MEMORANDUM

TO: The Finance Committee:

Vincent J. Mastracco Jr., Chair
Daniel R. Abramson
A. Macdonald Caputo
The Honorable Alan A. Diamonstein
Helen E. Dragas
Robert D. Hardie
Randal J. Kirk
Austin Ligon
Warren M. Thompson
John O. Wynne, Ex Officio
Daniel M. Meyers, Consulting Member

and

The Remaining Members of the Board:

Susan Y. Dorsey The Hon. Lewis F. Payne
W. Heywood Fralin Don R. Pippin
Glynn D. Key E. Darracott Vaughan, Jr., M.D.
Stewart H. Ackerly

FROM: Susan G. Harris

SUBJECT: Minutes of the Finance Committee Meeting on June 11, 2010

The Finance Committee of the Board of Visitors of the University of Virginia met, in Open Session, at 8:30 a.m., Friday, June 11, 2010, in the Board Room of the Rotunda; Vincent J. Mastracco, Jr., Chair, presided. Present were Daniel R. Abramson, A. Macdonald Caputo, The Honorable Alan A. Diamonstein, Ms. Helen E. Dragas, Robert D. Hardie, Randal J. Kirk, Austin Ligon, Warren M. Thompson, and John O. Wynne, Rector.

Also present were W. Heywood Fralin, Ms. Glynn D. Key, The Honorable Lewis F. Payne, E. Darracott Vaughan, Jr., M.D., and Stewart H. Ackerly.

The Chair asked Mr. Sandridge, Executive Vice President and Chief Operating Officer, to present the Agenda.

ACTION ITEM: DEBT APPROVALS

Mr. Sandridge said because of liquidity concerns, the University did not want to be in the upper range on variable rate debt. He said they are prepared to recommend issuing long term debt next month. They are still attracted to Build America Bonds. He asked Ms. Reynolds to review the details.

Ms. Reynolds said they typically issue long term bonds every year or two years. This is mainly to fund capital projects. The resolution allows issuance of either tax-exempt or Build America bonds (BAB). BAB allows governmental entities to issue in the taxable market and the federal government pays a 35% subsidy on the interest paid. This year the University intends to use a competitive bid rather than a negotiated deal.

Ms. Reynolds said the IRS is looking at "flipping" of BAB bonds—i.e. buying and immediately selling at a higher rate. She believes if the University was audited, we would be in okay shape. Also is the issue of offsets. The IRS has netted out taxes owed from the subsidy. Austin, Texas is an example of a locality that has experienced offset.

Ms. Reynolds said the BAB program was set to expire this year, but it is likely to be extended. The subsidy may be reduced in future years, and so it is important to move quickly. BAB versus tax-exempt will bring a savings of .32%.

Debt analysis shows that the University is within all of the balance sheet ratios. The University has an additional debt capacity of $263 million per the debt ratios, which are conservative. Debt capacity per third party calculation is $371 million. The new debt will be about $175 million.

Ms. Reynolds mentioned that Moody's has changed its municipal ratings scale, combining it with its corporate ratings scale. As a consequence, Moody's number of Aaa-rated public schools increased from 3 to 8. The University still remains only one of two public universities with three triple A ratings.
The projects to be funded with 2010 bonds were presented to the Committee. Mr. Sandridge said each one is brought to the Board as an individual, stand-alone capital project.

Ms. Reynolds said the resolution contains deal parameters including a principal not to exceed $250 million with a final maturity not to exceed 40 years, which will be most likely 30 years.

