
DEBT FINANCING POLICIES

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1801 DEBT FINANCING SELECTION

Subject: Debt Financing
Effective: December 1986
Revised: August 2017
Last Reviewed: August 2017
Resp. Office: Treasurer's Office
Approval: V.P. for Finance and Treasurer

PURPOSE

To ensure selection and use of the most cost effective debt financing to meet current operation and capital project needs.

POLICY

1. The Vice President for Finance and Treasurer is responsible for assessing and selecting the most cost effective debt financing alternatives to meet current operation and capital project needs.
2. The Trustees must approve all debt agreements in excess of \$1,000,000 prior to their execution.
3. Debt instruments shall be reviewed by the Debt Subcommittee of the Budget and Finance Committee annually.

1802 DETERMINATION OF DEBT CAPACITY

Subject: Debt Financing
Effective: December 1986
Reviewed: May 2006
Revised: April 2017
Resp. Office: Treasurer's Office
Approval: Trustees

PURPOSE

A constant monitoring of the University's debt capacity is essential for good financial management.

POLICY

1. The Vice President for Finance and Treasurer is responsible for determining and assessing the debt capacity of the University and reporting this assessment to the Trustees.

1803 DEBT MANAGEMENT – OPERATIONS

Subject: Debt Financing
Effective: December 1986
Revised: May 2006
Last Reviewed: April 2017
Responsible Office: Treasurer's Office
Approval: V.P. for Finance and Treasurer

PURPOSE

The use of debt may be used for operating capital needs.

POLICY

1. The V.P. for Finance and Treasurer is responsible for meeting the cash requirements for the University (i.e., interfund borrowings and from Trustee approved outside sources)
2. The Treasurer's Office is responsible for negotiating and executing debt agreements on behalf of the University with outside financial institutions as approved by the Trustees.
3. The Treasurer's Office is responsible for administering debt service requirements and ensuring compliance with applicable debt covenants.
4. Interest on all interfund borrowings will be charged at a rate as determined from time to time by the V.P. for Finance and Treasurer.
5. The V.P. for Finance and Treasurer will maintain written documentation for all internal loans borrowings.

1804 DEBT MANAGEMENT – CAPITAL PROJECT

Subject: Debt Financing
Effective: December 1986
Revised: April 2007
Last Reviewed: April 2017
Responsible Office: Treasurer's Office
Approval: Trustees

PURPOSE

Debt financing may be required in support of capital projects.

POLICY

1. The V.P. for Finance and Treasurer is responsible for selecting the debt financing alternative appropriate for capital projects. All debt financings must be supported by an identified debt service source.
2. Internal loans for capital will be managed by the Treasurer's Office. The status of internal loans for capital must be reviewed quarterly and reported to the V.P. for Finance and Treasurer.
3. All capital project financings greater than \$5,000,000 must be approved by the Trustees.
4. The Treasurer's Office is responsible for administering debt service requirements and ensuring compliance with applicable debt covenants.

1805 BANK LINES OF CREDIT

Subject: Debt Financing
Effective: December 1986
Revised: May 2006
Last Reviewed: April 2017
Responsible Office: Treasurer's Office
Approval: V.P. for Finance and Treasurer

PURPOSE

Secured and unsecured lines of credit may be established as a contingency to meet operating cash requirements.

POLICY

1. The Treasurer's Office is responsible for reviewing and determining the appropriate levels and types of bank lines of credit for approval by the Trustees.
2. The Treasurer's Office is responsible for establishing and administering all bank lines of credit as approved by the Trustees.
3. All borrowings against bank lines of credit will be governed by the Policy No: 1803 – Debt Management – Operations.
4. The status of all bank lines of credit will be reviewed by the Treasurer's Office and reported to the Trustees on an annual basis.
5. The Treasurer's Office is responsible for administering debt services requirements and ensuring compliance with applicable debt covenants

1806 BANK LETTERS OF CREDIT

Subject: Debt Financing
Effective: December 1986
Revised: May 2006
Last Reviewed: April 2017
Responsible Office: Treasurer's Office
Approval: V.P. for Finance and Treasurer

PURPOSE

Bank letters of credit may be required, or preferred, in support of University activities.

