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FOR
MEETING OF THE BOARD

Board Meeting: 8/9-10/2006
Arlington, Texas

<u>Wednesday, August 9, 2006 (continued)</u>	**Board/Committee Meetings**
b. U. T. System: Discussion and appropriate action regarding individual personnel matters relating to appointment, employment, evaluation, compensation, assignment, and duties of presidents (academic and health institutions), U. T. System Administration officers (Executive Vice Chancellors and Vice Chancellors), other officers reporting directly to the Board (Chancellor, Counsel and Secretary, and Director of Audits), and individual personnel aspects of the operating budget for the year ending August 31, 2007	
C. RECONVENE IN OPEN SESSION TO CONSIDER ACTION ON EXECUTIVE SESSION ITEMS	*1:25 p.m.*
D. RECESS FOR COMMITTEE MEETINGS	*1:30 p.m.*
Student, Faculty, and Staff Campus Life Committee	*1:30 – 2:45 p.m.*
Health Affairs Committee	*2:45 – 3:45 p.m.*
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E. RECESS	*5:15 p.m.*

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F.	RECONVENE IN OPEN SESSION	*8:00 a.m.*	
G.	APPROVAL OF MINUTES		
H.	CONSIDER AGENDA ITEMS		
1.	**U. T. System: Presentation on the state of the U. T. System**	*8:02 a.m.* **Report** *Chancellor Yudof*	**1**
2.	**U. T. System: Presentation and discussion of the draft U. T. System Strategic Plan and approval to complete and publish the Plan**	*8:15 a.m.* **Report/Action** *Chairman Huffines* *Chancellor Yudof* *Dr. Malandra*	**1**
3.	**U. T. System: Appropriation of $423.66 million of Permanent University Fund Bond Proceeds; amendment of the FY 2006-2011 Capital Improvement Program and the FY 2006-2007 Capital Budget to add projects; approval of modification of funding for previously approved projects; appropriation of funds for previously approved projects in the Capital Budget; appropriation of funds for repair and rehabilitation projects; resolution regarding parity debt; and authorization of institutional management for U. T. Southwestern Medical Center - Dallas North Campus Phase 5 project**	*9:00 a.m.* **Action** *Dr. Kelley*	**1**
4.	**U. T. System: Approval of Permanent University Fund Bond Proceeds allocation for Library, Equipment, Repair and Rehabilitation Projects for fiscal year ending August 31, 2007**	*9:15 a.m.* **Action** *Dr. Kelley*	**8**
5.	**U. T. System: Approval of the nonpersonnel aspects of the operating budgets for the fiscal year ending August 31, 2007**	*9:30 a.m.* **Action** *Chancellor Yudof* *Mr. Wallace*	**11**
6.	**U. T. System Board of Regents: Proposed appointment of George Willeford III, M.D., as Regental Representative to U. T. Austin Intercollegiate Athletics Council for Men and appointment of Dr. Susan C. Blackwood and reappointment of Mrs. Sylvie P. Crum as Regental Representatives to Intercollegiate Athletics Council for Women Effective September 1, 2006**	*9:45 a.m.* **Action** *Chairman Huffines*	**11**
7.	**U. T. System Board of Regents: Amendment to the Regents' *Rules and Regulations*, Series 10401, related to meetings of the Board and Standing Committees to add a new Section 6 related to accessibility**	*9:47 a.m.* **Action** *Ms. Frederick*	**13**
8.	**U. T. System Board of Regents: Amendments to the Regents' *Rules and Regulations*, Series 20202 (Presidential Cash Compensation) including retitling as Cash Compensation for Chief Administrative Officers**	*9:49 a.m.* **Action** *Ms. Frederick* *Mr. Wallace*	**14**

	Thursday, August 10, 2006 (continued)	Board Meeting	Page
9.	**U. T. System Board of Regents: Amendments to the Regents' *Rules and Regulations*, Series 20203 (Compensation for Key Executives)**	*9:51 a.m.* **Action** *Ms. Frederick* *Mr. Wallace*	**21**
10.	**U. T. System Board of Regents: Amendment to the Regents' *Rules and Regulations*, Series 20101, Sections 3.4 and 3.9 related to appointment of officers by the Chancellor**	*9:53 a.m.* **Action** *Ms. Frederick* *Mr. Wallace*	**24**
11.	**U. T. System Board of Regents: Amendment to the Regents' *Rules and Regulations*, Series 20201, Section 4.9 concerning the role of faculty, staff, and student governance groups, as appropriate, in the development of an institution's operating procedures**	*9:55 a.m.* **Action** *Dr. Malandra* *Dr. Shine*	**28**
12.	**U. T. System Board of Regents: Amendment of the Regents' *Rules and Regulations*, Series 60301 related to the development boards; Series 60302 related to advisory councils; and deletion of Series 60303 related to internal foundations**	*10:00 a.m.* **Action** *Dr. Safady* *Mr. Burgdorf*	**29**
13.	**U. T. System Board of Regents: Approval of the University of Texas Investment Management Company (UTIMCO) Board recommendations to (a) amend Exhibit A of the Investment Policy Statements for the Permanent University Fund (PUF), the General Endowment Fund (GEF) and the Intermediate Term Fund (ITF) related to the adoption of a new benchmark for the hedge fund asset class, effective January 1, 2006, for the PUF and the GEF, and effective February 1, 2006, for the ITF; and (b) restate and republish the hedge fund benchmark performance for the period January through April 2006**	*10:05 a.m.* **Action** *Regent Caven* *Mr. Boldt*	**44**
14.	**U. T. System Board of Regents: Approval of Restated University of Texas Investment Management Company (UTIMCO) Compensation Program**	*10:15 a.m.* **Action** *Regent Caven*	**52**
15.	**U. T. System Board of Regents: Approval of the Annual Budget, including the capital expenditure budget, and Annual Fee and Allocation Schedule for The University of Texas Investment Management Company (UTIMCO)**	*10:25 a.m.* **Action** *Regent Caven* *Dr. Kelley*	**97**
16.	**U. T. Medical Branch - Galveston: Discussion of implementation of Performance Improvement Plan**	*10:35 a.m.* **Report** *President Stobo*	**129**
17.	**U. T. System Board of Regents: Report on the Archer Center, Washington, D.C.**	*10:50 a.m.* **Report** *Mr. Shute*	**129**
I.	RECESS FOR MEETINGS OF THE STANDING COMMITTEES AND COMMITTEE REPORTS TO THE BOARD	*11:05 a.m.*	
J.	RECONVENE AS COMMITTEE OF THE WHOLE	*11:45 a.m.*	

1. **U. T. System: Presentation on the state of the U. T. System**

REPORT

Chancellor Yudof will present a report on the state of The University of Texas System. This is the first annual report and will precede a series of standard reports at each quarterly meeting of the Board.

2. **U. T. System Board of Regents: Presentation and discussion of the draft U. T. System Strategic Plan and approval to complete and publish the Plan**

RECOMMENDATION

Dr. Geri H. Malandra, Associate Vice Chancellor for Institutional Planning and Accountability and Interim Executive Vice Chancellor for Academic Affairs, Chairman Huffines, and Chancellor Yudof will outline the key elements of the Strategic Plan final draft, including the framework and context, strategic directions, priorities and initiatives, metrics to assess results, implementation steps, and related issues.

BACKGROUND INFORMATION

Board members will receive copies of the PowerPoint presentation, draft Executive Summary, and draft Plan in a separate mailing in advance of the meeting. At the Board meeting on May 11, 2006, the Board reviewed the outline for this Plan and a full preliminary draft was distributed for comment on June 9.

3. **U. T. System: Appropriation of $423.66 million of Permanent University Fund Bond Proceeds; amendment of the FY 2006-2011 Capital Improvement Program and the FY 2006-2007 Capital Budget to add projects; approval of modification of funding for previously approved projects; appropriation of funds for previously approved projects in the Capital Budget; appropriation of funds for repair and rehabilitation projects; resolution regarding parity debt; and authorization of institutional management for U. T. Southwestern Medical Center - Dallas North Campus Phase 5 project**

RECOMMENDATION

In accordance with the draft U. T. System Strategic Plan (see Item 2 above), the Constitutional debt capacity of the Permanent University Fund (PUF), and the passage of HB 153 by the 79th Legislature that authorized Tuition Revenue Bond (TRB) funding for U. T. System institutions, the Chancellor, the Interim Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Health Affairs, and the Executive Vice Chancellor for Business Affairs recommend that the U. T. System Board of Regents:

a. approve the appropriation of $423,660,000 of PUF Bond Proceeds for 22 capital projects listed in Table 1 on Page 4;

b. amend the FY 2006-2011 Capital Improvement Program (CIP) and the FY 2006-2007 Capital Budget to add projects as set forth in Table 2 on Page 5;

c. approve modifications in funding and revised project costs for previously approved projects in the FY 2006-2007 Capital Budget as set forth in Table 3 on Page 6;

d. appropriate funds for repair and rehabilitation projects as set forth in Table 4 on Page 7;

e. resolve in accordance with Section 5 of the Amended and Restated Master Resolution Establishing The University of Texas System Revenue Financing System that:

    - parity debt shall be issued to pay the projects' cost, including any costs prior to the issuance of such parity debt;

    - sufficient funds will be available to meet the financial obligations of the U. T. System, including sufficient Pledged Revenues as defined in the Master Resolution to satisfy the Annual Debt Service Requirements of the Financing System, and to meet all financial obligations of the U. T. System Board of Regents relating to the Financing System;

    - U. T. Arlington, U. T. Austin, U. T. El Paso, and U. T. San Antonio, which are "Members" as such term is used in the Master Resolution, possess the financial capacity to satisfy their respective direct obligations as defined in the Master Resolution relating to the issuance by the U. T. System Board of Regents of tax-exempt parity debt in the amount of $3,000,000, $25,000,000, $3,900,000, and $2,250,000, respectively.

f. authorize U. T. Southwestern Medical Center - Dallas to manage the total project budgets, appoint architects, approve facility programs, prepare final plans, and award contracts for the North Campus Phase 5 project.

BACKGROUND INFORMATION

The U. T. System Strategic Plan 2006-2015, drafted for consideration by the U. T. System Board of Regents on August 10, 2006, addresses the challenges for higher education in the 21st century, including 1) global integration and competition; 2) science, technology, and economic gaps in Texas; 3) demographic pressures; 4) the need to balance quality and growth; and 5) the opportunity to capitalize on the distinctiveness of the U. T. System by leveraging its resources across institutions.

The 26 capital projects to be considered as part of this Agenda Item represent a significant step forward at all 15 U. T. System institutions in addressing these challenges, particularly in terms of physical capacity for areas of focus such as science, technology, engineering, and medicine.

The total project cost of the 26 facilities is $1,622,495,673, and will be financed primarily by Tuition Revenue Bonds ($848,876,000) reimbursed by the State and Permanent University Fund Bonds ($423,660,000) paid through distributions from the PUF endowment. The remainder of the project costs will be financed with Federal Grants ($116,090,673), Revenue Financing System debt ($82,039,000), Gifts ($135,230,000), and Insurance Proceeds ($16,600,000). Any gift shortfalls will be covered by the institution.

As of May 31, 2006, the U. T. System's Constitutional debt capacity for the PUF was $818,400,000. The debt capacity is calculated as 20% of the cost value of the PUF endowment less PUF debt outstanding and authorized but unissued.

The projects to be added to the CIP include 11 New Construction projects totaling $735,945,000 and four Repair and Rehabilitation projects totaling $151,500,000 as itemized in Table 2 on Page 5. Ten existing FY 2006-2011 CIP projects will receive new PUF funding. Of the 10 projects, four are New Construction and six are Repair and Rehabilitation. Two existing projects will receive an increase in project cost and PUF funding. A summary of the adjustments to appropriations is reflected in Table 3 on Page 6. Projects that are New Construction will receive appropriation of funds at design development approval.

Repair and Rehabilitation projects will receive appropriation of funds through approval of this item, as shown in Table 4 on Page 7. The proposed off-cycle projects have been approved by U. T. System staff and meet the criteria for inclusion in the Capital Improvement Program. U. T. Southwestern Medical Center - Dallas Facilities Management personnel have the experience and capability to manage all aspects of the work for the North Campus Phase 5 project.

In accordance with Regents' *Rules and Regulations*, Series 80302, selected proposed projects listed in Table 2 will be reviewed to determine if any are of special interest to the Board because of proposed building site, historical or cultural significance, proposed use, or other unique characteristics. (See Item 2 in the Facilities Planning and Construction Committee on Page 223.)

