

# Institutional Capital Financing Credit Guidelines – Updated March 2025

## 1. Project Credit Review and Financial Performance Requirements

- A. **Project-Specific Credit Assessment Requirements** – For all proposed capital financing projects which anticipate additional revenues as a debt service repayment source, the Treasurer, defined below, will require the appropriate Unit to submit through the campus senior financial officer (typically a Vice Chancellor), a comprehensive pro forma financial projection that will extend over the proposed life of the financing being contemplated. Approval to proceed with project financing by the Treasurer will be contingent on project achievement of specific financial performance requirements. In the case of an extremely mission-critical project, the Treasurer may approve a project for financing that does not comport to the financial criteria articulated in these guidelines. Such pro forma projections will be in a format prescribed and/or approved by the Treasurer and will include, but not be limited to:
- i. Funding Source Reconciliation - A description of any Indiana University (“University”) funds that will be used to pay for a portion of the project, including University general ledger account numbers, or IU Foundation account numbers, and where funds are being held in reserve.
  - ii. Assumptions - A summary of all key financial and economic assumptions contained in the pro forma projections.
  - iii. Pro Forma Cash Flow Projections - For projects that will be financed in whole or in part by Consolidated Revenue Bonds and certain Certificates of Participation or Lease Purchase Obligations, an integrated cash flow statement that projects the impact on operating cash balances. This statement must include Net Income (gross revenues less Operating & Maintenance Expenses), existing and projected debt service payments as provided by the Office of the Treasurer, and transfers to reserves for R&R and other purposes, over the life of the anticipated debt.
  - iv. R&R Reserve Activity and Balance Projections - A statement that includes projections of Repair & Replacement Reserve balances, a long-term R&R expenditure projection and funding source projection, over the life of the anticipated debt.
  - v. Reserves Available for Debt Service - Reserves Available for Debt Service, at amounts not less than the minimum balances required under the Debt Service Coverage Test. Amounts set-aside typically are based on maximum annual debt service. To the extent that reserves exceed the requirement, only 25% of debt service may be used for the Debt Service Coverage Test.
  - vi. Debt Service Coverage Ratio - Each Revenue System or Unit that carries outstanding debt must maintain a Debt Service Coverage Ratio on an annual basis over the life of the financing of not less than 1.50. Exceptions may be made with approval of the Treasurer, based upon overall financial conditions of the unit and the University. It is expected that if debt service coverage falls below the minimum target, a plan shall be developed that returns coverage to the minimum target within a reasonable period of time. A credit of up to 0.25

toward the annual coverage ratio requirement will be allowed to the extent that Reserves Available for Debt Service are set aside in an amount equal to twenty five percent of the Annual Debt Service Requirement as of the beginning of the fiscal year. When reviewing estimates for future years, the actual for the fiscal year immediately preceding will be utilized.

## **2. Credit Market Relationships**

- A. **External Credit Assessment** - The Office of the Treasurer will engage in a formal review of the University's credit rating on a periodic basis, as deemed appropriate by the VPCFO and/or Treasurer. This review will incorporate the review and assessment of various aspects of the creditworthiness of the University including, but not limited to, areas such as strategic initiatives; student recruitment, enrollment and retention; research grants, expenditures and administration; development/fund-raising; financial performance; governance structure and significant organizational changes; investment and endowment portfolio structure and performance; capital financing portfolio structure and cost of capital; state and governmental relationships, the current fiscal health of the State, and comparisons to peer institutions.
  - i. **Peer Expert Engagement** - The Treasurer will engage as many other University Units in the review process as are needed to present a complete and accurate assessment of the University's operational and financial health, management and governance structure, and strategic plans & initiatives.
  - ii. **Pre-Official Statement Review** - A review of the University's credit rating that is completed in conjunction with preparing the Official Statement for issuing bonds or tax-exempt commercial paper may be considered as having fulfilled this requirement.
  - iii. **Periodic Reporting on Creditworthiness** - Subsequent to the completion of such a review, the VPCFO or Treasurer will report on the general creditworthiness and credit rating of the University to the Board of Trustees or its Finance & Audit Committee.

