Policies and Procedures

SECTION: **Financial**	*NO.* **3.1.18.**		
CHAPTER: **General**	*ISSUED:* 3/27/13	*REV. A*	*REV. B*
POLICY: **Debt Policy**			

PURPOSE

In support of its mission, the Creighton University (the "University") maintains a long-term strategic plan. The strategic plan establishes University-wide priorities as well as University-wide and divisional objectives. The University develops a capital plan to support these priorities and objectives.

The University's use of debt plays a critical role in ensuring adequate funding for the capital plan as well as providing a cost-effective source of funding for other purposes. By linking the objectives of its Debt Policy to its strategic objectives, the University ultimately increases the likelihood of achieving its mission.

SCOPE

The Debt Policy covers all forms of debt including long-term, short-term, fixed-rate, and variable-rate debt. It also covers other forms of financing including both on-balance sheet and off-balance sheet structures, such as leases, and other structured products used with the intent of funding capital projects.

The use of derivatives is considered when managing the debt portfolio and structuring transactions. Conditions guiding the use of derivatives are addressed in a separate Interest Rate Risk Management Policy.

OBJECTIVES

The objectives of this policy are to:

(i) Outline the University's philosophy on debt

(ii) Establish a control framework for approving and managing debt

(iii) Define reporting guidelines

(iv) Establish debt management guidelines

The Debt Policy formalizes the link between the University's strategic plan and the issuance of debt. Debt is a limited resource that must be managed strategically in order to best support University priorities.

The policy establishes a control framework to ensure that appropriate discipline is in place regarding capital rationing, reporting requirements, debt portfolio composition, debt servicing, and debt authorization. It establishes guidelines to ensure that existing and proposed debt issues are consistent with financial resources to maintain an optimal amount of leverage, a strong financial profile, and a strategically optimal credit rating.

Under this policy, debt is being managed to achieve the following goals:

(i) Maintaining access to capital and financial markets.

(ii) Managing the University's credit rating to meet its strategic objectives while maintaining the highest acceptable creditworthiness and most favorable relative cost of capital and borrowing terms;

(iii) Optimizing the University's debt mix (i.e. short-term and long-term, fixed-rate and floating-rate, traditional and synthetic) for the University's debt portfolio;

(iv) Managing the debt structure and maturity profile to meet liquidity objectives and make funds available to support future capital projects and strategic initiatives;

(v) Coordinating debt management decisions with asset management decisions to optimize overall funding and portfolio management strategies.

The University may use debt to accomplish critical priorities by more prudently using debt financing to accelerate the initiation or completion of certain projects, where appropriate. As part of its review of each project, the University evaluates all funding sources to determine the optimal funding structure to achieve the lowest cost of capital.

OVERSIGHT

The Vice President for Finance ("VP Finance") is responsible for implementing this policy and for all debt financing activities of the University. The policy and any subsequent, material changes to the policy are approved by the Creighton University's Board of Trustees ("Board"). The approved policy provides the framework under which debt management decisions are made. The VP Finance may delegate responsibilities for administration of this Debt Policy.

The Budget and Finance Committee of the Board will review the policy on an annual basis to ensure that the provisions are consistent with the goals of the University and capital market and credit conditions.

The exposure limits listed in the policy are monitored on a regular basis by the VP Finance. The VP Finance reports regularly to the Senior Vice President for Operations and the Board on the University's debt position and plans.

DEBT AFFORDABILITY AND CAPACITY

In assessing its current debt levels, and when planning for additional debt, the University takes into account both its debt affordability and debt capacity. Debt affordability focuses on the University's ability to service its debt through its operating budget and identified revenue streams and is driven by strength in income and cash flows. Debt capacity focuses on the University's financial leverage in terms of debt funding as a percentage of the University's total capital.

The University considers many factors in assessing its debt affordability and debt capacity including its strategic plan, ability to access capital markets and alternative sources of funding. The University uses four key ratios to provide a quantitative assessment of debt affordability and debt capacity.

Debt Affordability Measures

Debt Burden Percentage
This ratio measures the University's debt service burden as a percentage of total university expenses. The target for this ratio is intended to maintain the University's long-term operating flexibility to finance existing requirements and new initiatives.

Annual Debt Service / Total Operating Expenses ***Target < 5%***

The measure is based on aggregate operating expenses as opposed to operating revenues because expenses typically are more stable (e.g. revenues may be subject to one-time operating gifts, investment return fluctuations, variability of health services revenues, etc.) and better reflect the operating base of the University. This ratio is adjusted to reflect any non-amortizing or non-traditional debt structures that could result in significant single year fluctuations including the effect of debt refundings.