Table 1
Request to Amend The University of Texas System
FY 2006-2011 Capital Improvement Program and FY 2006-2007 Capital Budget

Institution	Project	Total Project Cost	TRB Authority	Proposed PUF Funding	RFS	Gifts	Insurance & Grants
U. T. System Academic Institution Tuition Revenue Bond Projects							
UT Arlington	Engineering Research Building	80,430,000	70,430,000	10,000,000			
UT Austin	Experimental Science Building Renovation	125,000,000	105,000,000	20,000,000			
UT Brownsville	Science and Technology Learning Center	33,800,000	33,800,000	-			
UT Dallas	Vivarium and Experimental Space	15,000,000	12,000,000	3,000,000			
UT El Paso	Physical Sciences / Engineering Core Facility	85,000,000	76,500,000	8,500,000			
UT Pan American	Fine Arts Academic and Performance Complex	49,745,000	39,796,000	-	9,949,000		
UT Pan American	Starr County Upper Level Center	7,500,000	6,000,000	-	1,500,000		
UT Permian Basin	Science and Technology Complex	56,000,000	54,000,000	2,000,000			
UT Permian Basin	Arts, Convocation, and Classroom Facility at the CEED	51,000,000	45,000,000	3,000,000		3,000,000	
UT San Antonio	Engineering Building, Phase II	82,500,000	74,250,000	8,250,000			
UT Tyler	Completion/Reno./Exp. for Engineering, Sciences	48,000,000	43,200,000	4,800,000			
UT Tyler	Expansion of the UT Tyler Palestine Campus	7,000,000	6,300,000	700,000			
Academic TRB Total		640,975,000	566,276,000	60,250,000	11,449,000	3,000,000	
Other U. T. System Academic Projects							
UT Arlington	Engineering Research Building Expansion	30,000,000	-	27,000,000	3,000,000		
UT Austin	Welch Hall	60,000,000	-	35,000,000	25,000,000		
UT Dallas	Math, Science, and Engineering Teaching-Learning Center	27,000,000	-	24,300,000	2,700,000		
UT El Paso	Science and Engineering Core Facilities Upgrade	39,000,000	-	35,100,000	3,900,000		
UT San Antonio	Combined Science Facility Renovations - 1604 Campus	22,500,000	-	20,250,000	2,250,000		
UT Tyler	Braithwaite Building Addition	2,400,000	-	2,160,000	240,000		
Academic Other Total		180,900,000	-	143,810,000	37,090,000		
Total PUF Funding Allocable to U. T. System Academic Institutions				204,060,000			
U. T. System Health Institution Tuition Revenue Bond Projects							
UT SMC-Dallas	North Campus Phase 5	156,000,000	42,000,000	42,000,000	29,000,000	43,000,000	
UT MB Galveston	Galveston National Laboratory	167,090,673	57,000,000	-			110,090,673
UT HSC Houston	Dental Branch Replacement Building	80,000,000	60,000,000	18,000,000		2,000,000	
UT HSC San Antonio	South Texas Research Facility	150,000,000	60,000,000	40,000,000		50,000,000	
UT M. D. Anderson	Center for Targeted Therapy Research Building	70,000,000	40,000,000	30,000,000			
Health TRB Total		623,090,673	259,000,000	130,000,000	29,000,000	95,000,000	110,090,673
Other U. T. System Health Projects							
UT MB Galveston	Specialty Care Center at Victory Lakes	35,000,000		30,500,000	4,500,000		
UT HSC Houston	Biomedical Research and Education Facility	62,000,000		41,100,000		20,900,000	
UT HSC Houston	Research Replacement Facility	80,530,000	23,600,000 (1)	18,000,000 (1)		16,330,000	22,600,000
Health Other Total		177,530,000	23,600,000	89,600,000	4,500,000	37,230,000	22,600,000
Total PUF Funding Allocable to U. T. System Health Institutions				219,600,000			
Total U. T. System TRB and Other Project Considerations (2)		1,622,495,673	848,876,000	423,660,000	82,039,000	135,230,000	132,690,673

(1) The $23.6M of TRBs for UTHSCH's Research Replacement Facility are from the 78th Legislature
(2) The TRB total excludes $21.12 million allocated to UTHC Tyler for the Academic Health Center

Prepared by OFPC
July 20, 2006

Table 2
Request to Amend The University of Texas System
FY 2006-2011 Capital Improvement Program and FY 2006-2007 Capital Budget

Projects to be added to the FY 2006-2011 CIP and FY 2006-2007 Capital Budget

Institution	R&R or New Construction	Total Project Cost	TRB Authority	Proposed PUF Funding	RFS	Gifts
UT Arlington						
Engineering Research Building Expansion	R&R	30,000,000	-	27,000,000	3,000,000	
UT Austin						
Welch Hall	R&R	60,000,000	-	35,000,000	25,000,000	
UT Brownsville						
Science and Technology Learning Center	New	33,800,000	33,800,000	-		
UT Dallas						
Math, Science, and Engineering Teaching-Learning Center	New	27,000,000	-	24,300,000	2,700,000	
UT El Paso						
Physical Sciences / Engineering Core Facility	New	85,000,000	76,500,000	8,500,000		
Science and Engineering Core Facilities Upgrade	R&R	39,000,000	-	35,100,000	3,900,000	
UT Pan American						
Fine Arts Academic and Performance Complex	New	49,745,000	39,796,000	-	9,949,000	
Starr County Upper Level Center	New	7,500,000	6,000,000	-	1,500,000	
UT San Antonio						
Engineering Building, Phase II	New	82,500,000	74,250,000	8,250,000		
Combined Science Facility Renovations - 1604 Campus	R&R	22,500,000	-	20,250,000	2,250,000	
UT Tyler						
Braithwaite Building Addition	New	2,400,000	-	2,160,000	240,000	
UT SMC-Dallas						
North Campus Phase 5	New	156,000,000	42,000,000	42,000,000	29,000,000	43,000,000
UT HSC Houston						
Dental Branch Replacement Building	New	80,000,000	60,000,000	18,000,000		2,000,000
Biomedical Research and Education Facility	New	62,000,000	-	41,100,000		20,900,000
UT HSC San Antonio						
South Texas Research Facility	New	150,000,000	60,000,000	40,000,000		50,000,000
Totals		887,445,000	392,346,000	301,660,000	77,539,000	115,900,000

Prepared by OFPC
July 20, 2006

Request to Amend the University of Texas System
FY 2006-2011 Capital Improvement Program and FY 2006-2007 Capital Budget
Table 3

Existing CIP Projects to Receive Modified Funding and/or Revised Project Cost

				Existing Funding (In millions)						New Funding (In millions)					
Project Name	Existing TPC	Adds	New TPC	RFS	TRB	Ins. Clm.	Gifts	Grants	Hosp. Rev.	PUF	RFS	TRB	Ins. Clm.	Gifts	Grants
UT Arlington															
Engineering Research Building	80,430,000		80,430,000	10.00	70.43					10.00		70.43			
UT Austin															
Experimental Science Building	125,000,000		125,000,000	20.00	105.00					20.00		105.00			
UT Dallas															
Vivarium and Experimental Space	15,000,000		15,000,000	3.00	12.00					3.00		12.00			
UT Permian Basin															
Science and Technology Complex	56,000,000		56,000,000		54.00		2.00			2.00		54.00			
Arts, Convocation, & Classroom Facility - CEED	45,000,000	3,000,000	48,000,000		45.00					3.00		45.00			
UT Tyler															
Completion/Reno./Exp. for Engineering, Sciences	48,000,000		48,000,000	3.60	43.20		1.20			4.80		43.20			
Expansion of the UT Tyler Palestine Campus	7,000,000		7,000,000	0.70	6.30					0.70		6.30			
UT MB Galveston															
Galveston National Laboratory	167,090,673		167,090,673	40.00			17.00	110.09				57.00			110.09
Specialty Care Center at Victory Lakes	30,000,000	5,000,000	35,000,000	30.00						30.50	4.50				
UT HSC Houston															
Research Replacement Facility	80,530,000		80,530,000		23.60	16.60	34.33	6.00		18.00		23.60	16.60	16.33	6.00
UT M. D. Anderson															
Center for Targeted Therapy Research Building	70,000,000		70,000,000	35.00			25.00		10.00	30.00		40.00			
Totals	724,050,673	8,000,000	732,050,673	142.30	359.53	16.60	79.53	116.09	10.00	122.00	4.50	456.53	16.60	16.33	116.09

Prepared by OFPC
July 20, 2006

Request to Amend the University of Texas System
FY 2006-2011 Capital Improvement Program and FY 2006-2007 Capital Budget
Table 4

Repair & Rehabilitation Projects to be added to the FY 2006-2011 CIP and FY 2006-2007 Capital Budget

Institution	R&R or New Construction	Total Project Cost	Proposed PUF Funding	RFS
UT Arlington				
Engineering Research Building Expansion	R&R	30,000,000	27,000,000	3,000,000
UT Austin				
Welch Hall	R&R	60,000,000	35,000,000	25,000,000
UT El Paso				
Science and Engineering Core Facilities Upgrade	R&R	39,000,000	35,100,000	3,900,000
UT San Antonio				
Combined Science Facility Renovations - 1604 Campus	R&R	22,500,000	20,250,000	2,250,000
Totals		151,500,000	117,350,000	34,150,000

Prepared by OFPC
July 20, 2006

4. U. T. System: Approval of Permanent University Fund Bond Proceeds allocation for Library, Equipment, Repair and Rehabilitation Projects for fiscal year ending August 31, 2007

RECOMMENDATION

The Chancellor, with the concurrence of the Interim Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Business Affairs, and the Executive Vice Chancellor for Health Affairs, recommends that the Permanent University Fund (PUF) Bond Proceeds allocation for Library, Equipment, Repair and Rehabilitation (LERR) for the fiscal year ending August 31, 2007, be approved.

It is requested that PUF Bond Proceeds in the amount of $66,855,000 be appropriated to the institutions to fund LERR Projects for Fiscal Year 2007. Of the $66,855,000, it is requested that $30,000,000 be appropriated directly to U. T. System institutions. This would authorize the purchase of approved equipment items and library materials and to contract for repair and rehabilitation projects following standard purchasing and contracting procedures within approved dollar limits. Substitute equipment purchases or repair and rehabilitation projects are to receive prior approval by the Chancellor, the appropriate Executive Vice Chancellor and, where required, the U. T. System Board of Regents. Transfers by U. T. System Administration of allocated funds to institutional control or to vendors will coincide with vendor payment requirements. Final approval of specific repair and rehabilitation projects will be in accordance with procedures for construction projects established by the U. T. System Board of Regents.

It is also requested that $20,000,000 of PUF Bond Proceeds be appropriated to provide additional funding to build and enhance research infrastructure to attract and retain the best qualified faculty known as the Science and Technology Acquisition and Retention (STARs) Program. Through a competitive proposal process determined by U. T. System Administration, funds will be distributed for the purpose of recruiting top researchers.

The remaining $16,855,000 requested is for U. T. System Administration to provide additional funding for the Shared Services Initiative ($11,900,000), Network Telecommunications upgrade ($3,160,000), Oracle Infrastructure Licensing update ($1,045,000), and Network Operations Center infrastructure ($750,000). These four additional requests will benefit all U. T. System institutions by providing the investment needed for capital improvement at the Shared Services Center, software and hardware purchases, and equipment to increase network infrastructure used in supporting all U. T. System institutions.

It is further recommended that LERR appropriations not expended or obligated by contract or purchase order within six months after the close of Fiscal Year 2007 are to be available for future System-wide reallocation unless specific authorization to continue obligating the funds is given by the appropriate Executive Vice Chancellor upon recommendation of the president of the institution.

BACKGROUND INFORMATION

A supplemental volume of the budget materials titled "Operating Budget Summaries and Reserve Allocations for Library, Equipment, Repair and Rehabilitation" is enclosed in the front pocket of this Agenda Book.

The appropriation of PUF Bond Proceeds will be presented in the Fiscal Year 2007 LERR Budget. The allocation of these LERR funds to the U. T. System institutions was developed from prioritized lists of projects submitted by the institutions and reviewed by U. T. System Administration staff.

As required by the Available University Fund (AUF) Spending Policy, a forecast of revenues and expenses of the AUF for seven years, including the above allocation has been prepared and is provided on Page 10. The additional appropriation of PUF Bond Proceeds for this allocation is within the policy as shown in the forecast.

Available University Fund Forecast
Actual and Forecast Data

	Actual	Estimated	Budget	Forecast				
AVAILABLE UNIVERSITY FUND	**FYE 05**	**FYE 06**	**FYE 07**	**FYE 08**	**FYE 09**	**FYE 10**	**FYE 11**	**FYE 12**
PUF Distributions	$ 341,174,270	$ 357,337,255	$ 400,685,603	$ 445,422,757	$ 485,511,898	$ 518,351,704	$ 546,003,376	$ 573,088,423
Surface & Other Income	8,332,900	9,087,000	8,274,500	8,274,500	8,299,500	8,324,500	8,349,500	8,374,500
Divisible Income	349,507,170	366,424,255	408,960,103	453,697,257	493,811,398	526,676,204	554,352,876	581,462,923
U. T. System Share (2/3)	233,004,781	244,282,837	272,640,069	302,464,838	329,207,599	351,117,469	369,568,584	387,641,949
AUF Interest Income	5,106,927	8,686,000	8,468,125	7,521,000	7,471,000	6,942,000	6,294,000	6,280,000
Income Available to UT	238,111,708	252,968,837	281,108,194	309,985,838	336,678,599	358,059,469	375,862,584	393,921,949
U. T. Net Divisible Income	238,111,708	252,968,837	281,108,194	309,985,838	336,678,599	358,059,469	375,862,584	393,921,949
TRANSFERS:								
PUF Debt Service	(79,996,795)	(90,460,000)	(96,197,102)	(100,476,083)	(100,328,420)	(100,765,072)	(66,604,922)	(66,600,622)
Additional PUF Debt Service	-	-	(10,324,271)	(41,474,835)	(62,479,630)	(83,663,673)	(105,027,706)	(113,188,601)
System Administration	(28,377,614)	(29,695,141)	(32,001,334)	(33,281,387)	(34,612,643)	(35,997,149)	(37,437,035)	(38,934,516)
IT Network Bandwidth/Office of Telecommunication Services	(1,060,000)	(1,060,000)	(1,060,000)	(1,060,000)	(1,060,000)	(1,060,000)	(1,060,000)	(1,060,000)
Support and Maintenance of U. T. Austin	(105,275,000)	(111,420,000)	(126,500,000)	(139,495,000)	(151,510,000)	(161,130,000)	(169,140,000)	(177,265,000)
Net Surplus/(Deficit)	**23,402,299**	**20,333,696**	**15,025,487**	**(5,801,467)**	**(13,312,093)**	**(24,556,424)**	**(3,407,078)**	**(3,126,790)**

5. **U. T. System: Approval of the nonpersonnel aspects of the operating budgets for the fiscal year ending August 31, 2007**

RECOMMENDATION

The Chancellor, with the concurrence of the Interim Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Business Affairs, the Executive Vice Chancellor for Health Affairs, and the presidents of the U. T. System institutions, recommends that the nonpersonnel aspects of the U. T. System Operating Budgets for the fiscal year ending August 31, 2007, including Auxiliary Enterprises, Grants and Contracts, Designated Funds, Restricted Current Funds, and Medical and Dental Services, Research and Development Plans, be approved.

It is further recommended that the Chancellor be authorized to make editorial corrections therein and that subsequent adjustments be reported to the U. T. System Board of Regents through the docket.

BACKGROUND INFORMATION

A supplemental volume of the budget materials titled "Operating Budget Summaries and Reserve Allocations for Library, Equipment, Repair and Rehabilitation" is enclosed in the front pocket of this Agenda Book.

The Chancellor's PowerPoint on the operating budget is being prepared and is not included in the Agenda materials.

See the Executive Session item related to the personnel aspects of the U. T. System Operating Budgets (Item 4 on Table of Contents Pages i - ii for Meeting of the Board).