POLICY

1. The Treasurer's Office is responsible for determining the appropriateness of bank letters of credit to support University activities.
2. The Treasurer's Office is responsible for negotiating the placement of all letters of credit.
3. The V.P. for Finance and Treasurer is authorized to execute letters of credit as approved by the Trustees as required for insurance related activities as long as total amount outstanding does not exceed \$100 million. The V.P. for Finance and Treasurer will annually submit to the Trustees a report of all outstanding letters of credit.
4. The V.P. for Finance and Treasurer is authorized to execute letters of credit as approved by the Trustees.

1807 INTERFUND BORROWING – EQUIPMENT PURCHASE LOAN PROGRAM (EPLP)

Effective: May, 2018

Revised: May, 2018

Reviewed: May, 2018

Responsible Office: Office of the
Treasurer

Approval: V.P. for Finance and Treasurer

PURPOSE

This policy governs the extension of internal loans from the University's working capital for the purpose of financing equipment acquisitions.

The objectives of the EPLP include the following:

- Provide a source of funding for equipment purchases which the school or center cannot self-fund.
- Provide bridge funding for project gift pledges maturing in five years or less.
- Promote efficient working capital management by generating a higher rate of return on University liquidity balances.
- Ensure that internal equipment loans will not be authorized without the borrowing school or center submitting a fiscally responsible and achievable business plan in support of timely repayment.

POLICY

1. Responsibility:

The Office of the Treasurer is responsible for administering the EPLP program.

2. Pool:

The maximum amount of loans outstanding under this program is \$5,000,000.

Principal repayments will create a revolving loan pool over time.

3. Terms and conditions:

Individual loans administered under this program must be between \$100,000 and \$1,000,000.

The maximum loan term is 5 years.

Borrowers will repay loan principal and interest over a predetermined time period through monthly fixed charges to the borrower's operating account.

Each loan will be analyzed to determine the most appropriate term, with the repayment term not exceeding the useful life of the asset being financed.

Loans may be prepaid early without penalty at any time.

4. Interest charges:

Interest will be calculated on the loan balance beginning on the date on which the funds are deposited into the appropriate general ledger account.

The interest rate will be set by the Treasurer's Office annually based on prevailing leasing rates, which are slightly higher than the University's overall cost of capital.

The FY19 rate is 5%.

5. Approvals:

All loan requests are to be submitted to the Office of the Treasurer. (Refer Procedures section below)

Loan request should first be approved by the School/Center's Dean and Senior Business Administrator prior to submission.

Loan amounts under \$500,000 will be subject to review approval by the Office of the Treasurer.

Loans amounts between \$500,000 and \$1,000,000 will require additional approval from the Capital Information and Technology Equipment (CITE) Committee and Capital Council.

6. Loan request procedures:

Loan requests must be submitted to Jeff McCray (jmccray@upenn.edu). The request must include a complete business plan justifying the financing and detailing debt service funding sources. The business plan should include the following:

- Exec Summary
- Background/ Rationale
- Business Description/ Objective
- Market Analysis (if applicable and/or associated with a revenue generating activity)
- Any opportunities and risks associated with this investment
- Funding requirements (acquisition, installation, and operating incremental operation costs)
 - Detailed equipment description including supplying vendor and price
 - Amount of the loan being requested
 - The estimated useful life of the equipment
 - Repayment period requested
 - Source of funds available for repayment, specifically cash in hand if gifts or bequests
 - 26 digit budget code to be charged for debt service

- **Financial Analysis/ Projections** - Copy of the departmental budget as recorded in Planning (form A3-Budget Analysis) including the prior 2 year actuals and 5 future year's projections. The budget should include debt service as provided by the Treasurer's Office
- **Summary**
- **Dated signature of Dean and Senior Business Administrator**

Upon review and approval of the Loan Request and Business Plan, the Office of the Treasurer will facilitate further approval, if applicable. For Loan Requests > \$500,000, a copy of the Capital Needs Statement signed by Provost or EVP for equipment over \$500,000 will be required.

