Ouachita Baptist University

Debt Management Policy

Adopted by Board of Trustees
March 8, 2012

Ouachita Baptist University
Debt Management Policy

Debt is an important tool to achieve the desired long-term strategies of the university. A formal debt policy provides a framework through which management can evaluate the prudent use of debt to achieve strategic goals. While there are advantages of using debt to advance the university's goals, unmanaged debt can financially overburden the university, limiting flexibility. The goal of this policy is to provide guidelines for determining manageable debt levels and debt structures.

Borrowing Authority
Only the Board of Trustees has approval authority to issue debt on behalf of the university, unless the board acts to delegate such authority to university administration. Signature authority to validate notes or leases shall be determined by board action.

Debt Capacity
The objective of university management shall be to maintain financial ratios equivalent to those of an "A" credit rating or higher institution, as reported by Moody's Investor Service, Private College and University Medians. Core financial ratios related to maintaining an "A" credit rating will be calculated from audited financial statements and monitored on a regular basis. At a minimum, the following ratios will be reported to the Board of Trustees annually. These ratios will be compared to median ratios for private higher education institutions and to university trends over time.

> *Expendable Financial Resources to Debt* – This ratio measures the university's leverage on its expendable assets. Expendable resources are unrestricted net assets plus temporarily restricted net assets less net investment in plant. Expected trend is positive.
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> *Total Financial Resources to Debt* – Measures the university's leverage on its total wealth. Total financial resources includes total net assets less net investment in plant. Expected trend is positive.
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> *Debt Service to Operations* – Typical measure used to evaluate a university's use of borrowed funds. Measured by highest annual debt service divided by total operating expense. Expected trend is negative.
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> *Debt Service Coverage* – Operating surplus plus depreciation and interest divided by principal and interest payments. Expected trend is positive or flat.

If the above ratios are not at or above median levels or they are not trending as expected, the presumption is that the university should not consider adding debt. If the ratios are not at or above median levels but they are trending as expected, additional debt capacity is possible but must be reviewed carefully. If the ratios are at or above median levels but they are not trending as expected, additional debt capacity is possible but must be reviewed carefully. If the ratios are at or above median levels and they are trending as expected, additional debt capacity is presumed to be available.

Debt Management

The University adopts the following debt management principles, strategies and procedures. These strategies will be utilized only after debt capacity has been assessed as outlined above.

Funding Principles

1. Only projects that relate to the mission of the University and meet strategic goals of the university will be considered for debt financing.
2. Projects which are self-funding or can create budgetary savings will receive priority consideration.
3. Cash reserves, budget allocations, philanthropy and all other sources of available funds are expected to finance a portion of a project's cost.
4. Management will balance the goal of achieving the lowest cost of capital with the goal of limiting exposure to interest rate risk and other financing and credit risks.
5. Debt is to be used sparingly and strategically.

Tax-exempt bonds are beneficial and the preferred form of financing. Taxable bond financing should be considered for projects that do not qualify for tax-exempt financing. Bank financing may also be considered when financially feasible.

Fixed rate debt will be the primary source of financing but, due to the typically low interest rate costs, variable rate debt may be considered in some situations. Variable rate debt, however, introduces a number of significant risks: the potential volatility of debt service requirements, a risk that associated credit arrangements that expire prior to the maturity of the underlying debt may be difficult or costly to renew, financing arrangements that may include covenants that could accelerate debt repayment and collateral pledge requirements. Thus, the amount of variable rate debt not swapped to fixed rates will be limited. The amount of variable rate debt will vary depending on capital market conditions and the level of interest rates.

Interest rate swaps will be used by the University in a manner consistent with the Derivatives Policy to reduce interest rate risk and to manage variable rate exposure. Interest rate swaps will be evaluated in a framework incorporating a cost/benefit analysis of any derivative instrument, market and interest rate conditions, and counterparty exposure. Under no circumstances will a derivative transaction be utilized that is not fully understood or that imposes inappropriate risk on the University. Only counterparties with ratings of "AA-" or better at the time of the transaction will be used.

Insurance, letters of credit or other credit enhancement features will be considered when feasible to reduce overall borrowing costs.

To obtain the lowest possible financing costs, debt should be structured with the strongest possible authorized security. However, security pledging must not violate restrictions stated in the university's bylaws. Debt maturity structures will not exceed the useful life of the facilities financed. Debt service should not exceed the expected revenues used to repay the debt at any time.

Outstanding debt will be monitored for refunding opportunities. As a general guideline, refunding debt that produces a 3% or greater net present value will be considered. Refunding outstanding debt will also be considered if the University benefits from eliminating restrictive covenants, payment obligations, reserve requirements, security requirements, or from consolidation into larger, more cost-effective transactions. Call features on new issues should be structured to provide maximum flexibility relative to cost.

Debt Compliance

Management will develop and implement procedures to ensure ongoing compliance with bond and loan covenants and requirements, including arbitrage rebate requirements.

Responsibility for implementing this policy and any related procedures lies with the university President and Chief Financial Officer.