6. **U. T. System Board of Regents: Proposed appointment of George Willeford III, M.D., as Regental Representative to U. T. Austin Intercollegiate Athletics Council for Men and appointment of Dr. Susan C. Blackwood and reappointment of Mrs. Sylvie P. Crum as Regental Representatives to Intercollegiate Athletics Council for Women effective September 1, 2006**

RECOMMENDATION

Chairman Huffines, with the concurrence of Chancellor Yudof and President Powers, recommends the following appointments as Regental representatives to the U. T. Austin

Intercollegiate Athletics Council for Men and the Intercollegiate Athletics Council for Women each for a four-year term beginning September 1, 2006:

a. Appoint George Willeford III, M.D., to replace Mr. Jeffrey M. Heller on the Intercollegiate Athletics Council for Men

b. Appoint Dr. Susan C. Blackwood to replace George Willeford III, M.D., and serve the remainder of his term until August 31, 2009, on the Intercollegiate Athletics Council for Women

c. Reappoint Mrs. Sylvie P. Crum on the Intercollegiate Athletics Council for Women.

BACKGROUND INFORMATION

The U. T. Austin Intercollegiate Athletics Council for Men is a nine member advisory group composed of a student, an ex-student, two Regental appointees, and five members of the University General Faculty. The Regental appointments are for four-year staggered terms. Mr. Jeffrey M. Heller was appointed to the Council on August 8, 2002, to serve through August 31, 2006.

Dr. George Willeford would be appointed to replace Mr. Heller and serve a term through August 31, 2010. Dr. Willeford is a gastroenterologist in private practice in Austin and a graduate of U. T. Austin and U. T. Southwestern Medical School - Dallas. Dr. Willeford's appointment will leave a vacancy on the Intercollegiate Athletics Council for Women.

The U. T. Austin Intercollegiate Athletics Council for Women is composed of nine voting members and one nonvoting member as follows: two students (one nonvoting), an ex-student, two Regental appointees, and five members of the University General Faculty. The Regental appointments are for four-year staggered terms. Dr. Willeford was appointed to the Council in August 1996, reappointed in May 2000, and again in July 2005 to serve a term to expire on August 31, 2009. Mrs. Sylvie P. Crum was appointed to the Council on August 8, 2002, to serve through August 31, 2006.

Dr. Susan C. Blackwood is Executive Director of the San Antonio Sports Foundation and Adjunct Professor at the Incarnate Word University. She was Associate Director of Athletics at U. T. Austin from 1990-1994, has worked in the private sector with Oshman’s Sporting Goods, and as Assistant Commissioner for the Southwest Athletic Conference and Assistant Athletics Director for the University Interscholastic League (UIL). Dr. Blackwood has worked closely with the U.S. Olympic Committee and the NCAA and is working in the San Antonio community on a program to involve young girls in more active lifestyles. Dr. Blackwood holds bachelor’s, master’s, and doctoral degrees from the University of Nebraska.

Mrs. Crum, a well-respected community leader, received a B.A. in Liberal Arts/Romance Languages in 1974 from U. T. Austin. She is an active supporter of the women's athletic program, establishing an endowed scholarship in women's volleyball.

Mr. R. Steven Hicks was appointed to the Intercollegiate Athletics Council for Men on July 8, 2005, for a term to expire August 31, 2009.

7. U. T. System Board of Regents: Amendment to the Regents' *Rules and Regulations*, Series 10401, related to meetings of the Board and Standing Committees to add a new Section 6 related to accessibility

RECOMMENDATION

The Chancellor concurs in the recommendation of the Counsel and Secretary to the Board and the Vice Chancellor and General Counsel that the Regents' *Rules and Regulations*, Series 10401 be amended to add Section 6 related to accessibility to Board meetings as follows in congressional style:

Sec. 6 Accessibility to Board meetings. People with disabilities interested in witnessing committee and/or Board meetings and requiring communication or other special accommodations should contact the Office of the Board of Regents.

BACKGROUND INFORMATION

The proposed amendment to the Regents' *Rules and Regulations*, Series 10401, is needed to ensure compliance with HB 2819, codified as *Texas Government Code* Section 2054.451 *et seq.* and Rule 206.70(1)(b) of the Department of Information Resources that takes effect September 1, 2006, related to accessibility to allow participation in public meetings. Under the new rule, institutions of higher education must provide accommodations related to an open meeting in accordance with Sections 2054.456 and 2054.457 of the *Texas Government Code*. These sections require State agencies to provide persons with disabilities comparable access and use to electronic and other information resources as is available to persons without disabilities unless doing so would impose significant difficulty or expense.

8. U. T. System Board of Regents: Amendments to the Regents' *Rules and Regulations*, Series 20202 (Presidential Cash Compensation) including retitling as Cash Compensation for Chief Administrative Officers

RECOMMENDATION

It is recommended that the Regents' *Rules and Regulations*, Series 20202 (Presidential Cash Compensation), be retitled as Cash Compensation for Chief Administrative Officers and be amended as set forth in congressional style on Pages 15 - 20.

BACKGROUND INFORMATION

Proposed changes to the Presidential Cash Compensation Policy, originally approved by the Board on August 7, 2003, are intended to provide clear guidance concerning the permissible elements of cash compensation for the institutional presidents and the Chancellor.

The proposed revisions remove the option of contracted use of university housekeeping staff in personal residences and discontinue the payment of a separately identified salary supplement provided as a substitute for a housing allowance. The revisions specifically authorize the payment of one-time merit pay when appropriate and provide that all elements of compensation for service as a chief administrative officer are subject to the guidelines and approval process outlined in the Regents' *Rules*.

The proposed revisions have been reviewed by the Chancellor, the Interim Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Business Affairs, the Executive Vice Chancellor for Health Affairs, the Vice Chancellor for Administration, the Vice Chancellor and General Counsel, the Counsel and Secretary to the Board, and the Associate Vice Chancellor - Controller and Chief Budget Officer and coordinate with proposed amendments to Series 20101, related to duties of the Chancellor (see Page 24), and Series 20203, related to compensation for key executives (see Page 21) and will include a definition of “Chief Administrative Officer” that covers the positions of Chancellor and President. Following action on these recommendations, the Counsel and Secretary will work with other staff members to integrate these policies into a single compensation policy to the extent possible.

1. Title

~~Presidential~~ Cash Compensation for Chief Administrative Officers

2. Rule and Regulation

Sec. 1 Purpose. This Rule sets forth the cash compensation structure authorized for the Chancellor and presidents (chief administrative officers) of the institutions of The University of Texas System. It is prospective in nature and application and is not intended to be applied retroactively. It does not pertain to, nor affect, benefit programs such as insurance, retirement benefits, and deferred compensation, which may also be a part of a chief administrative officer's ~~president's~~ overall compensation package.

Sec. 2 Elements of Compensation Structure. In order to attract and to retain effective, highly skilled and committed chief administrative officers ~~presidents~~ of the institutions of the U. T. System and to recognize their professional achievements, it is the policy of the U. T. System to offer competitive levels of cash compensation within a compensation structure consistently ~~that is~~ applied ~~consistently~~. This Policy establishes and defines the various elements for the cash compensation portion of a chief administrative officer's ~~the presidential~~ compensation package. Compensation packages for the presidents are recommended by the appropriate Executive Vice Chancellor to the Chancellor, and then by the Chancellor to the Board of Regents for approval. The compensation package for the Chancellor is determined by the Board of Regents and will address issues related to residence at Bauer House.

2.1 Base Salary. The base salary rate for each chief administrative officer ~~president~~ shall be set by the U. T. System Board of Regents following ~~based on a~~ review of ~~state and~~ national compensation survey data for respective peer institutions. ~~Comparable salaries are reported in surveys by the College and University Personnel Association and other nationally recognized organizations. These surveys typically exclude allowances such as car, housing, and housekeeping, and retirement plans and other fringe benefits.~~

2.2 Housekeeping Staff. ~~Each president, at his or her option, may privately employ a housekeeper, in which event the~~

~~president shall be responsible for the tax-related implications and expenses associated with the employment of the housekeeper, or the president may elect to use the services of the institution's housekeeping staff, in which event the president shall reimburse the institution for the salary and benefits associated with that use.~~ Each institution, at the institution's expense, shall provide appropriate housekeeping and other support services for business-related functions held at the chief administrative officer's ~~president's~~ residence, but no housekeeping or other support services will be provided for personal use at a residence that is not owned by the University.

2.3 Practice Plan Supplement. The bylaws of the physician practice plans provide that the compensation for the presidents of the health institutions may be supplemented by up to 30% of the president's salary from practice plan funds. The supplement is contingent on availability of funds in the practice plan. ~~Practice plan supplements are included in national surveys of chief executive compensation.~~ The practice plan salary supplement is not a part of the base salary and shall be reported as a separate element of the health president's cash compensation because of the special nature of the source of funding. Practice plan supplements are not eligible for Teacher Retirement System and Optional Retirement Program retirement benefits or other retirement benefits and no employer matching contributions may be made with respect to practice plan supplements.

2.4 ~~Salary Supplement. The salary supplement shall be paid in lieu of a housing allowance to all presidents, including those who are provided a residence owned by the U. T. System. It is intended to cover the hypothetical cost of a model residence, as described below. The salary supplement shall be eligible for retirement benefits but is not a part of the base salary.~~

~~(a) The amount of the salary supplement shall be calculated by determining the fair market rental value of a standardized model residence containing 4,100 square feet of improvements and located where the president owns or leases his or her personal~~

~~residence. In the case of a president who is provided a residence owned by the U. T. System, the 4,100 square foot model residence shall be valued as if situated where the institutionally-owned residence is located.~~

~~(b) When a new president takes office, he or she shall initially receive a salary supplement equal to the most recent fair market rental value determined for the location of his or her predecessor's residence until such time as he or she obtains permanent housing. It is anticipated that the new president will obtain permanent housing within one year of hire date. If, after one year, the president has not obtained permanent housing, the value of the salary supplement shall be calculated based on the fair market rental value of the 4,100 square foot model residence located at the president's current residence location.~~

~~(c) In no event may the amount of the salary supplement exceed the fair market rental value of the 4,100 square foot model residence calculated at the location of the Bauer House (the official residence of the U. T. System Chancellor).~~

Deferred Compensation. Upon approval by the Board, deferred compensation may be paid pursuant to a Deferred Compensation Plan originally adopted effective September 1, 1996, for the benefit of a select group of employees. The purpose of the plan is to offer those employees an opportunity to elect to defer the receipt of compensation pursuant to Section 457(f) of the Internal Revenue Code of 1987, as amended. Deferred compensation is not part of the base salary and shall be reported as a separate element of the chief administrative officer's cash compensation. Deferred compensation is not eligible for Teacher Retirement System and Optional Retirement Program retirement benefits or other retirement benefits.

2.5 One-time Merit Awards. In instances where a chief administrative officer has made a significant contribution in a particular year, the Board of Regents may elect to make a merit award on an annual basis. Merit awards are not eligible for Teacher Retirement System and Optional Retirement Program retirement benefits or other retirement benefits.

Sec. 3 Prohibited Allowances or Adjustments. No allowances or adjustments will be provided for the following items:

3.1 Housing Allowance. No separate allowance for housing may be paid. Base salary includes compensation sufficient to purchase or lease a residence.

3.2 Housing Maintenance Allowance. ~~(d)~~ No separate allowance for maintenance, utilities, landscaping, or other expenses attributable to a chief administrative officer's personal ~~the president's~~ residence may be paid. All personal expenses associated with a chief administrative officer's personal ~~president's~~ residence are intended to be covered by the base salary ~~supplement~~. No University physical plant personnel may be used to provide personal services related to repair or maintenance at a residence that is not owned by the University.

3.3 Car Allowance. No separate car allowance may be provided to a chief administrative officer. Base salary includes compensation sufficient to purchase or lease a car. An institution may reimburse a chief administrative officer for mileage associated with business use of a personal vehicle in accordance with the latest published Internal Revenue Service guidelines, the State Travel Regulations Act (*Texas Government Code* Chapter 660) and applicable institutional policies. No vehicle may be purchased for or assigned to the chief administrative officer for personal use.

Sec. 4 Other Compensation. This rule covers all compensation provided for service as a chief administrative officer by the institution or an external organization that is established to support the mission of the institution. Compensation for other service, such as service on outside boards must be pursuant to approval required by the System-wide policy titled *Service on Outside Boards*.

Sec. 5 University-Owned Housing. ~~(e.) Except as provided in the following sentence, each president of an institution for which a~~

~~residence owned by the U. T. System is available shall have the option of leasing from the U. T. System the institutionally-owned residence or acquiring a personal residence~~. If~~, however,~~ the Board of Regents makes arrangements that require ~~with~~ the chief administrative officer ~~president that require the president~~ to reside in the institutionally-owned residence or if covenants, conditions, or restrictions applicable to the institutionally-owned residence require occupancy by the chief administrative officer ~~president~~, then he or she ~~the president~~ shall reside in the institutionally-owned residence. In the absence of such requirements, each chief administrative officer of an institution, for which a residence is owned by the U. T. System and is available, shall have the option of leasing the residence from the U. T. System.

5.1 ~~(f.)~~ Those presidents who ~~either~~ elect to or are required~~, as provided in Section 2.4(e) above,~~ to reside in an institutionally-owned residence shall enter into a lease arrangement ~~of the residence~~ with the U. T. System. The rental rate to be paid by the president under the lease shall be based on the current fair market rental value of that portion of the residence that is used as the president's private residence.

