debt issuance. These pledges should have a high degree of confidence for collection and an appropriate amount provided as uncollectible;
   - At least 20% of the amount of the pledged gifts shall have been received at the time of debt issuance; and
   - An alternative funding source shall be identified to fund the applicable debt service should the gifts not be received as scheduled.
3. If the proposed funding source is from future general revenue of the University:
   - The operating budget of the University shall be modified to reflect this use of these net revenues.
4. If the proposed funding source is from existing assets of the University:
   - The existing assets shall be valued at that time and separated from other existing assets and invested in such a manner as to preserve the principal value of the asset to ensure that it will be sufficient to pay annual debt service when needed.
5. If the proposed funding source is based on alternative financing guidelines:
   - The Financing Plan shall be approved by the Vice President for Finance and CFO of the University in a manner consistent with the Debt Management Guidelines and Procedures.

d. Terms & Structure

The University will seek the lowest cost source of financing available while ensuring that its overall debt structure is not exposing the University to unnecessary future interest rate risk.

1. For self-supporting revenue bonds, the University should utilize the Commonwealth Treasury Board General Obligation Revenue Bond Financing Program authorized by Article X, Section 9 C of the Constitution of Virginia.
2. For other University debt obligations, the University should utilize the Virginia College Building Authority ("VCBA") unless a financing alternative is clearly superior to this VCBA pooled loan program.
3. For equipment or other energy related projects, the University may request financing through the Department of Treasury's Master Equipment Lease Program (MELP), through other Treasury financing options, or from private sources (with Treasury approval) when doing so better meets the needs of the Institution and when it either achieves an overall lower cost of funding or more favorable repayment terms.

4. All available structures should be reviewed prior to adopting a final plan of finance. The review should include, but not be limited to, an analysis of:
    - Fixed Rate, Variable Rate, and Synthetic Alternatives
    - Bank Qualified Designations
    - Public Sale or Private Placement
    - Credit Enhanced, Stand-Alone Credit, or Non-Rated Credit Transactions
    - Long-term, Short-Term, or Interim Financing Alternatives
    - Tax-Exempt or Taxable Financing
5. The average life of the indebtedness should not be greater than the average economic life of the asset being financed.
6. The debt should be amortized over the useful life of the assets financed; however, in no case shall the final maturity of the debt be in excess of 25 years without the expressed approval of the Board of Visitors.
7. The use of capitalized interest should be minimized whenever possible.
8. Debt should amortize in an expedited manner with a goal of 50% of the debt being amortized within the first 15 years.
9. Debt Service Reserve Fund's should be considered to enhance the security of the debt issue.
10. Debt should be structured in a manner that allows the coordination of borrowings and minimizes the effect of negative arbitrage on the borrowings.
11. The following ratios should be maintained based on the proposed financing:
    - Maximum Annual Debt Service Costs as a percentage of total Operating Expenses shall not exceed 7% for non-revenue producing capital projects. The debt burden ratio may exceed 7% in instances involving debt of revenue producing capital projects when such obligations are secured by income associated with the project.

e. Refinancing Obligations

The University should endeavor to keep track of its existing indebtedness (Direct, Indirect, or Synthetic) in an effort to reduce the annual debt service costs to the University.

1. For any debt obligations refunded to provide annual debt service savings, the following net present value savings thresholds shall generally apply:
    - 5% if call date is more than 5 years form the date of the refunding;
    - 3% if call date is within 5 years from the date of the refunding;
2. The final maturity on any Refunding Bonds should not generally exceed the final maturity on the refunded bonds.

3. Refunding's executed to provide relief from burdensome financial covenants or reduced annual debt service cost shall be approved by the Virginia State University Board of Visitors.

4. For Refunding Bonds, the University will seek to achieve approximate level annual debt service savings compared to the Refunded Bonds.

f. Synthetic Products

The University may desire to enter into contracts ancillary to its actual debt instruments. These contracts may include interest rate swaps, floors, caps, swaptions, and/or other derivative types of products.