On motion, the following resolution was adopted:

ISSUANCE OF GENERAL REVENUE PLEDGE BONDS FOR CAPITAL PROJECTS AND DEBT REFUNDING

WHEREAS, Chapter 9, Title 23 of the Code of Virginia of 1950, as amended (the "Virginia Code"), establishes a public corporation under the name and style of The Rector and Visitors of the University of Virginia (the "University") which is governed by a Board of Visitors (the "Board"); and

WHEREAS, Title 23 of the Virginia Code classifies the University as an educational institution of the Commonwealth of Virginia; and

WHEREAS, by Chapter 4.10, Title 23 of the Virginia Code (as amended, the "Act"), the University entered into a management agreement with the Commonwealth of Virginia which was enacted as Chapter 3 of Chapter 933 of the 2006 Virginia Acts of Assembly, which, as amended, classifies the University as a public institution of higher education and empowers the University with the authority to undertake and implement the acquisition of any interest in land, including improvements on the acquired land at the time of acquisition, new construction, improvements or renovations and to borrow money and make, issue and sell bonds of the University for such purposes, including the refinancing of any such facilities; and
WHEREAS, the Act further authorizes the University to provide for the payment of the principal of and the interest on any bonds from any one or more of the following sources: (i) its revenues generally; (ii) income and revenues derived from the operation, sale, or lease of a particular project or projects, whether or not they are financed or refinanced from the proceeds of such bonds, notes, or other obligations; (iii) funds realized from the enforcement of security interests or other liens or obligations securing such bonds, notes, or other obligations; (iv) proceeds from the sale of bonds, notes, or other obligations; (v) payments under letters of credit, policies of municipal bond insurance, guarantees, or other credit enhancements; (vi) any reserve or sinking funds created to secure such payment; (vii) accounts receivable of the University; or (viii) other available funds of the University; and

WHEREAS, the Board has previously approved resolutions declaring an intent to issue bonds and has authorized the issuance of debt funding for the costs associated with projects described in Exhibit A (the "Projects"); and

WHEREAS, a portion of the Projects has been financed on a short-term basis through issuance of the University's commercial paper (the "Commercial Paper Program"); and

WHEREAS, the Board desires to provide for the refunding of all or a portion of its outstanding bonds, (the "Outstanding Bonds"); and

WHEREAS, the Board desires to authorize the issuance of bonds in one or more series for financing or refinancing of all or a portion of the costs associated with the Projects, for the refunding of all or a portion of the outstanding principal amount of the Commercial Paper Program and for the refunding of all or a portion of the University's Outstanding Bonds, desires such bonds to be issued bearing interest at either tax-exempt or taxable rates including without limitation all or a portion as "Build America Bonds" or similar program provided for in the American Recovery and Reinvestment Act of 2009, and desires to authorize certain officers of the University to approve the final forms and details of the bonds, as set forth below; and

WHEREAS, the Board anticipates that the bonds will be secured by a general revenue pledge of the University and not be
in any way a debt of the Commonwealth of Virginia (the "Commonwealth") and shall not create or constitute any indebtedness or obligation of the Commonwealth, either legal, moral, or otherwise; and

RESOLVED, the Board hereby implements the plan of finance described in the Recitals by authorizing the issuance of one of more series of bonds for the purpose of financing or refinancing any or all of the costs associated with the Projects, including without limitation, capitalized interest, financing costs and working capital related thereto consistent with the University's debt policy, and for the purpose of refunding all or a portion of the outstanding principal amount of the Commercial Paper Program and the Outstanding Bonds, and providing for the terms thereof by the subsequent adoption by the Board or its Executive Committee of one or more bond resolutions (collectively, the "Bond Resolution"); and

RESOLVED FURTHER, the Vice President and Chief Financial Officer of the University, with the Chair of the Board's Finance Committee, is authorized to approve the final terms of each series of bonds, including, without limitation, their original principal amounts and series, the specific Projects to be financed or refinanced, the specific refundings to be undertaken, their maturity dates and amounts, redemption provisions, make-whole provisions, prices, interest rates and interest provisions, and any elections under the federal tax code, provided that (i) the maximum aggregate principal amount of all bonds to be issued hereunder shall not exceed $250 million; (ii) the maximum initial true interest cost of variable-rate obligations will not exceed five percent (5%) per annum (iii) the maximum true interest cost of any series bearing interest at a tax-exempt fixed rate shall not exceed six percent (6%) per annum; (iv) the maximum true interest cost of any series bearing interest at a taxable fixed rate shall not exceed eight percent (8%) per annum; (v) the final maturity of all bonds shall not exceed 40 years beyond issuance date; (vi) call protection on any tax-exempt bonds shall not exceed ten and one-half (10½) years; and (vii) no optional redemption premium on any tax-exempt bonds shall exceed two percent (2%) and