~~2.5 No Car Allowance. No separate car allowance may be provided to presidents of the institutions. An institution may reimburse a president for business use of the president's personal vehicle in accordance with the latest published Internal Revenue Service guidelines, the State Travel Regulations Act (*Texas Government Code* Chapter 660) and applicable institutional policies.~~

~~2.6 Institutionally Provided Property and Services. Institutionally-provided property and services, such as club memberships, shall not be considered elements of a president's cash compensation. Such property and services shall be subject to appropriate authorization and approval and monitoring of personal use and business use.~~

~~(a) No tax equity adjustments may be paid to a president. Tax equity adjustments are cash compensation to the president for the federal income tax consequences to the president arising out of the president's personal use of institutionally-provided~~

~~property or services. Rather, each president shall reimburse the institution for his or her personal use of institutionally-provided property and services at appropriate rates as determined by the institution in accordance with Internal Revenue Service guidelines and applicable institutional policies.~~

~~Sec. 3 Authority. The statutory authority for this Rule is provided by *Texas Education Code* Section 65.31, General Powers and Duties.~~

9. **U. T. System Board of Regents: Amendments to the Regents' *Rules and Regulations*, Series 20203 (Compensation for Key Executives)**

RECOMMENDATION

The Chancellor concurs in the recommendation of the Interim Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Business Affairs, the Executive Vice Chancellor for Health Affairs, the Vice Chancellor and General Counsel, the Counsel and Secretary to the Board, and the Vice Chancellor - Controller and Chief Budget Officer that the Regents' *Rules and Regulations*, Series 20203, regarding compensation for key executives, be amended as set forth in congressional style on Pages 22 - 23.

BACKGROUND INFORMATION

The proposed clarifying amendments to the Regents' *Rules and Regulations* mention optional additional elements of compensation to facilitate recruitment of individuals and delete an unneeded reference to vehicle allowances. The proposed revisions coordinate with proposed amendments to Series 20101, related to duties of the Chancellor (see Page 24), and Series 20202, related to cash compensation for chief administrative officers (see Page 14).

1. Title

Compensation for Key Executives

2. Rule and Regulation

Sec. 1 Compensation Philosophy. To attract, retain and motivate the top talent needed to lead The University of Texas System and accomplish its mission, and to recognize and reward performance, the Board of Regents seeks to compensate key executives at levels that are competitive in the marketplace, cost effective, and, to the extent possible, internally equitable.

Sec. 2 Market Review. To align executive compensation with the relevant market, the Office of the Board of Regents will oversee the conduct of a comprehensive survey and analysis to obtain current and reliable market data on total compensation of key executives in comparable positions at peer institutions. Market data will be adjusted using cost of living information related to respondent's geographic region. The survey will be conducted every three years. In non-survey years, the Office of the Board of Regents will obtain information concerning general changes in executive compensation in the marketplace, and the comprehensive survey will be adjusted accordingly.

Sec. 3 Elements of Compensation. The elements of compensation may include and are limited to base salary; short and long-term incentive pay; supplemental retirement plans, such as deferred compensation plans; one-time merit pay; special provisions necessary to recruit an individual to a key executive position, such as salary supplement for a limited time or a one-time relocation payment as necessary and prudent to recruit the top talent for the position; and perquisites such as ~~housing, vehicle allowance, and~~ memberships, parking privileges, and provision of or allowance for cell phone and/or other mobile communications devices as determined necessary for business purposes and as covered in individual agreements. Key executives must promptly reimburse the institution for any personal use of a membership provided by the institution. All compensation set pursuant to this Rule must comply with all applicable state and federal laws and must be approved and documented in budget summaries. All compensation for service as a key executive is covered by this Series. Elements of compensation paid on behalf of a chief administrative officer must be disclosed in the annual report of expenses required by Series 20205.

Sec. 4 Peer Institutions. Peer institutions or groups of institutions will be selected through an interactive, consultative process between the Chancellor, Executive Vice Chancellors, presidents and the organization engaged to conduct the comprehensive survey. To the extent possible, the same institutions will be surveyed during each comprehensive survey. Peer institutions may be changed based on sound business decisions; such changes will be fully disclosed to the Board of Regents. The Executive Vice Chancellors will maintain the list of peer institutions. Factors to consider in selecting peer institutions include size, purpose, institutions used in assessing ~~accessing~~ U. T. System performance and those from which U. T. System competes for key executives.

Sec. 5 Approval by ~~Presentation to~~ Board of Regents. All proposed elements of compensation, including taxable and nontaxable items, ~~Compensation data~~ will be presented to the Board of Regents for approval in advance of the annual budgeting process. ~~Taxable and non-taxable elements of compensation will be reported to the Board of Regents.~~

Sec. 6 Determining Compensation. In setting a key executive's initial compensation, the following factors should be considered: relevant market data, current compensation, cost of living differences, internal equity and the U. T. System budget. Where appropriate, U. T. System may target the 75th percentile of the market rate of a key executive's peer institutions.

Factors to consider in making future adjustments to a key executive's compensation include market data, key executive performance, the institution's progress on key performance indicators, internal equity, and the U. T. System budget.

Sec. 7 The presidents will implement appropriate policies and procedures concerning executive compensation for the direct reports at each U. T. System academic and health institution.

10. U. T. System Board of Regents: Amendment to the Regents' *Rules and Regulations*, Series 20101, Sections 3.4 and 3.9 related to appointment of officers by the Chancellor

RECOMMENDATION

It is recommended that the Regents' *Rules and Regulations*, Series 20101, Sections 3.4 and 3.9 related to appointment of officers by the Chancellor, be amended as set forth in congressional style on Pages 25 - 27.

BACKGROUND INFORMATION

The proposed revisions to the Regents' *Rules and Regulations* delete an outdated reference to nominations by the Chancellor and include specific authorization for payment of supplemental salary to individuals assuming additional duties. The proposed revisions coordinate with proposed amendments to Series 20203, related to compensation for key executives (see Page 21), and Series 20202, related to cash compensation for chief administrative officers (see Page 14).

The proposed revisions have been reviewed by the Vice Chancellor and General Counsel and the Counsel and Secretary to the Board of Regents.

1. Title

Chancellor

2. Rule and Regulation

Sec. 1 Role. The Chancellor is the chief executive officer of The University of Texas System. The Chancellor reports to and is responsible to the Board of Regents. The Chancellor heads the System Administration, which is used by the Board to exercise its powers and authorities in the governance of the U. T. System. The Chancellor has direct line responsibility for all aspects of the U. T. System's operations.

Sec. 2 Appointment. The Chancellor shall be elected by the affirmative vote of a majority of the Regents in office and shall hold office without fixed term, subject to the pleasure of the Board.

Sec. 3 Primary Duties and Responsibilities. The Chancellor, by delegation from the Board of Regents, is authorized to exercise the powers and authorities of the Board in the governance of the U. T. System. The Chancellor will normally act through the officers of the U. T. System regarding the matters delegated to them by the Regents' *Rules and Regulations*. The Chancellor, however, shall not be precluded from any direct participation and communication with System Administration officers or staff, institutional officers or staff, faculty members, and groups. The major duties of the Chancellor include:

3.1 Counseling, Implementing, and Representing. Counseling the Board with respect to the policies, purposes, and goals of the System; acting as executive agent of the Board in implementing Board policies, purposes, and goals and a system of internal controls; representing the U. T. System in all other respects as deemed appropriate to carry out such policies, purposes, and goals, and interpreting and articulating the U. T. System's academic, administrative, and developmental policies, programs, needs, and concerns to the general public and to other constituencies at the community, state, regional, and national levels.

3.2 Strategic Planning. Preparing a strategic plan for the U. T. System for recommendation to the Board of Regents in consultation with the institutional presidents.

The proposed plan should include periodic adjustments to the mission statement; assessments of the internal and external environment; and recommendations for U. T. System goals, priorities, and benchmarks of progress in academic programs, service, capital expenditures, and the allocation of financial resources.

3.3 Directing. Directing the management and administration of System Administration and all institutions of the U. T. System.

~~3.4 Nominating. Presenting nominations to the appropriate standing committees of the Board of Regents and to the Board for all officers of the U. T. System as provided in the Regents' *Rules and Regulations*.~~

3.4~~5~~ Organizing. Reviewing periodically the organization of the System Administration and the institutions of the U. T. System and reporting to the appropriate standing committees of the Board of Regents and to the Board recommendations for changes in organization, assignments, and procedures.

3.5~~6~~ Preparing and Approving Recommendations. Preparing and approving appropriate recommendations to the Board of Regents and standing committees of the Board along with the appropriate Executive Vice Chancellor, Vice Chancellor, or president of an institution.

3.6~~7~~ Budgeting. Preparing and approving annual operating budgets for the System Administration and the institutions of the U. T. System and submitting recommendations to the Board of Regents.

3.7~~8~~ Preparing Legislative Submissions. Preparing and approving biennial legislative submissions to the Legislative Budget Board and to the Governor for the System Administration and the institutions of the U. T. System for the consideration of the Board of Regents in accordance with Series 20501 of the Regents' *Rules and Regulations*.

3.8~~9~~ Fund Development. Serving as the chief executive officer for fund development and as the agent of the Board of Regents for the discharge of development responsibilities. Defining for the Board, at periodic intervals, descriptions of current and future needs, as determined by the presidents and System Administration, taking into account recommendations from institutions development boards.

3.9~~10~~ Appointment of Officers. Appointing the Executive Vice Chancellors and Vice Chancellors and taking administrative action and terminating employment regarding these positions. In making such appointments, the Chancellor shall adhere to the Board's policy on the compensation of key executives as outlined in Series 20203 of these *Rules and Regulations*. The Chancellor may also approve the payment of reasonable supplemental salary for an individual assuming additional duties including those of an interim appointment.

3.10~~1~~ Nominating Director of Audits. Nominating candidates for the position of System Director of Audits for appointment by the Board of Regents, as outlined in Series 20401 of these *Rules and Regulations*.

3.11~~2~~ Nominating Compliance Officer. Appointing the System-wide Compliance Officer, as outlined in Series 20401 of these *Rules and Regulations*.

3.12~~3~~ Oversight of UTIMCO. Serving on the Board of Directors of The University of Texas Investment Management Company (UTIMCO). Generally overseeing the operations of UTIMCO and coordinating interaction between the U. T. System and UTIMCO. Ensuring that UTIMCO implements the core investment functions delegated by the Board of Regents in conformance with the Regents' *Rules and Regulations*, the Investment Management Services Agreement, and the Investment Policy Statements adopted by the Board. Directing UTIMCO in areas other than core investment functions such as relations with the media, intergovernmental relations, and public disclosure issues. Recommending to the Board of Regents, in its fiduciary role, an effective oversight system for the proper management of UTIMCO, including, but not limited to clear procedures for the selection of UTIMCO directors; process for budget review; and periodic review of the Investment Management Services Agreement.

11. U. T. System Board of Regents: Amendment to the Regents' *Rules and Regulations*, Series 20201, Section 4.9 concerning the role of faculty, staff, and student governance groups, as appropriate, in the development of an institution's operating procedures

RECOMMENDATION

The Chancellor concurs in the recommendation of the Interim Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Health Affairs, and the Vice Chancellor and General Counsel that the Regents' *Rules and Regulations*, Series 20201, Section 4.9 concerning the role of faculty, staff, and student governance groups, as appropriate, in the development of an institution's operating procedures, be amended as follows in congressional style:

Sec. 4 Duties and Responsibilities. Within the policies and regulations of the Board of Regents and under the supervision and direction of the appropriate Executive Vice Chancellor, the president has general authority and responsibility for the administration of that institution. Specifically, the president is expected, with the appropriate participation of the staff, to:

. . .

4.9 Cause to be prepared and submitted to the appropriate Executive Vice Chancellor and the Vice Chancellor and General Counsel for approval, the rules and regulations for the governance of the institution and any related amendments. Such rules and regulations shall constitute the *Handbook of Operating Procedures* for that institution. Any rule or regulation in the institutional *Handbook of Operating Procedures* that is in conflict with any rule or regulation in the Regents' *Rules and Regulations*, is null and void and has no effect. <u>Input from the faculty, staff, and student governance bodies for the institution will be sought for all significant changes to an institution's *Handbook of Operating Procedures*.</u>

. . . .

The proposed Rule will direct the president to consult the faculty, staff, and student governing groups on changes to the Handbook of Operating Procedures (HOP) that affect them in general.

BACKGROUND INFORMATION

The Faculty Advisory Council recommended that Section 4.9 of the Regents' *Rules and Regulations*, Series 20201, be clarified concerning the role of faculty governing groups in the development of and participation in the HOP policies affecting these groups. The Office of Academic Affairs has been working with the Faculty Advisory Council to clarify duties and responsibilities of academic presidents and recommends the revised Rule to cover staff and student groups as well. Drafts of this proposed Rule were reviewed by members of the Faculty Advisory Council, presidents, and U. T. System administrators.

12. U. T. System Board of Regents: Amendment of the Regents' *Rules and Regulations*, Series 60301 related to the development boards; Series 60302 related to advisory councils; and deletion of Series 60303 related to internal foundations

RECOMMENDATION

The Chancellor concurs in the recommendation of the Interim Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Health Affairs, the Vice Chancellor for External Relations, and the Vice Chancellor and General Counsel that the Regents' *Rules and Regulations* be amended as set forth in congressional style as follows:

a. Series 60301, related to the development board of an institution, be amended as set forth on Pages 31 - 34;

b. Series 60302, related to advisory councils of an institution be amended as set forth on Pages 35 - 38; and

c. Series 60303, related to internal foundations of an institution, as set forth on Pages 39 - 43 be deleted.

BACKGROUND INFORMATION

In a joint effort, the Office of the Board of Regents, the Office of External Relations, and the Office of General Counsel have suggested revisions to the Regents' *Rules* regarding development boards and advisory councils. The revisions are designed to enhance each institution's ability to direct the activities of these entities while maintaining appropriate oversight by U. T. System Administration and the Board of Regents. These new Rules are structured to work in conjunction with a set of model bylaws that will function to allow System-wide consistency in the governance of these entities. The proposed Rules also incorporate any existing internal foundations into an institution's development board or an appropriate advisory council, thereby eliminating the need for a separate Rule concerning internal foundations.

Drafts of these proposed Rules were made available for review by the presidents and chief development officers at all institutions and, as presented, incorporate input from the institutions as well as various U. T. System offices.

1. Title

Development Board of an Institution

2. Rule and Regulation

Sec. 1 Authorization. With the approval of the president of an institution, the Vice Chancellor for External Relations, the appropriate Executive Vice Chancellor, the Chancellor, and the Board of Regents, ~~any~~ each institution may have a development board dedicated to its own unique interests. ~~Each institution development board shall work with the institution's president and the chief development officer to determine its role in seeking private support.~~

Sec. 2 Purpose. An institution's development board shall serve an institution of the U. T. System by assisting in the development plans and programs of the institution with an emphasis on increasing private support.