Debt Service Coverage Ratio
This ratio measures the University's ability to cover debt service requirements with revenues available for operations. The target established is intended to ensure that operating revenues are sufficient to meet debt service requirements and that debt service does not consume too large a portion of income.

(Operating Gain/(Loss) + Interest Expense + Depreciation) / Annual Debt Service ***Target > 2.0x***

This ratio is adjusted to reflect any non-amortizing or non-traditional debt structures that could result in significant single year fluctuations including the effect of debt refundings.

Debt Capacity Measures

Viability Ratio
This ratio indicates one of the most basic determinants of financial health by measuring the availability of liquid and expendable net assets to aggregate debt. The ratio measures the medium to long-term health of the University's balance sheet and debt capacity and is a critical consideration of universities with high credit quality.

Many factors influence the viability ratio, affecting both the assets (e.g., investment performance, philanthropy) and liabilities (e.g., timing of bond issues), and therefore the ratio is best examined in the context of changing market conditions so that it accurately reflects relative financial strength.

(Unrestricted Net Assets + Temporarily Restricted Net Assets – Net Investment in Plant) / Total Debt
Target > 1.1x

Debt Capitalization Percentage
This ratio measures what percentage of University capital comes from debt. A University that relies too heavily on debt capital may risk being over-leveraged and potentially reduce its access to capital markets. Conversely, a

university that does not strategically utilize debt as a source of capital may not be optimizing its funding mix, thereby sacrificing access to low-cost funding to invest in mission objectives.

Total Debt / (Total Net Assets + Total Debt) ***Target < 25%***

Use of Ratios in Managing University Credit Ratings
The ratios and limits are not intended to track a specific rating, but rather to help the University maintain a competitive financial profile, funding for facilities needs and reserves, and adequate debt service coverage.

The Debt Policy is shared with external credit analysts and other parties in order to provide them with background on the University's philosophy on debt and management's assessment of debt capacity and affordability.

FINANCING SOURCES

The University recognizes that there are numerous types of financing structures and funding sources available, each with specific benefits, risks, and costs. All potential funding sources are 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 the University's objectives. Regardless of what financing structure is utilized, due-diligence review must be performed for each transaction, including (i) quantification of potential risks and benefits, and (ii) analysis of the impact on University creditworthiness and debt affordability and capacity.

Tax-Exempt Debt
The University recognizes that tax-exempt debt is a significant component of the University's capitalization due in part to its substantial cost benefits; therefore, tax-exempt debt is managed as a portfolio of obligations designed to meet long-term financial objectives rather than as a series of discrete financings tied to specific projects. The University manages the debt portfolio to maximize its utilization of tax-exempt debt relative to taxable debt whenever possible. In all circumstances, however, individual projects continue to be identified and tracked to ensure compliance with all tax and reimbursement regulations.

For tax-exempt debt, the University will maximize the external maturity of any tax-exempt bond issue, subject to prevailing market conditions and opportunities and other considerations, including applicable regulations.

Taxable Debt
In instances where certain of the University's capital projects do not qualify for tax-exempt debt, the use of taxable debt may be considered. The taxable debt market offers certain advantages in terms of liquidity and marketing efficiency; such advantages will be considered when evaluating the costs and benefits of a taxable debt issuance.

Commercial Paper
Commercial paper provides the University with interim financing for projects in anticipation of philanthropy or planned issuance of long-term debt. The use of commercial paper also provides greater flexibility on the timing and structuring of individual bond transactions. This flexibility also makes commercial paper appropriate for financing equipment and short-term operating needs. The University recognizes that the amount of commercial

paper is limited by the Debt Policy ratios, the University's variable-rate debt allocation limit, and the University's available liquidity support.

University-issued vs. Authority-issued Debt
In determining the most cost effective means of issuing debt, the University evaluates the merits of issuing debt directly vs. issuing debt through Douglas County or other authorized issuer (e.g., Nebraska Educational Financing Authority.)

On a regular basis, the University performs a cost benefit analysis between these two options and takes into consideration the comparative funding costs, flexibility in market timing, and bond ratings of each alternative. The University also takes into consideration the future administrative flexibility of each issue such as the ability to call and/or refund issues at a later date, as well as the administrative flexibility to structure and manage the debt in a manner that the University believes to be appropriate.