The Treasurer's Office will advise the School if the Loan Request is approved. If the Loan Request is approved, a formal amortization schedule in a Memorandum of Agreement ("MOA") will be prepared for the school/center's review, signature and return. Once the Treasurer's Office receives the signed MOA, funding will be transferred to the school/center for their equipment.

1808 TAX-EXEMPT BOND POLICIES

Effective: December 1986
Last Revision: June 2012
Last Reviewed: April 2017
Responsible Office: Treasurer's Office
Approval: V.P. for Finance and Treasurer

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I. POLICY TO TRACK PRIVATE USE OF TAX-EXEMPT FINANCED SPACE

PURPOSE:

The Internal Revenue Service ("IRS") requires organizations to monitor private use of tax-exempt financed facilities and equipment financed with tax-exempt bonds. This policy outlines tracking procedures to monitor private use so that limitations for tax-exempt facilities are not exceeded.

POLICY/PROCEDURE:

Policy

Private use of tax-exempt financed facilities and equipment financed with tax-exempt bonds requires monitoring procedures to ensure that the private use stays within the legal limitations. Excessive private use may jeopardize the tax-exempt status of the bonds. Additionally, private business use information must also be reported annually on Form 990. For this reason, activities that might result in private use of tax-exempt facilities and equipment (such as through lease arrangements, management contracts and/or research agreements) require the review and approval of Comptroller's Office, Treasurer's Office and Office of General Counsel. Further, Comptroller's Office, Treasurer's Office and Office of General Counsel must periodically monitor and measure the private use of tax-exempt financed facilities.

Potential sources of private use of tax-exempt financed space may include the following:

- Unrelated trade or business activities
- Management and other service arrangements
- Sponsored research contracts
- Naming rights contracts

- Leases and subleases of facilities
- Joint venture/limited liability corporations/partnership arrangements

Procedure

Initial Issuance Procedures

Upon the initial issuance of a new series of bonds, Bond Counsel will produce a due diligence report that will outline anticipated sources of private business use of the tax-exempt bonds. This expected private use should be recorded and tracked throughout the life of the bond in addition to any new sources of private use after the bonds are issued.

Continued Tracking Procedures

Requests to use or lease facilities that are tax-exempt bond financed must be submitted to Comptroller's Office, Treasurer's Office and Office of General Counsel for review and approval under the following conditions:

1. Use of the tax-exempt bond financed facility by employees to operate an unrelated trade or business;
2. Use of a tax-exempt bond financed facility by individuals not employed by the university or a private party;
3. Use of tax-exempt bond financed facility in a joint venture/limited liability corporation/partnership agreement between the university and another entity.

Research sponsored by private non-government parties where the sponsor obtains rights to resulting technology or intellectual property may result in private use of the tax-exempt financed facility. Specific procedures have been established to monitor this type of use- See "Research Policy- Private Business Use Review Analysis." Comptroller's Office, Treasurer's Office and Office of General Counsel should review these contracts prior to acceptance to determine whether they meet the safe harbor for research agreements (Rev. Rul. 97-14).

On a periodic basis, the Comptroller's Office, Treasurer's Office and Office of General Counsel should evaluate requests from departments and individuals to use tax-exempt bond financed facilities. The amount of private use of bond proceeds that results from all private uses of the tax-exempt bond financed facilities should be recorded and tracked throughout the life of the bond.

Comptroller's Office, Treasurer's Office and Office of General Counsel on a regular basis, should hold discussions or circulate a questionnaire to departments to determine whether there has been any private business use of the tax-exempt financed facilities. Comptroller's Office, Treasurer's Office and Office of General Counsel may also find it beneficial to periodically provide education sessions to appropriate personnel within the various departments.

Calculation Procedures

Once identified, private use of bonds will be calculated on a yearly basis. This calculation should be completed for each bond issue separately.

