



## REQUEST FOR BOARD OF TRUSTEES ACTION

**Committee:** Audit and Oversight

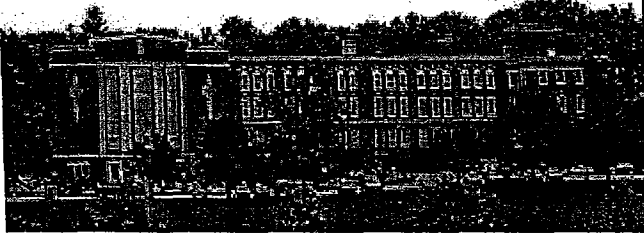
**Title:** Approval of the Proposed College Debt Policy

**Date:** January 24, 2007

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**Recommendation:** That the Board of Trustees approve the attached proposed Debt Policy for the College.

**Justification:** At the request of the Board of Higher Education, through its proposed Debt Policy Guidelines dated March 16, 2006, each Massachusetts community college must submit a Debt Policy to the Board of Higher Education for its approval. The proposed Quinsigamond Debt Policy was drafted based upon a model developed by the University of Vermont and models now being proposed by several other Massachusetts community colleges.



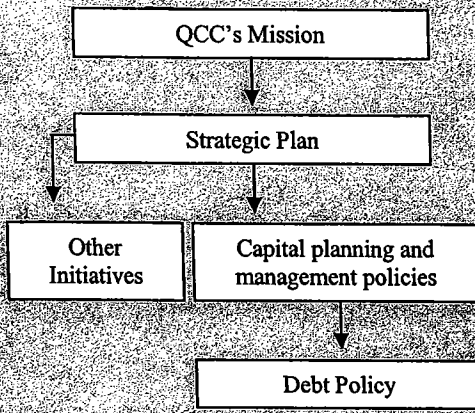
Quinsigamond Community College  
Debt Policy  
Awaiting approval at the Board of Trustees  
January 24, 2007 meeting.

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**OVERVIEW**

**Purpose**

1. Articulate the role of QCC's debt policy within the strategic planning process



The Quinsigamond Community College's strategic planning is a long-term process that establishes college-wide priorities as well as college and divisional programmatic objectives to guide principles and practices. The College's strategic plan identifies specific goals and initiatives, including capital plans that identify necessary and desired college facility investments. To fund its plan, the College will continue to utilize a mix of financing sources including State and Federal sources, philanthropy, internal reserves, and external college-supported debt.

As the College continues to balance the significant need for both current and future facilities investment, teaching, student, and other important needs and competing initiatives for capital from limited resources, the College is implementing this debt policy. This policy, in conjunction with the strategic planning, will aid management in ensuring that an appropriate mix and types of funding sources are utilized and that the College's debt capacity is allocated strategically. A QCC-specific debt policy is appropriate to ensure adequate financial strength to service existing and proposed debt, maintain leverage within an acceptable risk tolerance while investing in priority capital projects, and maintain the budgetary capacity to invest in other initiatives. Additionally, this policy will provide the foundation for internal procedures to ensure that appropriate reporting and management requirements are in place in order to meet objectives outlined in this policy, and to provide a more efficient process for the ongoing external and internal management of debt in order to optimize its utilization on campus.

Management and the Board of Trustees, acting through the Audit and Oversight Committee, will assess this policy on an ongoing basis to ensure that it remains responsive to QCC's evolving academic, research and strategic priorities and financial position.

**INTRODUCTION AND OBJECTIVES**

**Purpose**

1. Articulate QCC's philosophy regarding debt.
2. Establish objectives for debt policy.
3. Provide for regular review and potential update of policy to reflect evolving needs.

Over time, appropriate financial leverage serves an important role in funding the College's capital investments and should be considered a long-term component of QCC's balance sheet. Just as investments represent an integral component of assets, debt is viewed to be a long-term component of liabilities that therefore should be managed on a long-term portfolio-basis consistent with the institution's policy objectives. Debt provides a limited low cost source of funding for capital projects in order to achieve the College's mission and strategic objectives, and, together with other limited resources, should be utilized and allocated appropriately, strategically, judiciously, and equitably.

This objectives of the policy are to:

- (i) Maintain the College's access to capital. Debt financing should only be used to finance those projects that have been reviewed by the Board, are part of the BHE's Strategic Capital Program and which have been approved for financing by the Board. The 2003 study by Eva Klein Associates, *Matching Facilities to Missions: Strategic Capital Program*, equipped BHE with objective criteria and an open process for prioritizing capital projects and justifying them to various constituencies. This is vital not only for appealing to the Executive

and the General Court for funding and for public accountability, but for justifying the need for debt to bond issuing agencies and the market.