Sec. 3~~2~~ Composition ~~of Institution Development Board~~. ~~The~~ Unless otherwise excepted, the institution's development board shall consist of members recommended and appointed by the president of the institution ~~with final review and approval of the membership delegated by the Board of Regents to the Chancellor following consultation with the Executive Vice Chancellor for Health Affairs or the Executive Vice Chancellor for Academic Affairs and the Vice Chancellor for External Relations~~. Presidents of institutions shall adopt guidelines for the appointment ~~and/or reappointment~~ of the members of the institution's development board. The guidelines shall make clear each individual's term of office and the expectations and responsibilities of membership. Consideration shall be directed to appropriate balance in board membership, including ~~concerns relating to~~ gender, ethnicity, range of experience, geographical distribution, and the special needs of the institution and the ~~board. Institutions shall forward an accurate roster of~~ development board ~~membership to the Chancellor via the Vice Chancellor for External Relations annually~~. All terms shall officially begin on September 1. ~~Official rosters of board membership shall be maintained in the Office of the Vice Chancellor for External Relations.~~ The president of the institution ~~and the Chancellor (or his or her delegate)~~ shall be an ex officio member~~s~~ with voting privileges. ~~The institution~~

~~development board will elect a Chairman and such other officers as are appropriate from among its membership.~~

~~Sec. 3 General Policies. The following are general policies for institution development boards:~~

~~3.1 An institution development board shall serve the individual institution of the U. T. System by assisting in the plans and programs of that institution with consideration of development interests of all institutions in the U. T. System.~~

~~3.2 An institution development board will work closely with the internal foundations of the institution. No internal foundations shall be established or continued in existence except with the approval of the Vice Chancellor for External Relations, the appropriate Executive Vice Chancellor, the Chancellor, and the Board of Regents. The president of each institution shall be responsible for and have authority over the institution development board and internal foundations of the institution he or she heads.~~

Sec. 4 Governance and Bylaws. Consistent with the Regents' *Rules and Regulations*, the president of each institution shall be responsible for and have authority over the institution's development board. The institution's president may appoint from the development board's membership a chair and such other officers as appropriate or may choose to allow the membership to elect such officers.

4.1 Model Bylaws. Subject to the approval of the president of the institution, each development board shall adopt bylaws for its internal governance that are consistent with this Series and that substantially comply with model bylaws developed by the Office of General Counsel.

Sec. 5 Reporting Rosters and Expenses. Institutions shall annually forward an accurate roster of the development board membership to the Vice Chancellor for External Relations on a designated date. In addition, each institution shall maintain specifically identifiable accounts that document any development board related revenues and expenses out of the president's office or other offices that support development board activities. These accounts must be identifiable in an institution's annual operating budget.

Sec. 6 Role of Internal Foundations. As used in this Series, the term "internal foundation" means an entity created by resolution of the Board of Regents of The University of Texas System for certain development purposes. An internal foundation is part of the organizational structure of either a development board or an advisory council and functions as an administrative and accounting mechanism that is employed to approach prospective donors. Internal foundations are not encouraged and shall not be established or maintained except with the approval of the president of the institution, the Vice Chancellor for External Relations, the appropriate Executive Vice Chancellor, the Chancellor, and the Board of Regents.

Sec. 7~~4~~ ~~Special~~ Campaigns.

7.1 Special Purpose Campaigns. From time to time, special purpose campaigns for campus-specific objectives (for example, a significant scholarship fund or faculty endowment program) may be conducted~~, with or~~ without ~~the assistance of private fund-raising counsel~~ approval by the Board of Regents. ~~No such campaign shall be authorized or undertaken until the campaign has been approved by the Board of Regents.~~ However, special purpose campaigns regarding prominent buildings and programs as identified in Series 80307, must be approved by the Board of Regents.

7.2 Comprehensive Capital Campaigns. All broad-scale, institution-wide campaigns must be reviewed by the appropriate Executive Vice Chancellor and the Vice Chancellor for External Relations before campaign plans are implemented and consultants retained. Other than planning efforts necessary for appropriate review, no such campaign shall be authorized or undertaken until it is approved by the Board of Regents.

Sec. 8~~5~~ Ex-Students' Associations. Not withstanding the provisions hereof conferring authority upon and placing responsibility with the Chancellor for fund development and fund raising, it is understood that ex-students' associations of the U. T. System institutions may engage in fund raising for their own support through dues and payments for memberships, both annual and life. However, it is expected that no such ex-students' association will sponsor or participate in any other organized fund raising effort without first consulting with and gaining the approval of the president of the institution ~~and the Chancellor~~.

Sec. 9 Development Activity Reporting. Each institution shall participate annually in the Voluntary Support of Education (VSE) survey administered by the Council for Aid to Education (CAE) and submit the resulting report to the institution's president and the Vice Chancellor for External Relations.

1. Title

Advisory Councils of an Institution

2. Rule and Regulation

Sec. 1 ~~Establishment and Organization~~ Authorization. With the approval of the president of an institution, the Vice Chancellor for External Relations, the appropriate Executive Vice Chancellor, the Chancellor, and the Board of Regents, any school, college, or other comparable teaching or research unit may have an advisory council dedicated to its own unique interests. ~~Such an~~ An advisory council ~~is responsible through the dean or director to the president of the institution and through him or her to the institution development board for all private funds developed for that school, college, or comparable unit. Each advisory council shall determine its development needs and shall direct the formulation of plans and the promotion of support for its programs~~ for any subdivision or small unit such as a department or unit within a college or school requires specific approval of the president.

Sec. 2 Purpose. An advisory council shall promote and support, including assistance in increasing private support, a particular school, college, or other comparable teaching or research unit with which the advisory council is affiliated in a manner determined by the dean or the director of the school, college, or research unit subject to the approval of the institution's president.

Sec. 3~~2~~ ~~Membership~~Composition. An advisory council shall consist of members recommended by the dean or director of the school, college, or other approved unit and appointed by the president of the institution ~~with final approval of the membership delegated by the Board of Regents to the Chancellor following consultation with the appropriate Executive Vice Chancellor~~. Presidents shall, in consultation with the dean or director of the school, college, or other approved unit, adopt guidelines for the appointment ~~and/or reappointment~~ of the members of the institution's advisory council(s). The guidelines shall make clear each individual's term of office and the expectations and responsibilities of membership. Consideration shall be directed to appropriate balance in advisory council membership, including ~~concerns relating to~~ gender, ethnicity, years of involvement or experience with the college, school, or unit, geographical distribution, and the special needs of the school, college, or unit~~. Institutions shall forward accurate rosters of advisory council membership(s) to the Chancellor via the Vice Chancellor for External Relations no later than July 15 of each year~~ and the advisory council. All terms shall officially begin on September 1. ~~Official rosters of advisory council membership shall be maintained in the Office of the Vice Chancellor for External Relations.~~ A dean or director shall be an ex-officio member with voting privileges on the advisory council that serves the school, college, or unit's advisory council he or she administers. The president of the institution shall be an ex officio member ~~of~~ with voting privileges of all the institution's advisory councils.

Sec. 4~~3~~ ~~Officers~~ Governance and Bylaws. Consistent with the Regents' *Rules and Regulations*, the president of each institution shall be responsible for and have authority over the institution's advisory council. An advisory council ~~may~~ will elect a chair~~man~~ and such other ~~such~~ officers as are appropriate from among its membership. ~~The dean or director, and the president of the institution, or his or her delegate shall be ex officio members with voting privileges.~~

4.1 Model Bylaws. Subject to the approval of the president of the institution, each advisory council shall adopt bylaws for its internal governance that are consistent with this Series and that substantially comply with model bylaws developed by the Office of General Counsel.

~~Sec. 4 Duties and Responsibilities. The duties and responsibilities of an advisory council are as follows:~~

~~4.1 An advisory council shall seek to enlist the aid of numerous friends of the school, college, or comparable unit in fund-development efforts, and may establish such committees and other groups as seem desirable in carrying out its programs.~~

~~4.2 An advisory council shall recommend through the dean or director or the institution's president to the development board the consideration of current and long-range programs that shall secure private funds for the unit.~~

~~4.3 An institution advisory council shall have responsibility within that school, college, or comparable unit:~~

~~(a) for studying and developing private fund needs;~~

~~(b) for coordinating and formulating plans and actively promoting support for both current and long-range programs to meet the developmental needs;~~

~~(c) for periodic reports of progress to the chief administrative officer of the institution and the development board on the plans and programs of the advisory council; and~~

~~(d) for establishing a continuing program of collection and dissemination of information regarding gifts and endowments.~~

~~4.4 At periodic intervals, the dean or director shall lay before his or her advisory council descriptions of current development needs.~~

~~4.5 The work of all advisory councils shall be considered a part of the work of institution development boards.~~

Sec. 5 Reporting and Budget. Institutions shall annually forward an accurate roster of all advisory council memberships to the Vice Chancellor for External Relations on a designated date. Each institution shall maintain specifically identifiable accounts that document any advisory council related revenues and expenses out of the dean's office or other offices that support advisory council activities. These accounts must be identifiable in an institution's annual operating budget. An advisory council's budget shall be determined and approved through established budget procedures.

Sec. 6 Role of Internal Foundations. As used in this Series, the term "internal foundation" means an internal development entity created by resolution of the Board of Regents of The University of Texas System for certain development purposes. An internal foundation is part of an organizational structure of either a development board or an advisory council and functions as an administrative and accounting mechanism that is employed to approach prospective donors. Internal foundations are not encouraged and shall not be established or maintained except with the approval of the president of the institution, the Vice Chancellor for External Relations, the appropriate Executive Vice Chancellor, the Chancellor, and the Board of Regents.

~~1. Title~~

~~Internal Foundations~~

~~2. Rule and Regulation~~

~~Sec. 1 Creation. An internal foundation may be established to benefit an institution, or a school, college, or other comparable teaching or research unit within an institution upon the recommendation of a development board or an advisory council, after approval of the president of the institution, the appropriate Executive Vice Chancellor, the Chancellor, and the Board of Regents.~~

~~Sec. 2 Separate Groups. Divisions and departments below the level of a school, college, or other comparable teaching or research unit may effectively work as separate groups within the framework of the advisory council and internal foundation which represents a school or college or comparable teaching or research unit. Provisions for the designation of special funds to be used for specific activities within the framework of the various internal foundations and advisory councils will be made in order to avoid stifling the interest and initiative of these groups.~~

~~Sec. 3 Annual Review. There shall be an annual review of the activities of each internal foundation to determine its effectiveness; and, if it is unproductive for an unreasonable length of time, it shall be dissolved.~~

~~Sec. 4 Conformance with Board Rules. Every effort shall be made to permit a free range of initiative within the internal foundations, and their associated development boards and advisory councils, but activities must be in conformity with rules of the Board of Regents so as to permit maximum overall achievements in fund raising throughout the U. T. System.~~

~~Sec. 5 Expenditure of Funds. All internal foundation funds shall be appropriately accounted for in University endowment and restricted fund accounts. As in the case of other University funds, authorization for expenditure of all funds in internal foundation accounts is vested in the Board of Regents. Except for those funds to be spent in accordance with the terms of Regental acceptance, authorization for expenditure normally will be obtained during the annual institutional budget approval process.~~

~~Sec. 6 Standard Resolution. From and after October 24, 1980, the Board of Regents of The University of Texas System adopts the following standard resolution form with regard to the establishment and operation of internal foundations:~~

~~RESOLUTION OF THE BOARD OF REGENTS~~
~~OF THE UNIVERSITY OF TEXAS SYSTEM~~

~~WHEREAS, There exists a clear and specific need for means to finance the program of (name of school, college, or other component unit) of The University of Texas (name of component institution), in addition to the regular budgetary provisions, and~~

~~WHEREAS, It is the desire of interested persons to set up the facilities to encourage and assist in such financing,~~

~~IT IS NOW RESOLVED, That the Board of Regents of The University of Texas System hereby establishes the (name) Foundation of the (name of school, college, or other component unit) of The University of Texas (name of component institution).~~

~~AND FURTHER, That the purpose of the said Foundation shall be to foster the understanding and development of the programs of the (name of school, college, or other component unit) at The University of Texas (name of component institution), and to encourage the making of gifts to the Foundation by deed, grant, will or otherwise for any purpose appropriate to the work of the Foundation.~~

~~1. The funds of the Foundation shall be devoted solely to the enrichment of the academic programs of the (name of school, college, or other component unit) of The University of Texas (name of component institution) and shall not be used for the ordinary operating expenses of the (name of school, college, or other component unit).~~

~~2. A donation to the Foundation may be made for a specific purpose and may be given in the name of the donor or other designation specified by the donor or may be given as unrestricted funds.~~

~~3. The Board of Regents shall hold, manage, control, sell, exchange, lease, convey, mortgage or otherwise encumber, invest or reinvest, and generally shall have power to dispose of in any manner and for any consideration and on any terms the said gifts, funds, or property in their discretion and shall from time to time pay out of the income, or if the income be insufficient, out of the principal, all expenses of trust and all expenditures incurred in furthering the purposes of the trust.~~

~~4. Neither any donation to the (name) Foundation nor any fund or property arising there from in whatever form it may take shall ever be any part of the Permanent University Fund nor shall the Legislature have power or be in any way authorized to change the~~

~~purposes thereof or to divert such donation, fund or property from those designated purposes.~~

~~5. As in the case of other University funds, authorization for expenditure of all funds from the Foundation shall be vested in the Board of Regents and recommendations for such expenditures shall be made by the (president) through the appropriate Executive Vice Chancellor to the Chancellor and by the Chancellor to the Board of Regents of The University of Texas System.~~

~~Sec. 7 List of Foundations. Upon Regental approval of the standard resolution creating an internal foundation, the name of the foundation will be added to the list below. The Counsel and Secretary to the Board of Regents shall prepare a copy of the standard resolution in appropriate form for the Chairman's signature and shall distribute a copy to the appropriate Executive Vice Chancellor, the Chancellor, and to the president of the component institution involved.~~