RESOLVED FURTHER, either of the Executive Vice President and Chief Operating Officer of the University or the Vice President and Chief Financial Officer of the University are hereby authorized to negotiate, execute and deliver all
RESOLVED FURTHER, all officers of the University are authorized and directed to take all such further actions, including without limitation the designation of underwriters, paying agents, remarketing agents, trustees, and liquidity providers for the bonds, and to execute all such instruments, agreements, documents, and certificates as they shall deem necessary or desirable to carry out the terms of the financing plans presented to this meeting, including without limitation any liquidity facilities, swap or other interest rate management agreements associated with the bonds; and

RESOLVED FURTHER, pursuant to the Section 147(f) of the Internal Revenue Code of 1986, as amended, and applicable regulations thereunder, the University designates the Vice President and Chief Financial Officer of the University as the public hearing officer to hold any public hearings required in order to ensure the tax-exempt status of interest on all or any portion of the Bonds; and

RESOLVED FURTHER, all acts of all officers of the University which are in conformity with the purposes and intent of this Resolution and in carrying out the financing plans presented to this meeting are ratified, approved and affirmed; and

RESOLVED FURTHER, upon approval, this action shall take effect immediately.
ACTION ITEM: AUTHORIZATION FOR AN UNRESTRICTED LINE OF CREDIT

Mr. Sandridge asked Ms. Reynolds to explain why the University is asking for an unrestricted line of credit. Ms. Reynolds said the University has a line of credit with a bank. They would like authorization from the Board for $50 million additional in an unrestricted line of credit with a second bank. This would provide flexibility and is a first step in reducing credit exposure to one counterparty.

On motion, the Committee adopted the following resolution and recommended it to the full Board for approval:

AUTHORIZATION OF AN UNRESTRICTED LINE OF CREDIT

WHEREAS, the University is completing the process of assuring it has adequate liquidity to fund operations and protect itself against liquidity risks; and

WHEREAS, the University currently has $250 million of dedicated lines of credit to provide backup liquidity for its $82.01 million of variable-rate bonds and $300 million commercial paper program; and

WHEREAS, the University’s $250 million of credit lines are provided by one bank and the University seeks to enhance and diversify its credit profile by entering into a $50 million unrestricted line of credit with a second bank (the “Credit Facility”); and

WHEREAS, the Credit Facility will benefit the University by (1) providing it with additional credit that can be used to support operating and other needs, and (2) diversifying its credit providers;

RESOLVED, the Board of Visitors hereby authorizes the University to enter into the Credit Facility; and

RESOLVED FURTHER, the Vice President and Chief Financial Officer of the University shall be authorized to negotiate, execute, and deliver certain documents related to the Credit Facility, including, without limitation, a Revolving Credit Agreement; and

RESOLVED FURTHER, the Vice President and Chief Financial Officer and all other officers of the University are authorized and directed to take all such further actions, and to execute
all such instruments, agreements, documents, and certificates as they shall deem necessary or desirable in connection with the Credit Facility; and

RESOLVED FURTHER, all acts of all officers of the University which are in conformity with the purposes and intent of this Resolution are ratified, approved, and affirmed; and

RESOLVED FURTHER, upon approval, this action shall take effect immediately.

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ACTION ITEM: ADDITION TO THE MAJOR CAPITAL PROJECTS PROGRAM

Mr. Sandridge asked Ms. Sheehy to present the major capital projects program update. Ms. Sheehy said the two projects are an East Chiller Plant, and a combined Engineering School and Facilities Management building for both student projects and to provide additional shop space for Facilities Management. The University has received $1.7 million in gifts for the Facilities Management/Engineering building.