Corrective Actions

The goal of ongoing tracking and monitoring is to ensure that all tax-exempt bonds remain qualified and are held in compliance with regulatory standards. Such monitoring also ensures that any actual or

potential violations of federal tax requirements can be timely identified and corrected via self-remediation or through the IRS voluntary closing agreement program, if self-remediation is not available under applicable IRS regulations.

Central recordkeeping environment

Tracking records must be filed with Comptroller's Office, Treasurer's Office and Office of General Counsel for the life of the financing plus 3 years in order to meet the recordkeeping requirements of the IRS.

II. TRACKING OF ASSETS AND PROCEEDS ASSOCIATED WITH TAX-EXEMPT BOND ISSUES

PURPOSE:

Organizations are required to track the use of tax-exempt bond proceeds and to identify what assets are tax-exempt bond financed. This policy outlines procedures associated with the expenditure of tax-exempt bond proceeds and the tracking of the purchase/sale of tax-exempt bond-financed assets.

POLICY/PROCEDURE:

Policy

In its Official Statement and supporting documentation, the University of Pennsylvania will identify how it expects to spend the bond proceeds. Treasurer's Office will monitor the actual expenditure of bond proceeds to ensure they agree with these projected expenditures. Treasury will also need to track the assets purchased with bond proceeds so they can be identified for purposes of calculating private use and for tracking any dispositions.

Procedure

Initial Expenditures

Invoices should be first sent to the office of the VP of Facilities where, upon review and approval, should forward the invoices to Accounts Payable for processing. At the same time, Treasury should review the invoices for appropriateness of reimbursement by bond proceeds. Expenditures as reviewed and approved by Treasury should then be sent to the applicable bond trustee for reimbursement. In general, the University of Pennsylvania should request reimbursement from the applicable bond trustee within an allowable time frame from the original date of payment of the invoice.

Identification and Tracking of Assets

The University of Pennsylvania should ensure that bond-financed assets are identified and tracked. If a bond-financed asset is disposed of special care should be taken to identify the consequences of such disposal.

Central Recordkeeping requirement

Tracking records must be filed in the Finance Department to meet the recordkeeping requirements. See Section V, Record Retention Policy, for additional recordkeeping information.

III. UNRELATED BUSINESS INCOME

Purpose:

The University of Pennsylvania is exempt from income tax under Section 501(c)(3) of the Internal Revenue Code ("IRC") on income from activities that are substantially related to its educational and health care missions, which serve as the basis for its tax exemption.

However, the University of Pennsylvania is subject to tax on the net income of any unrelated business activities conducted, even though such activities may bring in funds to support the University of Pennsylvania's exempt operations. This policy outlines procedures to identify and track activities subject to the unrelated business income tax ("UBIT") for purposes of determining private business use.

Policy/Procedure:

Policy

Unrelated Business Income ("UBI") is the income from a trade or business activity that is regularly carried on by an exempt organization and that is not substantially related to the performance by the organization of its exempt purpose or function. Thus, for UBI to occur, three requirements must be met: (1) a trade or business activities, (2) which is regularly carried on, and (3) is not substantially related to the tax-exempt purpose of the University or the reporting affiliate. Any unrelated business use is deemed to be private business use.

For each UBI-generating activity identified, if it is determined that such activity is conducted in a tax-exempt bond-financed property, the amount of private use generated from such activity will be calculated and tracked based upon the "Tax-Exempt Bonds - Policy to Track Private Business Use of Tax-Exempt Financed Space" policy.

Tax-exempt organizations are required to annually report unrelated business income on Form 990-T (Federal).

Procedure

Identification of Activities (Revenue and Expense)

As indicated in Section I, Policy to Track Private Business Use of Tax-Exempt Financed Space, on a continuing basis, the Tax Department should evaluate requests from departments and individuals to use tax-exempt bond financed facilities. Procedures for these requests are outlined in a separate policy entitled "Private Use of Tax-Exempt Financed Facilities." The amount of private use of bond proceeds that results from all private uses of the tax-exempt bond financed facilities should be recorded and tracked throughout the life of the bond.