~~**Foundation**~~	~~**Date Established**~~
~~**The University of Texas at Austin**~~	
~~John Charles Townes Foundation (School of Law)~~	~~6/27/42~~
~~Pharmaceutical Foundation of the College of Pharmacy~~	~~12/10/52~~
~~Fine Arts Foundation of the College of Fine Arts~~	~~12/1/50~~
~~Architectural Foundation of the School of Architecture~~	~~5/30/52~~
~~Genetics Foundation of the Zoology Department~~	~~3/28/52~~
~~The Psychological Research Foundation~~	~~5/29/53~~
~~Geology Foundation of the Department of Geology~~	~~10/24/53~~
~~Engineering Foundation of the College of Engineering~~	~~3/11/55~~
~~College of Education Foundation (formerly Teacher Education Foundation – 9/22/56)~~	~~12/12/76~~
~~Social Work Foundation of the School of Social Work~~	~~10/1/66~~

~~Foundation~~	~~Date Established~~
~~The University of Texas at Austin~~	
~~Communication Foundation of the School of Communication (formerly the Journalism Foundation of the School of Journalism – established 1/10/59)~~	~~1/31/69~~
~~Graduate School Foundation~~	~~3/26/76~~
~~Graduate School of Library Science Foundation~~	~~6/20/69~~
~~College of Liberal Arts Foundation~~	~~7/11/80~~
~~College of Natural Sciences Foundation~~	~~7/11/80~~
~~Nursing Foundation of the School of Nursing~~	~~10/9/87~~
~~Longhorn Foundation~~	~~12/3/87~~
~~The University of Texas M. D. Anderson Cancer Center~~	
~~University Cancer Foundation~~	~~10/15/55~~
~~The University of Texas at Arlington~~	
~~The University of Texas at Arlington Foundation~~	~~1/28/67~~
~~The University of Texas Medical Branch at Galveston~~	
~~The University of Texas Medical Branch at Galveston Foundation~~	~~5/6/67~~
~~The University of Texas at El Paso~~	
~~The University of Texas at El Paso Foundation~~	~~7/29/67~~
~~The University of Texas at El Paso Miner Foundation~~	~~2/13/92~~

~~**Foundation**~~	~~**Date Established**~~
~~**The University of Texas at Dallas**~~	
~~Management School Foundation~~	~~2/11/93~~
~~**The University of Texas – Pan American**~~	
~~Bronc Foundation~~	~~10/7/94~~
~~**The University of Texas of the Permian Basin**~~	
~~Falcon Athletic Club Foundation~~	~~5/11/95~~

13. U. T. System Board of Regents: Approval of the University of Texas Investment Management Company (UTIMCO) Board recommendations to (a) amend Exhibit A of the Investment Policy Statements for the Permanent University Fund (PUF), the General Endowment Fund (GEF), and the Intermediate Term Fund (ITF) related to the adoption of a new benchmark for the hedge fund asset class, effective January 1, 2006, for the PUF and the GEF, and effective February 1, 2006, for the ITF; and (b) restate and republish the hedge fund benchmark performance for the period January through April 2006

RECOMMENDATION

The Chancellor and the Executive Vice Chancellor for Business Affairs concur in the recommendation of the Board of Directors of The University of Texas Investment Management Company (UTIMCO) that the U. T. System Board of Regents approve the adoption of a new benchmark for the Hedge Fund asset class, which requires amending Exhibit A of the Investment Policy Statements for each of the Permanent University Fund (PUF), the General Endowment Fund (GEF), and the Intermediate Term Fund (ITF) and approve restatement and republication of the corresponding benchmark performance of the MSCI Investable Hedge Fund Index. Amendments to Exhibit A are detailed in the following:

a. PUF Exhibit A (See Page 46)

b. GEF Exhibit A (See Page 47)

c. ITF Exhibit A (See Page 48)

BACKGROUND INFORMATION

The current benchmarks for the PUF and GEF were adopted by the U. T. System Board of Regents on August 11 and made effective September 1, 2005. The benchmarks for the ITF approved by the U. T. System Board of Regents on February 9, 2006, were made effective as of July 1, 2006. The benchmarks for the directional hedge funds and the absolute return hedge funds were composites of Standard & Poor's (S&P) "investable" hedge fund indices.

The integrity and reliability of these indices have been called into question since the investment manager, PlusFunds, had disputed dealings with Refco in late 2005 and subsequently filed for bankruptcy in early 2006. On June 28, 2006, S&P announced that due to the diminishing number of managed accounts and their distribution in the index as of July 1, 2006, the S&P hedge fund indices would not be representative of the broad range of strategies that hedge funds employ and therefore would no longer be published. The S&P has not published final numbers for May 2006, and therefore, preliminary numbers that were reported for May cannot be verified.

Due to the elimination of the S&P benchmark, a replacement benchmark is required. Therefore, UTIMCO staff conducted a thorough review of alternative benchmark solutions for the portfolio and recommended a new benchmark, the MSCI Investable Hedge Fund Index, to be used for both the Directional Hedge Funds and the Absolute Return Hedge Funds. On July 13, 2006, the UTIMCO Board approved use of the proposed MSCI Investable Hedge Fund Index.

The UTIMCO Board approved the effective date for the new benchmark as January 1, 2006, for the PUF and GEF and February 1, 2006, for the ITF. January 1, 2006 is recommended as the effective date for the new benchmark because this date approximately coincides with Refco's claim against PlusFunds, the catalyst that created the disruptive developments surrounding the S&P investable indices.

Items I and II on Pages 49 - 50 demonstrate the effect of the retroactive change for the period January through April 2006 as a reduction in the PUF and GEF hedge fund asset class benchmark performance of -0.06%. The effect of the retroactive change for this four-month period on the policy portfolio benchmark performance for the PUF and GEF is a reduction of -0.02%.

Item III on Page 51 demonstrates the effect of the retroactive change for the ITF's hedge fund asset class benchmark performance for the period February through April 2006 as a reduction of -0.34%. The effect on the ITF policy portfolio benchmark performance for this three-month period is a reduction of -0.08%.

The hedge fund benchmark performance reported from January 1 through April 30, 2006, is not an "error" as defined by the U. T. System Investment Performance Reporting Error Correction Policy (approved July 8, 2005) since it was not misstated, miscalculated, or presented incorrectly. The policy does provide, however, that the U. T. System Board of Regents will make the final determination concerning whether a proposed restatement and republication should be made in cases where a benchmark is replaced for reasons other than an actual error. The restatement relates to the hedge fund benchmark only and does not affect actual investment performance.

EXHIBIT A

PERMANENT UNIVERSITY FUND
POLICY TARGETS, RANGES AND PERFORMANCE OBJECTIVES

	Percent of Portfolio (%)		
Asset Category	**Policy Targets**	**Policy Ranges**	**Benchmarks**
U.S. Equities	**20.0**	**10 to 30**	Russell 3000 Index
Global ex U.S. Equities	**17.0**	**10 to 30**	
Non-U.S. Developed Equity	10.0	0 to 30	MSCI EAFE Index with net dividends
Emerging Markets Equity	7.0	0 to 10	MSCI Emerging Markets Index with net dividends
Hedge Funds	**25.0**	**15 to 27.5**	**MSCI Investable Hedge Fund Index***
Directional Hedge Funds	10.0	5 to 15	~~Combination index: 50% S&P Event-Driven Hedge Fund Index plus 50% S&P Directional/Tactical Hedge Fund Index~~
Absolute Return Hedge Funds	15.0	10 to 20	~~Combination index: 66.7% S&P Event-Driven Hedge Fund Index plus 33.3% S&P Arbitrage Hedge Fund Index~~
Private Capital	**15.0**	**5 to 15**	Venture Economics' Periodic IRR Index
Venture Capital	4.0	0 to 8	
Private Equity	11.0	5 to 15	
Inflation Linked	**13.0**	**5 to 20**	
REITS	5.0	0 to 10	Dow Jones Wilshire Real Estate Securities Index
Commodities	3.0	0 to 6	Combination index: 66.7% GSCI minus .5% plus 33.3% DJ-AIG Commodity Index
TIPS	5.0	0 to 10	Lehman Brothers US TIPS Index
Fixed Income:	**10.0**	**5 to 15**	Lehman Brothers Aggregate Bond Index
Liquidity Reserve	**0.0**	**-1 to 10**	90 Day T-Bills
Unencumbered Cash			
Temporary Cash Imbalance**			
Net non-trading receivable			

Expected Annual Return (%)	8.34
1 year Downside Deviation (%)	-7.6
Standard Deviation (%)	10.8

	% of Target Risk
Upper Risk Bound: 1 year Downside Deviation (%)	128%
Lower Risk Bound: 1 year Downside Deviation (%)	74%

*Effective date: January 1, 2006

** 3 trading days or less

EXHIBIT A

GENERAL ENDOWMENT FUND
POLICY TARGETS, RANGES AND PERFORMANCE OBJECTIVES

	Percent of Portfolio (%)		
Asset Category	**Policy Targets**	**Policy Ranges**	**Benchmarks**
U.S. Equities	**20.0**	**10 to 30**	Russell 3000 Index
Global ex U.S. Equities	**17.0**	**10 to 30**	
Non-U.S. Developed Equity	10.0	0 to 30	MSCI EAFE Index with net dividends
Emerging Markets Equity	7.0	0 to 10	MSCI Emerging Markets Index with net dividends
Hedge Funds	**25.0**	**15 to 27.5**	**MSCI Investable Hedge Fund Index***
Directional Hedge Funds	10.0	5 to 15	~~Combination index: 50% S&P Event-Driven Hedge Fund Index plus 50% S&P Directional/Tactical Hedge Fund Index~~
Absolute Return Hedge Funds	15.0	10 to 20	~~Combination index: 66.7% S&P Event-Driven Hedge Fund Index plus 33.3% S&P Arbitrage Hedge Fund Index~~
Private Capital	**15.0**	**5 to 15**	Venture Economics' Periodic IRR Index
Venture Capital	4.0	0 to 8	
Private Equity	11.0	5 to 15	
Inflation Linked	**13.0**	**5 to 20**	
REITS	5.0	0 to 10	Dow Jones Wilshire Real Estate Securities Index
Commodities	3.0	0 to 6	Combination index: 66.7% GSCI minus .5% plus 33.3% DJ-AIG Commodity Index
TIPS	5.0	0 to 10	Lehman Brothers US TIPS Index
Fixed Income:	**10.0**	**5 to 15**	Lehman Brothers Aggregate Bond Index
Liquidity Reserve	**0.0**	**-1 to 10**	90 Day T-Bills
Unencumbered Cash			
Temporary Cash Imbalance**			
Net non-trading receivable			

Expected Annual Return (%)	8.34
1 year Downside Deviation (%)	-7.6
Standard Deviation (%)	10.8

	% of Target Risk
Upper Risk Bound: 1 year Downside Deviation (%)	128%
Lower Risk Bound: 1 year Downside Deviation (%)	74%

*Effective date: January 1, 2006

** 3 trading days or less

EXHIBIT A

INTERMEDIATE TERM FUND
POLICY TARGETS, RANGES, AND PERFORMANCE OBJECTIVES

Asset Categories	Percent of Policy (%)		Benchmarks
	Policy Targets	Policy Ranges	
U.S. Equities	**15**	**5 to 20**	**Russell 3000 Index**
Global ex U.S. Equities	**10**	**0 to 15**	
Non - U.S. Developed Equity	5	0 to 10	MSCI EAFE Index with net dividends
Emerging Markets Equities	5	0 to 10	MSCI Emerging Markets Index with net dividends
Hedge Funds	**25**	**10 to 27.5**	**MSCI Investable Hedge Fund Index***
Directional Hedge Funds	12.5	5 to 20	~~Combination index: 50% S&P Event-Driven Hedge Fund Index plus 50% S&P Directional/Tactical Hedge Fund Index~~
Absolute Return Hedge Funds	12.5	5 to 20	~~Combination index: 66.7% S&P Event-Driven Hedge Fund Index plus 33.3% S&P Arbitrage Hedge Fund Index~~
Inflation Linked	**25**	**10 to 35**	
REITS	10	0 to 15	Dow Jones Wilshire Real Estate Securities Index
Commodities	5	0 to 10	Combination Index: 66.7% GSCI minus .5% plus 33.3% DJ-AIG Commodity Index
TIPS	10	5 to 15	Lehman Brothers US TIPS Index
Fixed Income	**25**	**15 to 40**	Lehman Brothers Aggregate Bond Index
Liquidity Reserve	0.0	-1 to 20	90 Day T-Bills
Unencumbered Cash			
Temporary Cash Imbalance**			
Net non-trading receivable			

Expected Annual Return (%)	7.08
1 year Downside Deviation (%)	-5.0
Standard Deviation (%)	7.5

		% of Target Risk
Upper Risk Bound: 1 year Downside Deviation (%)		127%
Lower Risk Bound: 1 year Downside Deviation (%)		69%

* Effective date: February 1, 2006

** 3 trading days or less

I. PERMANENT UNIVERSITY FUND
Fiscal Year to Date Performance Attribution through April 30, 2006

Presented with current Hedge Fund Benchmark

Asset Class	Returns: Portfolio	Returns: Policy Benchmark	Value Added: From Asset Allocation	Value Added: From Security Selection	Value Added: Total
Cash and Cash Equivalents	2.79%	2.63%	0.02%	0.00%	0.02%
U.S. Equities	5.63%	9.57%	0.01%	-0.81%	-0.80%
Non-U.S. Developed Equity	26.37%	24.61%	0.37%	0.15%	0.52%
Emerging Markets Equity	29.17%	40.58%	-0.10%	-0.70%	-0.80%
Directional Hedge Funds	6.56%	6.52%	0.03%	0.00%	0.03%
Absolute Return Hedge Funds	8.43%	5.74%	0.00%	0.41%	0.41%
REITS	17.32%	14.79%	-0.01%	0.12%	0.11%
Commodities	-0.57%	-3.05%	-0.30%	0.08%	-0.22%
TIPS	-2.01%	-2.36%	0.10%	0.02%	0.12%
Fixed Income	-0.43%	-1.26%	-0.04%	0.09%	0.05%
Total Marketable Securities	**9.82%**	**10.40%**	**0.08%**	**-0.64%**	**-0.56%**
Private Capital	12.16%	18.25%	-0.06%	-0.87%	-0.93%
Total	**10.07%**	**11.56%**	**0.02%**	**-1.51%**	**-1.49%**

	Policy Target Allocation	Benchmark Return	Weighted Benchmark
Directional Hedge Funds	10.00%	6.52%	2.61%
Absolute Return Hedge Funds	15.00%	5.74%	3.44%
Total Hedge Fund Benchmark			6.05%