- (ii) Manage the College's credit to meet its long-term strategies objectives while maintaining creditworthiness consistent with the most favorable relative cost of capital and borrowing terms. Maintaining the highest acceptable credit rating will permit the College to continue to issue debt and finance capital projects at favorable interest rates while meeting its strategic objectives;
- (iii) Limit risk of the College's debt portfolio. Debt will be managed on a portfolio, rather than a transactional or project-specific, basis. Management's continuing objective of incurring the lowest achievable long-term risk-adjusted cost of capital will be balanced within acceptable budgetary parameters. Financial Feasibility as it applies to specific projects and long term strategic planning will be review for future projected debt on a portfolio basis. Various types of debt structures and financial instruments will be considered, monitored, and managed within the framework established in this policy and according to internal management procedures; and
- (iv) Permit the optimization of the investment of the College's working capital and cash balances. Management will explore various options and alternatives to internal cash holdings regarding the optimal funding mechanism for short-term equipment needs, bridge financing and cash requirements. Management recognizes that working capital requirements, debt management, and the investment of cash should be viewed comprehensively in order to optimize overall funding and investment return strategies.

In addition to establishing a framework relating to the administration of debt, the policy provides for periodic updates pertaining to QCC's debt capacity and financial management to both internal and external parties.

## OVERSIGHT

### Purpose

1. Provide mechanism for oversight and review on periodic basis.
2. Provide management flexibility to make ongoing financing decisions within the framework of the policy.

By adopting this policy and regularly reviewing its results and appropriateness with the Audit and Oversight Committee, management will follow and report on guidelines and requirements regarding debt utilization. With appropriate authorizations consistent with the policy, management will have flexibility to implement specific financial transactions and utilize approved financing vehicles consistent with the policy and specific authorizations in accordance with stated procedures.

The Office of the Vice President for Administrative Services will manage all funding sources, including debt, for capital projects authorized by the Board. The structure of any individual transaction will be based upon overall College's needs to ensure that (i) long-term costs to the College and its operating units are minimized consistent within the context of other strategic objectives and (ii) overall risk does not exceed acceptable levels as defined in this policy.

Because this debt policy is a living document, the Audit and Oversight

Committee will review this policy on an annual basis and report any recommended changes or revisions to the Board of Trustee. This review process is necessary to ensure that the policy remains consistent with the College's objectives and responsive to evolving practices, competitive pressures in the external environment, and financial indicators.

**POLICY RATIOS**

**Purpose**

Ratio 1 - Debt Burden Ratio  
Ratio 2 - Viability Ratio  
Ratio 3 - Primary Ratio  
Ratio 4 - Return on Net Assets Ratio

The College believes that financial discipline is a critical component of long-term debt management and that the Board and management, operating through the Audit and Oversight Committee should establish a limited number of financial ratios and targets in order to manage debt within acceptable ranges consistent with QCC's objectives. These measures will be monitored and reported on in light of QCC's evolving strategic initiatives and capital needs.

Actual and pro forma financial ratios can signal whether an institution is operating within appropriate financial bounds. Although other ratios may be included in a debt policy, the primary financial ratios are:

*Ratio 1 - Debt Burden Ratio*

This ratio expresses annual debt service payments as a percent of total expenses. It measures an institution's ability to repay debt service on all outstanding debt and its impact on the institution's overall budget.

Ratio = Annual Debt Service/Total Expenses

It is believed that if more than 10% of an institution's budget were devoted to debt service, that institution's flexibility to devote its resources to other needs would be compromised. It is understood that rising expenses could make this ratio seem more attractive, though misleading, and is evaluated in conjunction with an institution's income statement

*Ratio 2 - Viability Ratio*

This ratio measures the availability of expendable net assets to pay off long term debt. A ratio of .50 or higher indicates an institution has sufficient net assets to satisfy debt requirements.

Expendable Net Assets/Long-Term Debt

*Ratio 3 - Primary Reserve*

This ratio provides a snapshot of an institution's financial strength and flexibility. The ratio indicates how long the college could operate using expendable reserves without relying on additional new assets generated by operations. Trend analysis indicates whether an institution has increased its net worth in proportion to its rate of growth. A negative or decreasing trend indicates a weakening financial condition.

Ratio = Unrestricted & Expendable Net Assets / Total Operating Expenses

*Ratio 4 – Return on Net Assets Ratio*

This ratio reports whether an institution's resources are growing and if it is financially better off than in previous years. It is important to assess this ratio as a linear trend – an increasing trend indicates an increase in net assets and an increased likelihood that the institution is able to set aside financial resources to strengthen future flexibility. Single year events, like a substantial gift or extreme investment performance, can cause significant year-to-year volatility.