1. These contracts are not to be used for speculative purposes, but may be used:
   - To achieve lower overall cost of funds
   - To hedge interest rate risk
   - To increase financial flexibility or
   - For other purposes as deemed appropriate

2. All contracts should be based on and contain the terms and conditions set forth in the International Swap and Derivative Association, Inc. ("ISDA") Master Agreement.

3. Contracts with counterparties must be rated at least in the "A" Category by National Rating Agencies as long as the transaction is appropriately collateralized. Counterparties with credit ratings in the "AA" category are exempt from the collateral requirement.

4. Prior to the execution of a Synthetic Product, the President, acting through the Vice President for Finance and CFO, should prepare a Recommended Financing Plan for Synthetic Products for review by the Board of Visitors. This plan shall include:
   - The objective of the use of the Synthetic Product
   - The type of Synthetic Product to be used
   - Identification of potential risks of the Synthetic Product
   - The firm (counterparty) to be used to provide the Synthetic Product
   - Structural provisions of the Synthetic Product
   - The termination provisions of the Synthetic Product and collateralization requirements
   - What annual/quarterly reporting guideline will be required
   - Bond Counsel and Financial Advisor role in procuring the Synthetic Product

g. Reporting Requirements

Prior to the issuance of debt, the President, acting through the Vice President for Finance and CFO, shall prepare a Recommended Plan of Finance for review by the Board of Visitors.

1. The Recommended Plan of Finance shall include the following items:
    - Purpose of the Financing
    - Security and/or Source of future debt service payments
    - Description of the proposed sale (fixed, variable, synthetic, etc.) and how determined
    - Legal authority to undertake the project
2. Structural components of proposed issuance:
    - Projected Use of Synthetic Products
    - Significant Financial Covenants
    - The percentage of maximum annual debt service to Unrestricted Operating Expenses
    - Capitalized Interest
    - Proposed amortization
    - The percentage of total debt to Unrestricted and Temporarily Restricted Net Assets
    - Debt Service Reserve Fund
    - Call Provisions
    - Credit Enhancement, if any
    - Expected annual debt service costs
    - Estimated issuance costs
    - Expected Credit Rating, if applicable
3. If the Recommended Plan of Finance includes the use of a Synthetic Product, then a Recommended Financing Plan for Synthetic Products shall also be prepared.
4. On an annual or other periodic basis, the President, acting through the Vice President for Finance and CFO, shall review and make recommendations on any required changes to the Virginia State University Debt Management Guidelines and Procedures.
5. On an annual basis, the Vice President for Finance and CFO shall prepare a report for review by the Virginia State University Board of Visitors. This report shall include:
    - Direct Debt Obligations of the University
    - Direct Debt Obligations of the University Foundations (on behalf of Virginia State University)
    - Amount of variable and fixed rate indebtedness and any recommendation as to the composition of this debt
    - Existence and market value of any Synthetic Transactions
    - Status of fund raising and pledges used to support previous debt issuance

- Projected annual debt service cost and projected funding of Direct, Indirect, and Synthetic based debt issues for the next three-year period
- Status of Credit Agreements being used as Credit Enhancement
- Compliance with all significant financial and operating covenants of existing indebtedness
- Additional debt capacity of the Foundations based on existing Financial Covenants
- Direct or Indirect Debt expected to be issued during the next 12 months
- Planned Synthetic transactions during the next 12 months
- Status of any Arbitrage Rebate calculations on existing debt issues
- Estimated annual debt service savings available from refunding existing Direct, Indirect, or Synthetic debt of the Alumni Agencies

References

Code of Virginia, Title 23 Chapter 10, §2.2-2416

VSU "Master Development Plan"

ISDA "Master Agreement"

Approved By:

H. Black

Harry Black, Rector

Thursa D. Crittenden

Thursa Crittenden, Secretary

9/15/17

Date

9.15.17

Date