On motion, the Committee adopted the following resolution and recommended it to the full Board for approval:

APPROVAL OF FINANCIAL PLANS FOR NEW CAPITAL PROJECTS

WHEREAS, the University proposes to add the East Chiller Plant ($25.8 - $29.0 million) and the School of Engineering and Applied Science Student Projects/Facilities Management Shop Building ($3.5 - $4.2 million) projects to the University’s Major Capital Projects Program; and

WHEREAS, the $57 million North Chiller Plant Replacement Chillers project currently listed in the Major Capital Projects Program will be removed at the next revision of the program; and

WHEREAS, the $1 million School of Engineering and Applied Science Student Projects Building currently listed in the Major Capital Projects Program will be removed at the next revision of the program; and

WHEREAS, an enforceable gift agreement at least equal to the Engineering School’s share of the joint School of Engineering and Applied Science/ Facilities Management Shop building must be received prior to starting the project;
RESOLVED, the financial plan for the East Chiller Plant is reasonable and complete with the estimated $25.8 - $29.0 million cost to be financed with University bonds and repaid from Medical Center operating revenues and Utility Infrastructure Fund reserves;

RESOLVED FURTHER, the financial plan for the School of Engineering and Applied Science Student Projects/Facilities Management Shop Building is reasonable and complete, with the estimated $3.5 - $4.2 million cost to be funded by $1.7 million in gifts documented by a valid gift agreement and $1.8 - $2.5 million in Facilities Management operating reserves.

**ACTION ITEM: PROJECT SCOPE AND BUDGET REVIEW, MCLEOD HALL RENOVATION**

Ms. Sheehy said the McLeod Hall renovation can be done in phases to match the gifts received. Renovation will reduce deferred maintenance on the building.

On motion, the Committee adopted the following resolution and recommended it to the full Board for approval:

**APPROVAL OF PROJECT BUDGET AND SCOPE REVIEW, MCLEOD HALL RENOVATION**

RESOLVED, that an increase to the McLeod Hall Renovation project of $8,735,000 and 20,000 gross square feet, bringing the total project to $14,810,000 and 50,000 gross square feet, is approved contingent on the availability of gifts in hand and documented enforceable pledges.

**ACTION ITEM: 2010-2011 BUDGET**

Mr. Sandridge began the discussion of the 2010-2011 Budget. The total budget is about $2.4 billion. It is an increase of 4.2% over the previous year. The increase in the academic division budget is because of research activity and state economic stimulus funds which are still in the budget. The same is true for the College at Wise.

Employment levels will increase from last year by 292, primarily to support the new buildings coming on line and the staff related to increased amount of research activity in part related to stimulus money. Those hires are employed on the basis of availability of funds.

Mr. Sandridge said the University has been able to take some modest steps to strengthen certain areas. They have tried to avoid
making long-term commitments, and they have tried to position the University to not have to take drastic action when the stimulus funds are removed next year. Also, this is the third year that employees have not received increases. The budget has a 3% bonus built into it. Finally, the budget attains the target operating margin of 4.9% for the Medical Center.

Mr. Sandridge introduced Ms. Sheehy to review the details of the academic budget and the College at Wise. Ms. Sheehy said the Board has already approved many aspects of the budget such as tuition.

Ms. Sheehy said patient revenues, tuition and fees, and sponsored programs are the largest sources of revenue for the University. She turned to a discussion of the academic division. The academic division available funds are $1.333 billion. The state appropriation will be 10.2% of the total. Stimulus money is built into the budget. There are 8,800 full time equivalent (FTE) positions in the academic division.

New money available in the budget includes $25 million in new tuition; $21.9 million in stimulus money; other sources are $3.4 million; and general fund money of $271,000. It will be spent on a long list of prior commitments including operation and maintenance of facilities and the student system maintenance and support, addenda allocations, and one-time funds of $21.9 million. The stimulus money will be used for AccessUVA in its entirety, which will free up other unrestricted funds for other purposes.

Addenda allocations include: $841,000 for the School of Medicine new curriculum and enrollment growth; Alderman Library collections; School of Nursing graduate teaching support; Curry School graduate fellowships; Museum support; summer session and January term expanded offerings; Batten School base support; and support for the Engineering School Produced in Virginia program. Addenda allocations for support services include funds for student financial services; environmental health and safety; Southwest Virginia Economic Development partnership; new associate dean of students; and others.

