GENERAL REPORT

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Ben Langley

USHE – Debt Ratio Analysis

Background

During the March 2014 Regents Finance & Facilities Committee review of [R588, *Delegation of Debt Policy to Boards of Trustees*][1], several members recommended the Commissioner's office prepare a systemwide debt ratio analysis to be presented in a future meeting and consider including in policy a statement requiring institutions to annually provide an informational debt report to the USHE Board of Regents.

Three common ratios were chosen (viability, debt burden, and composite score) that historically have proven to be good basic measures, from the KPMG publication, *Strategic Financial Analysis for Higher Education: Identifying, Measuring & Reporting Financial Risks*[2]. Each ratio is defined and presented by each institution, using industry standards and formulas.

- **Viability Ratio** — measures how many times an institution can cover its entire long-term debt obligation using their total expendable net assets. A ratio of 1:1 or greater indicates that an institution has sufficient expendable net assets to satisfy debt obligations. As the ratio falls below 1:1, the institution's ability to respond to adverse conditions from internal resources diminishes, as does its ability to attract capital from external sources and its flexibility to fund new objectives.

- **Debt Burden Ratio —** measures an institution's dependence on borrowed funds to finance its operation, by measuring the relative cost of borrowing to overall expenditures. Industry standards recommend 7% as the upper threshold for a healthy institution. The higher the ratio, the fewer resources are available for other operational needs. A level trend, or a decreasing trend, indicates that debt service has sufficient coverage, whereas a rising trend signifies an increasing demand on financial resources to pay back debt.

- **Composite Index —** this calculation combines and weights all four ratios (viability, debt burden, leverage, and primary reserve) into one single financial metric. This allows a weakness or strength in a specific ratio to be offset by another ratio result, thereby allowing a more holistic

[1] Utah System of Higher Education, *R588, Delegation of Debt Policy to Boards of Trustees,* https://ushe.edu/ushe-policies/r588-delegation-of-debt-policy-to-boards-of-trustees/
[2] KPMG Institutes, *Strategic Financial Analysis for Higher Education: Identifying, Measuring & Reporting Financial Risks, 7th edition,* http://nacubo.org/

approach to understanding the institution's total financial health. KPMG's publication establishes a threshold value of 3.0 for institutions that are considered to have a good financial position.

Institutional Controllers submitted all financial information from their audited annual financial statements and will have reviewed the results along with Chief Financial Officers, Budget Officers, and OCHE staff.

Ratio Calculation Observations

Salt Lake Community College

Salt Lake Community College had no debt at Fiscal Year-End, June 30, 2016. During FY 2017, their only debt was a DFCM Energy Loan, which is an interest-free vehicle. This resulted in ratios that were not meaningful. For this reason, the report reflects "no debt" for both FY 2016 and 2017.

Snow College

Between FY 2015 and FY 2018, Snow College's viability ratio was below the standard. The components of the viability ratio are expendable net assets/long-term debt. For FY 2019, Snow's viability ratio is above the standard at 1.25. The reason for this is an increase in Snow's expendable net assets. Snow's viability ratio increased in FY 2019 because the college had better investment earnings, grant revenue was higher than prior years, and the foundation started a few different campaigns that increased the college's gift revenue.

Southern Utah University

During FY 2018 and 2019, Southern Utah University had a decline in its viability ratio and composite index. During fiscal years 2017 through 2019, SUU engaged in financing arrangements for the acquisition of airport hangars, flight simulators, and various fixed-wing and rotor-wing aircraft for the operation of an aviation program. Total funding under these arrangements amounted to $13.3 million, with a large share ($10.9 million) on a seven-year lease-purchase arrangement, with the balance primarily financed through seven-year or 10-year notes payable to various individuals and entities. The current amount outstanding on these financing arrangements is $10.3 million. This is in addition to the $12.4 million still outstanding on the issuance of 2011 auxiliary and 2016 refunding bonds. It should be noted that SUU is still well within the standard for the viability and composite index.

Ratios Not Meeting Standards

Dixie State University

Dixie State University recognizes that its viability ratio has been under the standard. The composite index is also below the standard, but there is an increase to 2.28 in FY 2019. The main component that is negatively affecting the viability ratio and the composite index is the amount of long-term debt that DSU has. As a growing institution, DSU must plan for the future. Part of that planning is to ensure that they have the appropriate housing and other facilities for their student population in place. To meet these needs, the issuance of long-term bonds is sometimes necessary. The ratios are lower because DSU has bonded for student housing and for the Human Performance Center, which provides a facility to meet the health and recreation needs of both current and future students. These facilities are necessary to meet DSU's growing student base.

Southern Utah University

In FY 2016, Southern Utah University had a debt burden ratio of 9.3% which is 2.3% higher than the standard. During FY 2016, the College acquired refunding bonds. SUU used the proceeds from these bonds to pay off $10 million of their 2008 auxiliary bonds. There was also a $3.4 million reduction from the payoff of a line of credit for construction of SUU's Center for the Arts project that was completed that year. It should be noted that this is the only year from FY 2015 to FY 2019 that the ratio is out of the expectation. All of the other years presented are well within the 7% threshold.