Ratio = Increase (Decrease) in Net Assets / Beginning of Year Net Assets

The debt policy will be shared with external credit analysts and other third parties in order to provide them with the context regarding QCC's assessment of self-determined debt capacity and affordability, which is subject to ongoing review.

Quinsigamond Community College annually monitors the above ratios. Under this policy an analysis of any changes to the ratios will be reviewed whenever any additional debt is being considered or changes in existing debt contemplated. The proposed impact on these ratios will be reviewed as part of the decision making process.

**TYPES OF FINANCINGS**

Purpose
1. Review of all potential funding sources for projects
2. Commonwealth General Obligation Bonds
3. HEFA
4. Tax Exempt Lease Purchase
5. Other Financing Sources
6. QCC Foundation

The state and community colleges under the aegis of the Board of Higher Education (BHE) receive funding for capital projects from sources such as: Commonwealth General Obligation Bonds, bonds issued by the Massachusetts Health and Educational Facilities Authority (HEFA), Tax Exempt Lease Purchase agreements by Operation Services Division and other financing sources.

The College recognizes that there are numerous types of financing structures and funding sources available, each with specific benefits, risks, and costs. All potential funding sources will be reviewed by management within the context of the debt policy and the overall portfolio to ensure that any financial product or structure is consistent with QCC's objectives. Regardless of what financing structure(s) is(are) utilized, a full understanding of the transaction, including (i) quantification of potential risks and benefits, and (ii) analysis of the impact on College's creditworthiness and debt capacity, will be required.

*Commonwealth General Obligation Bonds*

General obligation bonds provide the largest source of capital funding and, as their name suggests, provide capital funding for all of state government. Portions of the funds available through this source are assigned to various agencies through debt caps assigned by the Executive Office for Administration and Finance. The cost of this debt and its availability depends on the creditworthiness of the Commonwealth as a whole.

HEFA

HEFA debt is issued by quasi-public authorities for specific types of capital projects and are paid for via dedicated revenue streams. HEFA states its mandate as providing financing or refinancing for any capital project related to the "primary charitable purpose" of an institution. The cost and availability of HEFA debt depends on the creditworthiness of the individual community college for which a project is being financed.

Tax Exempt Lease Purchase

As a component unit of the Commonwealth of Massachusetts, QCC is eligible to utilize Tax Exempt Lease Purchase (TELP) agreements negotiated by the Operational Services Division through a competitive bid process.

Other Financing Sources

The Colleges recognizes that a variety of transactions, not limited to debt insured directly by QCC, may impact the Credit's credit while the College's limited debt capacity and substantial capital needs require the consideration of various financing alternatives, including possible opportunities for alternative and non-traditional transaction structures. The College recognizes these types of transactions may also impact the College's credit and also often can be more expensive than traditional College debt structures.

Therefore all non-traditional financing structures including guarantees and third party debt can only be considered once the economic benefit and the likely impact on the College's debt capacity and credit has been determined. Specifically, for any third-party, management will ensure the full credit impact of the structure is evaluated and quantified to the extent possible prior to execution and the analysis must be presented to the Audit and Oversight Committee and must receive the Subcommittee's recommendation and Board approval prior to execution.

Quinsigamond Community College Foundation, Inc.

The Quinsigamond Community College Foundation, Inc a separately incorporated non profit corporation, was formed in 1985 to render financial assistance and support to the educational programs and development of the College. When applicable, funding for capital projects can be obtained through the Foundation.

**PORTFOLIO MANAGEMENT OF DEBT**

**Purpose**

1. Permit decisions regarding debt issuance and structure to be made on a portfolio basis, rather than on a per-project basis.
3. Evaluate exposure to other financing

The College considers its debt portfolio holistically; that is, it optimizes the portfolio of debt for the entire College rather than on a project-by-project basis, and takes into account the College's cash and investments. Therefore, management will make decisions regarding project prioritization, financing structures within the context of the overall needs and circumstances of the College.

vehicles and third parties on a portfolio-wide basis.

*Overall Exposure*

The College recognizes that it may be exposed to short-term interest rates, third-party credit, and other potential risks in areas other than direct College debt and, therefore, exposure will be considered on a comprehensive College-wide basis.

**FILING**

**Purpose**

1. Trustee-approved debt policy to Board of Higher Education by February 28, 2007.

State and community colleges must file with the Board of Higher Education a trustee-approved debt policy by February 28, 2007. Any changes, modifications, or amendments to a state or community college's debt policy must be approved by the college's board of trustees and must be filed with the Board of Higher Education within sixty days of approval by the board of trustees.