## **3. Financing Instruments and Structures Standard Practices**

- A. **Multi-Project Financing Preferred** – “Bundling” or combining various project financing activities into fewer, larger financing transactions will be encouraged to enhance the efficiency of the debt issuance process, while being mindful of certain project specific requirements that result in an exception to this practice.
- B. **Selection of Financing Mode** – All available modes of financing will be considered and analyzed relative to project financing in order to select the mode that is most appropriate and cost effective. Each project financing analysis and evaluation will take into consideration the significant characteristics of all available modes of debt.
  - i. **Fixed Rate Mode**
    - a) Provides a high level of budgetary certainty

- b) Has been the primary mode of financing that the State has preferred the University to use when issuing Student Fee Bonds that are eligible for Fee Replacement
  - c) Provides very little flexibility with respect to the timing of principal reduction or early prepayment of debt
  - d) Has historically been more expensive than variable rate financing
- ii. Variable Rate, defined below, Mode (may use commercial paper)
  - a) Provides for less budgetary certainty
  - b) Has historically been a less expensive form of financing than fixed rate instruments
  - c) Allows for more flexibility with respect to the timing and amounts of principal reduction
  - d) Generally, requires more vigilant oversight and management than fixed rate debt
- iii. Synthetic/Swap Mode
  - a) Synthetic fixed and synthetic variable rate debt structures may be used to manage interest rate risk, pursuant to statute, and will not be entered into for speculative purposes.
  - b) Synthetic fixed and synthetic variable rate debt structures will only be entered into pursuant to a properly executed International Swap and Derivatives Association, Inc. (ISDA) master agreement or other market standard and schedules.
  - c) Synthetic fixed and synthetic variable rate debt that is achieved through the use of Swaps or other Derivative Products will be evaluated to assess how the underlying financing structure, as well as the synthetic structure that is created with a counterparty will perform under varying market conditions.
  - d) Synthetics modes of debt will have a further level of analysis and review applied with respect to the following risks:
    1. *Basis Risk* – The mismatch between actual variable debt services and variable rate indices used to determine Swap payments.
    2. *Tax Risk* – The risk created by potential tax changes that could affect Swap payments.
    3. *Counterparty Risk* – The failure of the counterparty to make required payments.

4. *Termination Risk* – Premature termination of a hedge position requiring one of the parties to an agreement to make termination payment and the ability to enter into an equivalent substitute transaction.
  5. *Liquidity Risk* – The inability to access or renew a liquidity facility when required, e.g., upon premature termination of a swap.
  6. *Credit Risk* – The occurrence of an event modifying the credit rating of a counterparty or otherwise lowering its creditworthiness.
- C. **Cost of Issuance** – Recover any direct debt issuance costs through direct reimbursement of costs of issuance from proceeds of the financing. Cost of issuance which may be reimbursed to the University include, but are not limited to, bond and tax counsel fees, financing-specific advisor or consultant fees, rating agencies fees, certain credit facility and credit enhancement fees, remarketing fees that have a causal relationship to the debt issues, and direct personnel costs incurred by the University and its service providers.
- D. **Ongoing Cost of Financing** – On-going costs of financing, such as dealer or remarketing fees, bank trust fees and rating agency surveillance fees (if allocated) will be paid over the life of the debt. These are components of the financing costs that will be charged to Units on a pro rata basis at the Treasurer's discretion.
- E. **Self-Liquidity** – The University may use components of the University's cash and investment portfolios to provide self-liquidity for commercial paper. The University may also utilize credit lines to provide liquidity for variable rate debt, including commercial paper.

#### 4. **Accounting and Internal Controls**

Engage in prudent internal control practices and procedures designed to ensure the complete and timely payment of debt service obligations, the preservation and protection of University assets, and the accuracy of accounting and financial transactions and reporting. Office of Treasurer practices and procedures are as follows:

- i. Reconciliation - Produce a monthly or quarterly reconciliation of all general ledger accounts.
- ii. Quarterly Reporting - Produce a quarterly report on the status of the University's debt portfolio, including external financing and internal capital lending activity and related balances.
- iii. Treasury Procedures - Produce, maintain and update procedures to document accounting, transaction processing, and other general business practices.
- iv. Business Continuity Plan - Maintain and update a business continuity plan on an annual basis.