Derivative Products
Management recognizes that derivative products may enable more opportunistic and flexible management of the debt portfolio. Derivative products, including interest rate swaps and locks, may be employed primarily to manage or hedge the University's interest rate exposure. The University utilizes a framework to evaluate potential derivative instruments by considering (i) its current variable-rate debt allocation, (ii) existing market and interest rate conditions, (iii) the impact on future financing flexibility, and (iv) the compensation for assuming risks or the costs for eliminating certain risks and exposure. Risks include, but are not limited to, tax risk, interest rate risk, liquidity risk, counterparty credit risk, basis risk, and any other potential risks either imposed or removed through the execution of any transaction.

The University analyzes and quantifies the cost/benefit of any derivative instrument relative to achieving desirable long-term capital structure objectives. Under no circumstances will a derivative transaction be utilized that is not understood fully by management or that imposes inappropriate risk on the University. All derivative transactions will be governed by the University's Interest Rate Risk Management Policy.

Other Financing Sources
Given limited debt capacity and substantial capital needs, opportunities for alternative and non-traditional transaction structures may be considered, including off-balance sheet financings. The University recognizes these types of transactions often can be more expensive than traditional University debt structures; therefore, the benefits of any potential transaction must outweigh any potential costs.

All structures can be considered only when the economic benefit and the likely impact on the University's debt capacity and credit have been determined. Specifically, for any third-party or developer-based financing, management ensures the full credit impact of the structure is evaluated and quantified.

PORTFOLIO MANAGEMENT OF DEBT

The University considers its debt portfolio in aggregate, that is, it optimizes the portfolio of debt for the entire University rather than on a project-by-project basis while taking into account the University's cash and investment portfolio. Therefore, management makes decisions regarding project prioritization, debt portfolio optimization, and financing structures within the context of the overall needs and circumstances of the University.

Variable-Rate Debt

The University recognizes that a degree of exposure to variable interest rates within the University's debt portfolio is desirable in order to:

(i) take advantage of repayment/restructuring flexibility;

(ii) benefit from historically lower average interest costs;

(iii) provide a "match" between debt service requirements and the projected cash flows from the University's assets; and

(iv) diversify its pool of potential investors.

Management monitors overall interest rate exposure, analyzes and quantifies potential risks, including interest rate, liquidity and rollover risks, and coordinates appropriate fixed/variable allocation strategies. The portfolio allocation to variable-rate debt may be managed or adjusted through (i) the issuance or redemption of debt in the conventional debt market (e.g. new issues and refundings) and (ii) the use of interest rate derivative products including swaps.

The amount of variable-rate debt outstanding (adjusted for any derivatives) shall not exceed the following target percentage of the University's outstanding debt. This limit is based on the University's desire to: (i) limit annual variances in its interest payments, (ii) provide sufficient structuring flexibility to management, and (iii) utilize variable-rate debt (including derivatives) to optimize debt portfolio allocation and minimize costs.

Total Variable-rate Debt (including synthetic) / Total Debt ***Target < 35%***

Refinancing Outstanding Debt

The University monitors its debt portfolio on a continual basis to assure portfolio management objectives are being met and to identify opportunities to lower its cost of funding, primarily through refinancing outstanding debt.

The University monitors the prices and yields of its outstanding debt and attempts to identify potential refunding candidates by examining refunding rates and calculating the net present value of any refunding savings after taking into account all transaction costs. The University may choose to pursue refundings for economic and/or legal reasons.

Liquidity Requirements

The University's portfolio of variable-rate debt and commercial paper require liquidity support in the event of the bonds or paper being put back to the University by investors. Generally, the University can purchase liquidity support externally from a bank in the form of a standby bond purchase agreement, letter of credit or line of credit.

In addition, the University can also use its own capital in lieu of or to supplement external facilities. Alternatively, it can utilize variable-rate structures that do not require liquidity support (e.g. auction-rate products.)

Just as the University manages its debt on a portfolio basis, it also manages its liquidity needs by considering its entire asset and debt portfolio, rather than managing liquidity solely on an issue-specific basis. This approach permits institution-wide evaluation of desired liquidity requirements and exposure, minimizes administrative burden, and reduces total liquidity costs.

A balanced approach is used to provide liquidity support to enhance credit for variable-rate debt, through a combination of external bank liquidity, self-liquidity, auction market or derivative structures. Using a variety of approaches limits dependence on an individual type or source of credit; it also allows for exposure to different types of investors. The University must balance liquidity requirements with its investment objectives and its cost and renewal risk of third-party liquidity providers.