Presented with proposed Hedge Fund benchmark restated from January 1, 2006 - April 30, 2006

Asset Class	Returns: Portfolio	Returns: Policy Benchmark	Value Added: From Asset Allocation	Value Added: From Security Selection	Value Added: Total
Cash and Cash Equivalents	2.79%	2.63%	0.02%	0.00%	0.02%
U.S. Equities	5.63%	9.57%	0.01%	-0.81%	-0.80%
Non-U.S. Developed Equity	26.37%	24.61%	0.37%	0.15%	0.52%
Emerging Markets Equity	29.17%	40.58%	-0.10%	-0.70%	-0.80%
Directional Hedge Funds	6.56%	6.45%	0.03%	0.01%	0.04%
Absolute Return Hedge Funds	8.43%	5.69%	0.00%	0.42%	0.42%
REITS	17.32%	14.79%	-0.01%	0.12%	0.11%
Commodities	-0.57%	-3.05%	-0.30%	0.08%	-0.22%
TIPS	-2.01%	-2.36%	0.10%	0.02%	0.12%
Fixed Income	-0.43%	-1.26%	-0.04%	0.09%	0.05%
Total Marketable Securities	**9.82%**	**10.38%**	**0.08%**	**-0.62%**	**-0.54%**
Private Capital	12.16%	18.25%	-0.06%	-0.87%	-0.93%
Total	**10.07%**	**11.54%**	**0.02%**	**-1.49%**	**-1.47%**

	Policy Target Allocation	Benchmark Return	Weighted Benchmark
Directional Hedge Funds	10.00%	6.45%	2.58%
Absolute Return Hedge Funds	15.00%	5.69%	3.41%
Total Hedge Fund Benchmark			5.99%

II. GENERAL ENDOWMENT FUND
Fiscal Year to Date Performance Attribution through April 30, 2006

Presented with current Hedge Fund Benchmark

Asset Class	Returns: Portfolio	Returns: Policy Benchmark	Value Added: From Asset Allocation	Value Added: From Security Selection	Value Added: Total
Cash and Cash Equivalents	2.79%	2.63%	0.04%	0.00%	0.04%
U.S. Equities	5.95%	9.57%	-0.03%	-0.74%	-0.77%
Non-U.S. Developed Equity	25.99%	24.61%	0.35%	0.12%	0.47%
Emerging Markets Equity	28.61%	40.58%	-0.19%	-0.73%	-0.92%
Directional Hedge Funds	6.46%	6.52%	0.04%	-0.01%	0.03%
Absolute Return Hedge Funds	8.36%	5.74%	0.00%	0.40%	0.40%
REITS	17.35%	14.79%	-0.02%	0.12%	0.10%
Commodities	-0.55%	-3.05%	-0.30%	0.08%	-0.22%
TIPS	-2.00%	-2.36%	0.12%	0.02%	0.14%
Fixed Income	-0.22%	-1.26%	-0.04%	0.11%	0.07%
Total Marketable Securities	**9.73%**	**10.40%**	**-0.03%**	**-0.63%**	**-0.66%**
Private Capital	11.51%	18.25%	-0.02%	-0.97%	-0.99%
Total	**9.91%**	**11.56%**	**-0.05%**	**-1.60%**	**-1.65%**

	Policy Target Allocation	Benchmark Return	Weighted Benchmark
Directional Hedge Funds	10.00%	6.52%	2.61%
Absolute Return Hedge Funds	15.00%	5.74%	3.44%
Total Hedge Fund Benchmark			6.05%

Presented with proposed Hedge Fund benchmark restated from January 1, 2006 - April 30, 2006

Asset Class	Returns: Portfolio	Returns: Policy Benchmark	Value Added: From Asset Allocation	Value Added: From Security Selection	Value Added: Total
Cash and Cash Equivalents	2.79%	2.63%	0.04%	0.00%	0.04%
U.S. Equities	5.95%	9.57%	-0.03%	-0.74%	-0.77%
Non-U.S. Developed Equity	25.99%	24.61%	0.35%	0.12%	0.47%
Emerging Markets Equity	28.61%	40.58%	-0.19%	-0.73%	-0.92%
Directional Hedge Funds	6.46%	6.45%	0.04%	0.00%	0.04%
Absolute Return Hedge Funds	8.36%	5.69%	0.00%	0.41%	0.41%
REITS	17.35%	14.79%	-0.02%	0.12%	0.10%
Commodities	-0.55%	-3.05%	-0.30%	0.08%	-0.22%
TIPS	-2.00%	-2.36%	0.12%	0.02%	0.14%
Fixed Income	-0.22%	-1.26%	-0.04%	0.11%	0.07%
Total Marketable Securities	**9.73%**	**10.38%**	**-0.03%**	**-0.61%**	**-0.64%**
Private Capital	11.51%	18.25%	-0.02%	-0.97%	-0.99%
Total	**9.91%**	**11.54%**	**-0.05%**	**-1.58%**	**-1.63%**

	Policy Target Allocation	Benchmark Return	Weighted Benchmark
Directional Hedge Funds	10.00%	6.45%	2.58%
Absolute Return Hedge Funds	15.00%	5.69%	3.41%
Total Hedge Fund Benchmark			5.99%

III. INTERMEDIATE TERM FUND
Inception to Date Performance Attribution through April 30, 2006

Presented with current Hedge Fund Benchmark

Asset Class	Returns: Portfolio	Returns: Policy Benchmark	Value Added: From Asset Allocation	Value Added: From Security Selection	Value Added: Total
Cash and Cash Equivalents	1.12%	1.08%	-0.03%	0.00%	-0.03%
U.S. Equities	2.72%	3.02%	0.00%	-0.04%	-0.04%
Non-U.S. Developed Equity	8.70%	7.99%	0.01%	0.03%	0.04%
Emerging Markets Equity	3.89%	7.94%	0.01%	-0.20%	-0.19%
Directional Hedge Funds	2.96%	2.81%	-0.04%	0.02%	-0.02%
Absolute Return Hedge Funds	3.76%	2.97%	0.02%	0.10%	0.12%
REITS	4.86%	3.75%	-0.02%	0.10%	0.08%
Commodities	0.21%	1.04%	0.00%	-0.05%	-0.05%
TIPS	-1.94%	-2.32%	-0.01%	0.04%	0.03%
Fixed Income	-0.17%	-0.83%	0.02%	0.17%	0.19%
Total	**2.13%**	**2.00%**	**-0.04%**	**0.17%**	**0.13%**

	Policy Target Allocation	Benchmark Return	Weighted Benchmark
Directional Hedge Funds	12.50%	2.81%	1.41%
Absolute Return Hedge Funds	12.50%	2.97%	1.49%
Total Hedge Fund Benchmark			2.89%

Presented with proposed Hedge Fund benchmark restated from February 1, 2006 - April 30, 2006

Asset Class	Returns: Portfolio	Returns: Policy Benchmark	Value Added: From Asset Allocation	Value Added: From Security Selection	Value Added: Total
Cash and Cash Equivalents	1.12%	1.08%	-0.03%	0.00%	-0.03%
U.S. Equities	2.72%	3.02%	0.00%	-0.04%	-0.04%
Non-U.S. Developed Equity	8.70%	7.99%	0.01%	0.03%	0.04%
Emerging Markets Equity	3.89%	7.94%	0.01%	-0.20%	-0.19%
Directional Hedge Funds	2.96%	2.55%	-0.04%	0.05%	0.01%
Absolute Return Hedge Funds	3.76%	2.55%	0.02%	0.15%	0.17%
REITS	4.86%	3.75%	-0.02%	0.10%	0.08%
Commodities	0.21%	1.04%	0.00%	-0.05%	-0.05%
TIPS	-1.94%	-2.32%	-0.01%	0.04%	0.03%
Fixed Income	-0.17%	-0.83%	0.02%	0.17%	0.19%
Total	**2.13%**	**1.92%**	**-0.04%**	**0.25%**	**0.21%**

	Policy Target Allocation	Benchmark Return	Weighted Benchmark
Directional Hedge Funds	12.50%	2.55%	1.28%
Absolute Return Hedge Funds	12.50%	2.55%	1.28%
Total Hedge Fund Benchmark			2.55%

14. U. T. System Board of Regents: Approval of Restated University of Texas Investment Management Company (UTIMCO) Compensation Program

RECOMMENDATION

The University of Texas Investment Management Company (UTIMCO) Board of Directors recommends that the U. T. System Board of Regents (Board) approve the restated UTIMCO Compensation Program as set forth in congressional style on Pages 59 - 96. The proposed revisions, approved by actions of the UTIMCO Board of Directors on July 13, 2006, and July 25, 2006, amend and restate the UTIMCO Compensation Program that was approved by the Board on September 28, 2004, to be effective for the full Plan Year beginning July 1, 2006, except for specific provisions required to be effective earlier by IRS Regulations.

BACKGROUND INFORMATION

UTIMCO originally adopted a compensation program effective September 1, 2000. This program was amended and restated in its entirety effective September 1, 2004, (the "Prior Plan") for key investment and operations staff. The salaries and merit bonuses for employees other than the key investment and operation staff are determined by Corporation's management in accordance with the Compensation Committee Charter of the UTIMCO Board. The proposed FY 2007 UTIMCO budget on Page 100 includes funding for a discretionary bonus program for employees not eligible for the Compensation Program.

The Prior Compensation Plan included a two-part structure for determining annual compensation, base salary, and an annual incentive plan. Changes to the Prior Plan were approved by actions of the UTIMCO Board on July 13, 2006, and July 25, 2006, and it has been restated in its entirety as the UTIMCO Compensation Program (the "Compensation Program"). The effective date of the restatement is July 1, 2006, except that the provisions relating to Section 409A of the *Internal Revenue Code of 1986*, as amended are effective January 1, 2005, and the changes to Section 5.7 are effective September 1, 2004.

Primary Substantive Changes

The most significant changes to the Prior Plan are

(1) change in Table 1 of Appendix C on Page 94 related to target and maximum incentive award opportunities (percent of salary). The proposed changes to Appendix C (see Item 12 on Page 58) increase the maximum potential performance incentive award opportunities by approximately $1.6 million (39.9%) to $5.619 million. FY07 budgeted incentive award funding increased also by 39.9% ($569,000) as a result of the proposed changes. The budget estimates that 50% of maximum potential incentive awards will be earned, of which 70% will be paid in the current budget year (30% is deferred and paid over the three

years following); however, if performance maximum thresholds are achieved, incentive awards at the maximum potential are payable to eligible participants, 70% paid currently and 30% paid over three successive years.

(2) inclusion of the new Intermediate Term Fund (formed February 1, 2006) in the basis for measuring entity performance and performance of the asset classes in determining entitlement to awards

(3) requirement of the distribution of nonvested deferred awards immediately after they became vested due to the addition of Section 409A (409A) to the *Internal Revenue Code of 1986*, as amended.

The remaining changes clarify operational provisions of the Compensation Program, are necessary to conform or exempt the Compensation Program to/from 409A, and are stylistic.

1. <u>Intermediate Term Fund</u>

The Prior Plan is amended to incorporate the Intermediate Term Fund ("ITF") as a measure of entity performance and asset class performance effective July 1, 2006. For the entity performance portion, the actual total return of the ITF is measured against the ITF policy portfolio benchmark. For purposes of entity performance, the performance of the total endowment assets is weighted at 85%, and the performance of the ITF is weighted at 15%. The weighting was determined by calculating the approximate percentage of the ITF assets compared to the total of the endowment funds and ITF. Until June 30, 2009, instead of a three-year historical period, the performance of the ITF will be measured based on the actual number of years it is part of the Compensation Program. The benchmarks and performance standards for measuring the ITF are outlined in Table 4 that has been inserted as Appendix D in the Compensation Program (Pages 95 – 96).

<u>Summary of Changes Related to Intermediate Term Fund</u>

a. Section 5.8, Performance Measurement Standards, is amended to add provisions relative to the 15% weighting of the ITF to measure entity performance.

b. Section 5.9, Modification of Performance Standards for Newly Hired Employees. The title of this section is changed to Modifications of Measurement Period for Measuring Equity and Asset Class Performance Goals and stylistic changes have been made. Section 5.9(a) is added regarding the measure that will be used for the ITF until three years of historical data is available.

c. Section 8, Definition of Terms. Section 8.1, Asset Class Performance and Section 8.8, Entity Performance, definitions are updated to include references to the ITF. Section 8.10 adds the definition of ITF. Section 8.22 adds a definition of Policy Portfolio Return as the benchmark return for the ITF policy portfolio and is calculated by summing the neutrally weighted index returns (percentage weight for each asset class multiplied by the benchmark return for the asset class) for the various asset classes in the Intermediate Term Fund portfolio for the Performance Period.

2. **<u>Continued Investment with UTIMCO of Vested Awards/Compliance with *Internal Revenue Code* Section 409A</u>**

On October 4, 2004, Congress amended the *Internal Revenue Code of 1986*, as amended by adding Section 409A that requires changes in the operation and provisions of most nonqualified deferred compensation plans. The Prior Plan falls within the definition of a nonqualified deferred compensation plan for purposes of 409A. The new rules were effective January 1, 2005, and as of that date, nonqualified deferred compensation plans (with a few exceptions) must be operated in compliance with 409A or face significant adverse federal income tax consequences. Failure to comply with 409A subjects plan participants to a penalty tax equal to 20% of the amounts deferred plus interest. Plan administrators, however, have until December 31, 2006, to amend plan documents to comply with the new law.

Because of the change in law, it was necessary to delete the provision in the Prior Plan that had been added on September 1, 2004, that permitted participants to continue to invest with UTIMCO their Nonvested Deferred Awards after the award became vested (and continue to be credited or debited for the net returns of the endowment assets) (the "Vested Award"). Continued investment with UTIMCO of the Vested Award would have violated the 409A rules relating to permissible payment times for nonqualified deferred compensation. Because counsel for UTIMCO and U. T. System were aware that amendments to the Prior Plan might be needed to delete this provision at the time the Prior Plan was rolled out to employees, this option was never made available to employees and no employees had Vested Awards that would have been eligible for continued investment with UTIMCO. As such, the deletion of the provision is made effective September 1, 2004, the effective date of the Prior Plan. As amended, all Nonvested Deferred Awards will be distributed to participants upon vesting as provided in the original plan in effect from September 1, 2000 to August 31, 2004.