Ms. Sheehy said the potential 3% bonus will cost the University $7.6 million. There is a contingency reserve of $4.1 million that will serve as a buffer for the scheduled reduction in state funding next year.

Ms. Sheehy said there are challenges: the University has positioned itself in a way that it will not be dependent on the stimulus funds for ongoing support, however, the reductions in state support predicted to be $14.7 million in 2011-2012 will be difficult to address. Other challenges include faculty compensation, and addressing higher research infrastructure costs with a flat revenue stream.
Ms. Sheehy mentioned the Pratt Fund. It may be used for faculty salaries, scholarships, and equipment in the Departments of Biology, Mathematics, Physics, and Chemistry, as well as for research and scholarships in the School of Medicine. The endowment has a market value of $97.5 million. The 2010-2011 Pratt Fund allocation for the School of Medicine is $2.3 million and for the College of Arts and Sciences it is $2.4 million.

Ms. Sheehy turned to the College at Wise budget. She said it has flat enrollment projected for next year. Approximately 46% of the College’s budget comes from the state General Fund, so what the state does impacts them heavily.

The annual renovation and infrastructure projects plan, which is funded with all cash, is $21.8 to $26.6 million for the academic division and $37 to $42 million for the Medical Center.

Mr. Sandridge called on Mr. Howell to present the Medical Center budget. Mr. Howell said the budget was a challenge to put together this year with the opening of the Transitional Care Hospital, the uncertainty about Medicare and indigent care funding, and other issues. Mr. Howell asked Larry Fitzgerald to present the budget details. Mr. Fitzgerald said there is a reduction in Medicare and indigent care funding that will reduce revenues by $9.6 million. The impact of federal healthcare reform is uncertain. An immediate impact is a reduction in Medicare funding.

Mr. Fitzgerald said they have been able to maintain a clinical workforce, and they are working hard to manage length of stay, which can have a significant impact on revenues. The conversion to the electronic medical record will be difficult especially on the outpatient side.

The Medical Center budgeted operating income is $52.9 million, which is the first time it has exceeded $50 million. The operating margin is 4.9%. The budget does not include gains in investments with UVIMCO. He said the case mix index is very high and above benchmark at 1.90. Length of stay is close to the benchmark at 6.0.

Mr. Sandridge asked the Committee to approve the budget resolutions. On motion, the following resolutions were approved and recommended to the full Board for approval:

APPROVAL OF THE 2010-2011 OPERATING BUDGET AND ANNUAL RENOVATION AND INFRASTRUCTURE PLAN FOR THE ACADEMIC DIVISION

RESOLVED, the 2010-2011 Operating Budget and Annual Renovation and Infrastructure Plan for the Academic Division is approved, as recommended by the President and the Chief Financial Officer.
APPROVAL OF THE 2010-2011 OPERATING BUDGET FOR THE UNIVERSITY OF VIRGINIA'S COLLEGE AT WISE

RESOLVED, the 2010-2011 Operating Budget for The University of Virginia’s College at Wise is approved, as recommended by the President and the Chief Financial Officer.

APPROVAL OF THE 2010-2011 OPERATING AND CAPITAL BUDGETS AND ANNUAL RENOVATION AND INFRASTRUCTURE PLAN FOR THE UNIVERSITY OF VIRGINIA MEDICAL CENTER

RESOLVED, the 2010-2011 Operating and Capital Budget and the Annual Renovation and Infrastructure Plan for the University of Virginia Medical Center is approved, as recommended by the President, the Chief Financial Officer, and the Medical Center Operating Board.

APPROVAL OF PRATT FUND DISTRIBUTION FOR 2010-2011

RESOLVED, the budget for the expenditure of funds from the Estate of John Lee Pratt is approved to supplement appropriations made by the Commonwealth of Virginia for the School of Medicine and the Departments of Biology, Chemistry, Mathematics and Physics in the College of Arts and Sciences. Departmental allocations, not to exceed $4,700,000 for 2010-2011, are suggested by the department chairs and recommended by the dean of each school. To the extent the annual income from the endowment is not adequate to meet the recommended distribution, the principal of the endowment will be disinvested to provide funds for the approved budgets.