Further, a portfolio-approach to liquidity can enhance investment flexibility, reduce administrative requirements, lower total interest costs, and reduce the need for external bank liquidity.

Overall Exposure
The University recognizes that it may be exposed to interest rate, third-party credit, and other potential risks in areas other than direct University debt (e.g., off-balance sheet transactions, counterparty exposure in the investment portfolio, etc.) and, therefore, exposures are considered on a comprehensive University-wide basis.

STRATEGIC DEBT ALLOCATION

Recognizing that financial resources are not sufficient to fund all capital projects, management must allocate debt strategically, continuing to explore alternate sources of funding for projects. External support and philanthropy remain critical to the University's facilities investment plan.

Management allocates the use of debt financing internally within the University to reflect the prioritization of debt resources among all uses, including plant and equipment financing, academic projects, and projects with institutional impact. Generally, the University favors debt financing for those projects critical to the attainment of its strategic goals and those projects with identified revenue streams for the repayment of debt service and incremental operating costs.

Each capital project is analyzed at its inception to ensure that capital is used in the most effective manner and in the best interests of the University. There is an initial institutional review of each project, prior to its inclusion in the University's strategic plan, to determine if debt leveraging would be desirable even if not requested by the project sponsor.

As part of this initial institutional review, the University also will assess, based on the project's business plan, the sufficiency of revenues to support any internal loans. If the University determines that collateral is necessary, it may require the entity to segregate unrestricted funds for this purpose.

In general, a given project should generate sufficient revenue or be supported by designated gifts such that the anticipated debt service coverage attributable to the project is at least 1.25:1.

CENTRAL LOAN PROGRAM MANAGEMENT

Each division is responsible for the repayment of all funds borrowed from the central loan program, plus interest and certain fees established in the University's internal lending policies, regardless of the internal or external source of funds.

Loan structures with standard financial terms are offered to divisional borrowers. The University may provide for flexible financing terms in order to accommodate individual divisions if it is determined to be in the University's best interest. The VP Finance clearly articulates the policies and procedures for the assumption and repayment of debt to all borrowers.

De-linking External and Internal Debt Structures

The University has adopted a central loan program under which it provides funding for projects across schools and divisions under the guidance of the VP Finance. In this regard, the University has established a pool of financing resources, including debt, for a central source of capital.

The benefits of this program include:

(i) enabling the structuring of transactions in the best economic interests of the University that otherwise wouldn't be possible on a project-specific basis;

(ii) providing continual access to capital for borrowers and permitting the University to fund capital needs on a portfolio basis rather than on a project-specific basis;

(iii) funding specific projects with predictable financial terms,

(iv) achieving the lowest average internal borrowing costs while minimizing volatility in interest rates,

(v) permitting prepayment of internal loans at any time without penalty, and

(vi) allowing the University to effectively manage its relationships with various financial institutions.

The central loan program can access funds from a variety of sources to originate loans to divisions. The University manages its funding sources on a portfolio basis, and therefore payments from divisions are not tied directly to a particular source of funds. (Note: Due to federal tax and reimbursement requirements, actual debt service for certain projects still must be tracked.)

Blended Interest Rate
The University charges a blended interest rate to its divisions based on its cost of funding. In some instances, at the discretion of the VP Finance, the type and useful life of the project being financed may affect the appropriate term and interest rate of any loan.

This blended interest rate may change periodically to reflect changes in the University's average aggregate expected long-term cost of borrowing. The blended interest rate may also include a reserve for interest rate stabilization purposes.

In addition to charging borrowers interest, the central loan program collects amounts to pay for costs of administering the debt portfolio. These costs are clearly articulated to divisions, and are passed on to borrowers in the form of a rate surcharge and an upfront fee for loan origination. These charges may be reviewed and adjusted from time-to-time.

APPROVAL PROCESS

All transactions for debt issuance or major modifications to existing debt agreements shall be reviewed with the Budget and Finance Committee. If the Budget and Finance Committee approves a transaction, it will recommend that such be authorized through a Board or Executive Committee resolution. Within the authorizing resolution, the Board or Executive Committee shall establish financing parameters for the transaction.

In the event that the Budget and Finance Committee does not elect to recommend a transaction to the Board or Executive Committee and University management feels that such transaction is in the best interest of the University, the VP Finance shall have the right to present the transaction for approval directly to the Board or Executive Committee.

As part of the approval resolutions, the Board or Executive Committee shall delegate the authority to approve the pricing of such debt, the execution of related financing documents, and the on-going administration of such debt to the VP Finance and the Associate Vice President for Finance.