## **Definitions**

- A. **Annual Financial Operations Review** – Conduct an evaluation of the University's financial operations performance including, but not limited to, trend and peer institution analyses. Per the Capital Financing policy, the Treasurer will evaluate financial performance ratios calculated based on information derived from the University's annual audited financial statements. The calculations and definitions of these ratios will be made consistent with credit market analytical practices and shall be incorporated into the University Financial Model ("UFM"), defined below.
- B. **Bonds** – Any debt obligation including bonds, notes, or commercial paper
- C. **Code** – The Internal Revenue Code, attendant U.S. Treasury regulations, and related interpretive guidance published by the Internal Revenue Service
- D. **Debt Service Coverage Test** (Debt Coverage Ratio) – A financial viability test calculation whereby the numerator of the ratio consists of the sum of Net Income plus Reserves Available for Debt Service; the denominator of this ratio consists of the sum of the Annual Debt Service Requirement plus Other Uses of Net Income.
- E. **Derivative Products** – Contractual arrangements which create a synthetic bond structure, including but not limited to, rate swap agreements, basis swaps, forward rate agreements, rate cap agreements, rate flow agreements, rate collar agreements, or any other similar agreements (including options to enter into any such agreements).
- F. **Fee Replacement Appropriation** – The General Assembly may choose to provide direct funding support for debt that is payable from student fees, through a biennial appropriation called "fee replacement appropriation" which, in effect, reimburses state universities for student fees used to pay debt service specific buildings. Fee Replacement Appropriation is unique and distinct from other forms of state appropriations for operations, repair & replacement, and other forms of special appropriations that are made to state universities. The unique and distinct nature of the Fee Replacement Appropriation not being co-mingled with other forms of state appropriations is critical to the credit strength of the University.
- G. **Fixed Rate** – A bond or other debt instrument that is issued at a fixed rate of interest to the final maturity of such bond
- H. **Indenture (Indenture of Trust)** – A legal contract between the University and a trustee bank on behalf of the owners of bonds that the University issues. The Indenture outlines responsibilities of the University as a borrower/issuer of bonds and the bank as trustee on behalf of the owners of the bonds.
- I. **Other Uses of Net Income** – An amount that is spent during a given fiscal year from the Repair and Replacement reserves (R&R) of a Revenue System or Unit, in excess of the beginning balances in those reserves as of July 1 of that same fiscal year. Other Uses of Net Income serve to increase the denominator of the Debt Service Coverage Test calculation and to create an incentive to Revenue Systems to

provide adequate funding on an on-going basis to R&R reserves, and a disincentive to underfund or overspend R&R reserves in any given fiscal year.

- J. **Rating Agencies** – Specifically Moody’s Investors Service and S&P Global Ratings, with other credit rating service providers used at the Treasurer’s discretion
- K. **Repair & Replacement (R&R) Reserve (Building Repair, Major Repair, Equipment Reserves should be separate)** – A reserve established and funded for the purpose of making major repair, rehabilitation, replacement, improvement, renovation, or other similar expenditures of a capital (non-routine) nature. Such reserves are located on the University general ledger in the “92 account series”.
- L. **Reserves Available for Debt Service** – Unrestricted cash reserve funds that are segregated from the operating cash and R&R cash reserve funds and which are internally designated through the use of distinct general ledger account or sub-account identification as an unrestricted reserve that is available to cover debt service requirements. These funds can be included in the debt service coverage ratio in amounts equal to 25% of the Annual Debt Service Requirement.
- M. **Revenue System** – A system of facilities and related operational activity which produce Net Income of a character recognized under the Indiana Code as available to pay debt service on bonds issued for facilities including (i) student housing facilities, which may include dining, (ii) parking facilities, (iii) research facilities on the IU Bloomington or IUPUI campuses, (iv) student health and healthcare facilities, (v) Athletic Facilities at IU Bloomington, and (vii) certain other revenue producing facilities as allowed by law and/or so designated by the General Assembly.
- N. **Tax exempt Bonds** – Bonds, the interest on which is intended to be excludable from gross income for federal income tax purposes under Section 103 of the Code.
- O. **Treasurer** – The Treasurer of the Board of Trustees of Indiana University (“Board”) performs certain functions per the applicable Indentures, bond documents, Board resolutions, and Indiana Code, but may designate those functions to the Assistant Treasurer of the Board, a Signature Authority, or staff in the Capital Finance department. The University Treasurer may/may not be the Treasurer of the Board.
- P. **Unit** – An academic, administrative, auxiliary, service, or other School or Department which operates in facilities which were financed with debt issued by the University, e.g., the Department of Intercollegiate Athletics, the School of Medicine
- Q. **University Financial Model (UFM)** – Maintain for long-term institutional planning, as well as assessing the various components that combine to produce the University’s overall credit profile. The UFM will include a 10-Year Balance Sheet, Income Statement, and Net Projection with at least 5 years being forward looking. The model shall incorporate the most recent capital appropriation request as informed by discussions between the Vice President Capital Planning & Facilities and the Treasurer.
- R. **Variable Rate** – Interest rate resets with short frequency over the life of the bond for variable rate bonds or may change at maturity of commercial paper when rolled to a future maturity date