Vice President’s Remarks

Mr. Sandridge said the University has renewed a fire services agreement with the City of Charlottesville for 10 years. The annual fee is $250,000 subject to inflation adjustments. The City has agreed to build a fire station close to the University on Fontaine Avenue, and the University will contribute $750,000 toward the costs of this new fire station. The City also will provide accommodations for up to four students in the fire station. The City and County will vacate property on 250 West next to the University police station when the Fontaine site is operational. The City has also agreed to set aside $40,000 a year for the regional hazardous materials response team, which is important to the University because of its 1900 research labs.

Mr. Sandridge also mentioned health care reform legislation. Some of the requirements do not affect the University, however, the current lifetime health benefits maximum for individuals must be removed from the health plan, and the plan must allow dependents up to age 26 to be covered under the parents’ plan.
Mr. Sandridge said the Retirement Administrative Committee report on page 29 of the Committee Booklet is important. The Committee, which oversees the retirement program, includes Mr. Mastracco and Ms. Dragas. At the recent meeting, they reviewed the funds' performance and due diligence underway with the three vendors to reduce administrative costs. No changes in the plan are recommended at this time. The Chair added that Ms. Reynolds is the chair of the Committee and it is well run, providing employees with advice on investing and a number of funds to choose from.

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University of Virginia Investment Management Company

Mr. Sandridge asked Mr. Caputo to give an overview of the University of Virginia Investment Management Company (UVIMCO) CEO search. Mr. Caputo is the Chair of the UVIMCO Board. Mr. Caputo said the search committee is the Executive Committee of the UVIMCO Board plus a staff member and another Board member. After reviewing a number of firms, they chose Spencer Stuart as the search firm. Mr. Caputo asked the Board members to consider making referrals of candidates. He said the team at UVIMCO is a great team, they are just looking for a new leader.

Mr. Caputo turned over the discussion to Michael Aked to give a quarterly endowment report. Mr. Aked is a Managing Director of UVIMCO.

Mr. Aked explained the governance structure of UVIMCO, which is a 501(c)(3) tax-exempt organization. There are 10 members of the Board of Directors and 25 staff members. He said John Macfarlane is leading the investment committee and Leonard Sandridge is handling administration during this interim period.

He said the current long term pool is $4.6 billion. The performance strategy is focused on long-term gains. Ten year historical performance is 8%, which is double the policy benchmark. The major sectors are equity, real assets, and fixed income. Each sector has delivered about the same return over the ten year historical period. Current fiscal year to date return is 17% which trails the policy benchmark at 22.8%. Public equity and fixed income have done well, but the alternative assets have done less well.

Mr. Aked reviewed the peer data that is available. The "official" peer group is the Cambridge $2 billion plus endowments of colleges and universities. This peer group historically has outperformed others. UVIMCO has been in the top quartile over a ten year period.
Mr. Aked said UVIMCO has changed its strategy allocations over the last five years by decreasing hedge funds and increasing private assets. From June 2009 to June 2010, the only change has been a reduction in bond and cash investments.

The position analysis indicates that the portfolio has a large exposure to North America. This is driven by the desire and ability of managers to find investments in large, North American corporations. Currency is an outtake of that; there is an 80% exposure to the U.S. dollar and only a small exposure to the euro and Asian currencies.

Liquidity in the portfolio has been a recent focus. The private portfolio investment exposure is 38%. The private aggregate (investments and unfunded commitments) is 64%, which is slightly above where they would like to be over the long term. The endowment could manage up to five years without distributions from private managers. Unfunded commitments are lower than previously as a percentage of the portfolio.

Mr. Aked said that going forward they expect the market to deliver a 5% nominal return over the next 10-to 20-year period. The endowment is expected to deliver an 8% return over the same period. Annualized returns over a 10-year period should be within the zero to 18% range.

The Chair adjourned the Finance Committee meeting at 10:30 a.m.

SGH: jb
These minutes have been posted to the University of Virginia’s Board of Visitors website.
http://www.virginia.edu/bov/financeminutes.html