Finance, on a regular basis, should hold discussions or circulate a questionnaire to departments to determine whether there has been any private business use of the tax-exempt financed facilities. Finance may also find it beneficial to periodically provide education sessions to appropriate personnel within the various departments.

Reporting of Activities

The Tax Department will be responsible for completing Form 990-T (Federal) and any applicable state/local filings to report unrelated business income. The Tax Department should evaluate on a yearly basis the allocation of income and expense to unrelated business activities.

Central recordkeeping requirement

Records must be filed in the Tax Department to meet the recordkeeping requirements of the IRS.

IV. ARTBITRAGE REBATE CALCULATION POLICY

Purpose:

The IRC has strict rules regarding the investment of tax-exempt bond proceeds. Failure to comply with these requirements can result in the loss of tax-exempt status of the bonds. This policy outlines procedures associated with completing arbitrage rebate requirements.

Policy/Procedure:

Policy

IRC §148(f) requires payment to the Internal Revenue Service of the excess of the amount earned on the investment of bond proceeds over the bond yield investment rate. All of the funds and accounts established under a bond issue are subject to this rebate requirement. There are special rules associated with construction and refunding issues. The procedures outlined below are intended to assist in assuring that the rebate requirement is met. These procedures outline general requirements under the IRC and regulations. A review of the bond tax certificate should be performed to determine the specific requirements for any one particular issue.

Procedure

Upon issuance of the bonds, Finance personnel should review the tax certificate to determine if there are any specific arbitrage rebate requirements for the bond issue in addition to the statutory requirements. At a minimum, unless certain exceptions apply, a rebate calculation is required at the end of the fifth bond year, at the end of every fifth bond year thereafter, and upon retirement of the bond. Treasury shall be responsible for ensuring that arbitrage requirements are fulfilled by contracting with a third party to fulfill such requirements.

Special Circumstances

Special circumstances with regards to a bond issue may require more detailed monitoring of arbitrage rebate requirements. These circumstances include:

- Monitoring expenditures prior to semi-annual target dates for six-month, 18-month and 24-month spending exceptions.
- For advance refunding escrows, confirming that any scheduled purchases of State and Local Government series obligations (SLGs) are made on scheduled dates.
- More frequent computations based on an agreement with bond trustee may be required.

Central recordkeeping requirement

Arbitrage rebate records must be filed in the Finance Department to meet the recordkeeping requirements. See Section V, Record Retention Policy, for additional recordkeeping information.

V. RECORD RETENTION POLICY

Purpose:

The IRS provides general rules for the proper retention of records for federal tax purposes. This policy outlines procedures for complying with the record retention rules in connection with tax-exempt bonds.

Policy/Procedure:

Policy

The University of Pennsylvania will retain the records regarding its tax-exempt bonds and their use necessary to support the exclusion from tax.

Procedure

Records to Retain

Certain records in connection with the tax-exempt bonds must be retained for the life of the bond plus 3 years. These records include:

- Basic records relating to the bond transaction (including the trust indenture, loan agreements and bond counsel opinions). These items are also found in the closing binder.
- Documents evidencing expenditure of bond proceeds.
- Documentation evidencing use of bond-financed property by public and private sources (i.e. copies of leases, management contracts and research agreements).
- Documentation evidencing all sources of payment or security for the bonds.
- Documentation pertaining to any investment of bond proceeds (including the purchase and sale of securities, SLGs subscriptions, yield calculation for each class of investments, actual investment income received from the investment of proceeds, guaranteed investment contracts, and rebate calculations).

This list is not inclusive. Each issuance is unique and may therefore have additional documents that are material to the financing. The decision as to whether a certain record is material should be evaluated by Comptroller's Office, Treasurer's Office and Office of General Counsel.

Record Format

Records may be kept in paper or electronic format.

Record Retention

Records should be retained for as long as the bonds are outstanding plus 3 years after the final redemption of the bonds. If upon redemption the bonds are being refunded (another bond is being used to pay back the bonds) then documentation associated with the original bond (the refunded bond) should be maintained until 3 years after the final redemption date of both bond issues.