Overview of Financial Statements and Financial Planning

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Overview of Financial Statements and Financial Planning

System financial health inputs and processes
BOR financial planning metrics
Bond ratings

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How are System finances managed?

Institutional leadership:

- Operating budget and capital spending under $1M – *institution fund balance goal requires saving $1 out of every $100 spent*

Chancellor and Board of Regents discipline:

- Capital spending over $1M – *spending progress tracked, considered outside of institution fund balance goals so that project timing not impacted*
- Bond authorizations approvals based on institution and USM affordability
- The fund balance goal is set annually to maintain ratio of reserves to debt

USM financial planning annually takes into consideration externalities:

- Pension liability
- Investment returns
- Pandemic or other crisis
- Fund balance reversions

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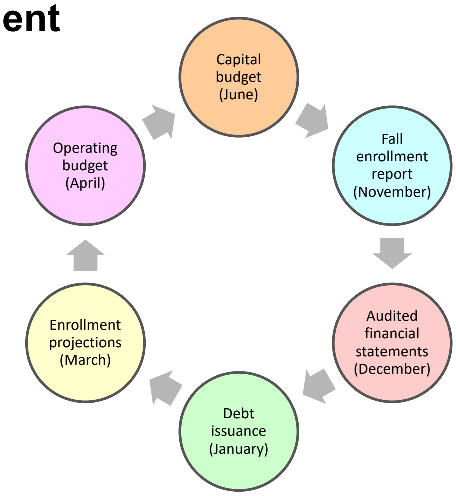
Annual Cycle for Inputs into Financial Management



Other off cycle processes:

- Campus master plans (rotating cycle every 5 years)
- Out of cycle project approvals (ongoing)

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Financial Planning Metrics

Board of Regents Policy on Debt Management ***(VIII-12.00)***

- Minimum 'Available Funds to Debt' of 90% on an 'adjusted' basis
- Maximum debt service ratio of 4% (currently just over 3%)
- Standards are designed to ensure institutions have reserves for:
  - Opportunistic initiatives
  - Crisis like the pandemic where revenues temporarily decline
  - To satisfy obligations when due

Institution fund balances are not a 'rainy day fund' – fund balances are the result of hundreds of business managers across the System making prudent decisions to meet long-term needs – when an unanticipated challenge arises requiring use of fund balances, institution presidents need to make difficult choices

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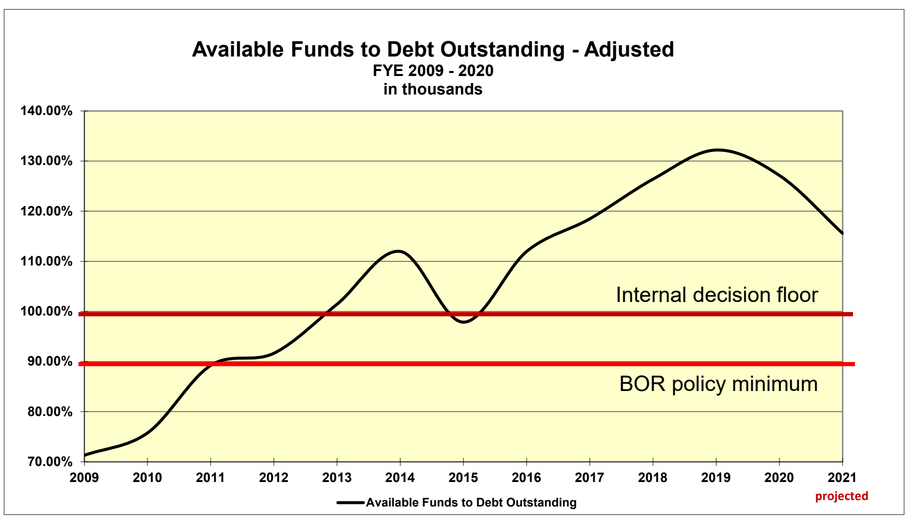
Trend in USM financial health



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USM Bond Ratings (reaffirmed past week)

- Moody's Aa1 (since September 2010)
- Standard & Poor's AA+ (since June 2008)
- Fitch AA+ (since December 2010)

All 3 with stable outlook

What does this mean for the System:

1. Lower interest rates
2. Access to refinancings of previously issued debt
3. Partnership opportunities associated with credit strength
4. Requires financial strength to be maintained (lower borrowing)

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The Rating Agency Evaluation

- Needed for selling USM debt to provide facilities needed for mission
- Better rating = lower borrowing costs + enhanced fiscal discipline
- USM BOR debt policy designed to support financial health
- Rating agency evaluation takes into consideration:
  - Quality of leadership and decision-making
  - Financial statement results
  - Financial plans
  - Public-private partnership projects retained risk

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Bond Issuance Practices

- Issue annually to fund coming 12 months of project spending
- Level debt service to provide budgetary predictability
- 3% to 5% coupon rates against a 2% true interest cost yields larger bond premiums (cash proceeds in excess of par)
- Refinancing to lower debt portfolio-wide interest spending
- 10, 20 and 30-year term borrowings
- Auxiliary projects pay their proportionate debt service based on proceeds use
- Academic projects debt service paid from System-wide pool

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