Other provisions of the Prior Plan also required modification to conform to 409A or, alternatively, to exempt the plan from the 409A rules. These provisions are proposed to be effective January 1, 2005.

Proposed regulations pertaining to 409A were issued by the IRS in 2005 and the IRS is expected to issue final regulations in September 2006. All plan documents must be amended to conform to the new law by December 31, 2006. Although final guidance has not yet been issued, it is the opinion of UTIMCO counsel and U. T. System counsel that changes beyond those incorporated into the Compensation Program to conform to the new law are unlikely.

<u>Summary of Changes related to *Internal Revenue Code* Section 409A</u>

a. Section 5.6, Form and Timing of Payouts of Performance Incentive Awards. A deadline for distribution of Performance Incentive Awards has been added to conform to the definition of short-term deferrals in 409A and is intended to exempt the Compensation Program from the provisions of 409A.

b. Section 5.7, Nonvested Deferred Awards. Section 5.7(c)-(e) regarding Vested Deferred Awards has been deleted to eliminate the option permitting continued investment of Awards even after the award is vested as required by 409A. Section 5.7(b)(4) adds a deadline for distribution of Vested Awards to conform to the definition of short-term deferrals in 409A and is intended to exempt the Compensation Program from the provisions of 409A.

c. Section 5.10, Termination Provisions. Section 5.10(a) provision regarding distribution of Vested Deferred Awards is deleted because the provisions regarding continued investment of Vested Deferred Awards were deleted to comply with 409A. Section 5.10(c) regarding payment of Nonvested Deferred Awards due to death or disability has been amended to add a deadline for distribution of such awards to conform to the definition of short-term deferrals in 409A and is intended to exempt the Compensation Program from the provisions of 409A. Section 5.10(d), language is added to clarify that Nonvested Deferred Awards will continue to vest and be paid as provided in the Compensation Program when a Participant is out on a Compensation Committee-approved leave of absence.

d. Section 8, Definition of Terms. Section 8.5, definition of "disability" has been added to conform to the definition required by 409A.

<u>Additional Changes</u>

1. <u>Title</u>. Language has been added on the cover page to identify the restatement of the Compensation Program: "Restated effective July 1, 2006".

2. <u>Table of Contents</u>. The Table of Contents has been adjusted to conform to new Compensation Program format.

3. <u>Section 1, Program Structure</u>. The title of this section has changed to "Compensation Program Structure and Effective Date." The first paragraph has been added to clarify the purposes of the two sections of the Compensation Program, the base salary portion and the annual performance incentive plan portion. The second paragraph, relocated from Section 5.1(b), has been added explaining the effective date of the original and restated Compensation Program.

4. Section 3, Total Compensation Program Philosophy. Stylistic changes have been made in this section.

5. Section 4, Base Salary Administration. Section 4.2 has been amended to provide that the base salary for the President and CEO will be determined by the UTIMCO Board and the base salary of all other eligible employees will be determined by the UTIMCO Compensation Committee. Stylistic changes have also been made in this section.

6. Section 5, Performance Incentive Plan.

Section 5.1(b) has been moved to Section 1, with a modification to address the restated Compensation Program.

Section 5.3, Eligibility and Participation. The Compensation Program is modified to clarify how positions become approved eligible positions annually and how participants filling the eligible positions are reported each year to the UTIMCO Board for approval. UTIMCO staff has been updating the eligible positions each year for UTIMCO Board approval and has been providing the UTIMCO Board with the individuals filling the eligible positions for approval. The modified language explains the steps that UTIMCO staff is already performing to keep the UTIMCO Board apprised of the eligible positions and the participants. Also, the time period in which the UTIMCO Board will approve the eligible positions and designate the participants was changed from 60 days after the start of the performance period to 90 days after the start of the performance period, a revision which was approved by the UTIMCO Board on September 14, 2005.

Section 5.4, Performance Goals. Stylistic revisions and cross-references have been added. In Section 5.4(d), the Compensation Program is amended to permit the UTIMCO Compensation Committee to adjust the assigned weighting for a performance goal upon a determination that weighting is inappropriate for a participant because of his or her length of service, tenure in position, or prior work experience and to provide that weightings for the Performance Goals for each Performance Period are subject to approval by the UTIMCO Board.

Section 5.5, Incentive Award Opportunity Levels and Performance Incentive Awards. Section 5.5(a) is amended to clarify that the incentive award opportunity is determined by the UTIMCO Compensation Committee for the eligible position rather than for the participant, subject to approval by the UTIMCO Board. Section 5.5(b) is revised to remove Table 1 to Appendix C and provide that it will be revised each Performance Period as soon as administratively practicable after the relevant information (e.g., eligible positions, weightings, incentive award opportunities for each eligible position) is approved by the UTIMCO Board. Section 5.5(e) is revised to reference Appendix A, which outlines the methodology for calculating Incentive Award Opportunities and Performance Incentive Awards (prior reference contained in Section 5.5(f)) and provide that Performance Incentive Awards will be interpolated in a linear fashion between threshold and target as well as between target and maximum.

Section 5.5(f) is amended to add that the Performance Incentive Award calculations submitted to the UTIMCO Compensation Committee for review will be based on certification of its advisors. Section 5.5(g), miscellaneous stylistic revisions were made.

Section 5.7, Nonvested Deferred Awards. Section 5.7(a)-(b) is clarified regarding the creation and crediting of a hypothetical account on UTIMCO's books for each participant for the Nonvested Deferred Awards and provides for the forfeiture of the Nonvested Deferred Award if the participant is not employed by UTIMCO on the date the Nonvested Deferred Award would be credited to the participant's account.

Section 5.8, Performance Measurement Standards. The table in this Section 5.8 is identified as Table 2 for the period 7/1/04 through 8/31/05. Table 3 is added to identify benchmarks for each asset class as well as threshold, target, and maximum performance standards for the Performance Period 9/1/05 through 6/30/06. Language is added to provide that similar information for the Performance Period beginning July 1, 2006, will be set forth in Table 4, which is attached as Appendix D and that revised tables for future Performance Periods will be updated as soon as administratively practicable after the benchmarks and standards are set and will be attached as Appendix D.

Section 5.10, Termination Provisions. Section 5.10(e) is added to clarify how an award is calculated and prorated when a participant ceases to be a participant prior to the end of a Performance Period.

7. Section 6, Plan Authority and Responsibility. The title of this section is changed to Compensation Program Authority and Responsibility. Section headers have been added to provide clarification. Section 6.2 has been amended to provide that in addition to the powers necessary or advisable to administer the Compensation Program, the UTIMCO Board has all powers specifically vested in the Compensation Program plan document necessitating deletion of Sections 6.2(3) and (4) because these powers are already stated in other sections of the plan document or have been vested in the UTIMCO Compensation Committee.

8. Section 7, Performance Incentive Plan Interpretation. The title of this section is changed to Compensation Program Interpretation and "Plan" is replaced by "Compensation Program" throughout this section to conform to the change in title. Section 7.3, Recordkeeping and Reporting, incorporates a revision approved by the UTIMCO Board on September 14, 2005, to be effective September 1, 2005, changing the responsibility for the review of relative performance data and calculations from the investment consultant to UTIMCO's external auditor. Section 7.9 is amended to clarify the effect of the restatement of the Compensation Program on the Prior Plan.

9. Section 8, Definition of Terms. Section 8.16, Definition of Peer Group, is amended to incorporate a definition of peer group, approved by the UTIMCO Board on September 14, 2005.

10. Appendix A. Appendix A is changed to reflect the calculation of awards considering the Intermediate Term Fund and updated tables.

11. Appendix B. Stylistic changes have been made.

12. Appendix C. Appendix C is added to include Table 1 of updated eligible positions, weightings, and incentive award opportunities for each eligible position for the Performance Period beginning July 1, 2006. Under the Prior Plan, the maximum bonus calculated based on current eligible participants is $4,016,000; under the restated Plan, the maximum bonus potential calculated based on current eligible participants is $5,619,000. This is an increase of 39.9% and a total budget impact of $569,089 or 1.1%, based on 70% payout of an estimated 50% potential earned.

13. Appendix D. Appendix D is added to include Table 4, Benchmarks for Asset Class, Threshold, Target, and Maximum Performance Standards for Performance Periods beginning on or after July 1, 2006, and Performance Standards for Intermediate Term Fund for Performance Periods beginning on or after July 1, 2006.

UTIMCO
COMPENSATION PROGRAM

Restated: Effective July 1, 2006

TABLE OF CONTENTS

~~Table of Contents~~

1. **COMPENSATION** PROGRAM STRUCTURE **AND EFFECTIVE DATE**

The UTIMCO Compensation Program **(“Compensation Program” or “Plan”)** consists of two elements~~,~~**:** base salary and an annual incentive plan (the “Performance Incentive ~~Plan” or “~~Plan”):

Base Salary	+	Performance Incentive	=	Total Compensation

The base salary portion of the Compensation Program sets forth a structure and guidelines for establishing and adjusting the salaries of key investment and operations staff employees. The Performance Incentive Plan portion of the Compensation Program sets forth the criteria for calculating and receiving annual incentive awards for key investment and operations staff who are eligible Participants in the Performance Incentive Plan. Provisions of the Compensation Program relating solely to the base salary portion of the Compensation Program are described in Section 4. Provisions of the Compensation Program relating solely to the Performance Incentive Plan portion of the Compensation Program are described in Section 5. Sections 1, 2, 3, 6, 7, and 8 of the Compensation Program relate to both the base salary portion and the Performance Incentive Plan portion except where otherwise specified in any such Section.

***Effective Date*: The original Compensation Program was effective September 1, 2000. It was amended and restated in its entirety effective September 1, 2004. This document amends and restates the Compensation Program with an “Effective Date” of July 1, 2006, except that (i) provisions of the Performance Incentive Plan relating to the further deferral of Nonvested Deferred Awards after they become vested are eliminated effective September 1, 2004, and (ii) provisions of the Performance Incentive Plan that are deleted, added, or modified to conform to, or exempt the plan from, section 409A of the Internal Revenue Code (Sections 5.6(a), 5.7(b)(4), 5.10(c), and 8.5) are effective January 1, 2005.**

2. COMPENSATION PROGRAM OBJECTIVES

UTIMCO’s Compensation Program serves a number of objectives:

- To attract and retain key investment and operations staff of outstanding competence and ability.
- To encourage key investment staff to develop a strong commitment to the performance of the assets for which UTIMCO has been delegated investment responsibility.
- To motivate key investment staff to focus on maximizing real, long-term returns for all funds managed by UTIMCO while assuming appropriate levels of risk.

- To facilitate teamwork so that members of UTIMCO operate as a cohesive group.

3. TOTAL COMPENSATION PROGRAM PHILOSOPHY

UTIMCO aspires to attract and retain high caliber employees from nationally recognized peer institutions and the investment management community in general. UTIMCO strives to provide a total compensation program that is competitive nationally, with the elements of compensation evaluated relative to comparably sized ~~University~~**university** endowments, foundations, in-house managed pension funds**,** and for-profit investment management firms with a similar investment philosophy (e.g., externally managed funds).

UTIMCO's total Compensation Program is positioned against the competitive market as follows:

- Base salaries are targeted at the market median (e.g., 50th percentile).
- Target total compensation (salary plus target Incentive Award Opportunity) is positioned at the market median.
- Maximum total compensation (salary plus maximum Incentive Award Opportunity) is targeted at the market 75th percentile if performance is outstanding. (For this purpose, 0 is the lowest point and 100 is the highest.)

Although base salaries**,** as well as target and maximum total compensation**,** have a targeted positioning relative to market, an individual employee's actual total compensation may vary from the targeted positioning based on the individual's experience, education, knowledge, skills**,** and performance as well as UTIMCO's investment performance as described in this document. Except as provided in ~~Section~~**Sections** 5.8 **and 5.9** for purposes of determining the length of historical performance, base salaries and Incentive Award Opportunities (as well as the actual Performance Incentive Awards) are not determined based on seniority at UTIMCO.

4. BASE SALARY ADMINISTRATION

4.1. Salary Structure

(a) Base salaries are administered through a Salary Structure as set forth in this Section 4.1. Each **employment** position has its own salary range, with the midpoint set approximately equal to the market median base salary for **employment** positions with similar job content and level of responsibility. In most cases, the salary range will be from 20% below the midpoint to 20% above the midpoint.

(b) The salary range midpoints will be determined by the Compensation Committee based on consultation with an outside compensation consultant and with UTIMCO management. Salary range midpoints for key management, investment**,** and operations positions will be updated at least every three years based on a salary benchmarking study conducted by a qualified compensation consultant selected by the Compensation Committee. In years in which the Compensation Committee does not commission a formal salary survey, the base salary midpoints may be adjusted at the Compensation Committee's discretion based on expected annual salary structure adjustments as reported in one or more published compensation planning surveys.

4.2. Salary Adjustments

(a) ~~Individual employees' base salaries are~~**The base salary of the President and CEO is** determined by the Board**, and the base salaries of the other key investment and operations employees are determined by the Compensation Committee**. Base salaries will be set within the salary range for each **employment** position. An individual's base salary within the range may be higher or lower than the salary range midpoint based on his or her level of experience, education, knowledge, skills**,** and performance. On an exception basis, the Board may set individual base salaries outside of the salary range if an individual either substantially exceeds or does not meet all of the market criteria for a particular position (e.g., recent promotion).

(b) Individuals may receive an annual adjustment (increase or decrease) of their base salaries at the discretion of the **Compensation Committee or, in the case of the President and CEO, at the discretion of the** Board. Base salary adjustments, if any, will be determined based on each ~~Participant~~**individual employee**'s experience, education, knowledge, skills**,** and performance. Employees are not guaranteed an annual salary increase.

5. PERFORMANCE INCENTIVE PLAN

5.1. Purpose of the Performance Incentive Plan ~~*and Effective Date*~~

~~(a)~~ The purpose of the Performance Incentive Plan is to provide ~~an~~ annual Performance Incentive ~~Award~~**Awards to eligible Participants** based on specific objective criteria relative to UTIMCO's and each Participant's performance. The primary objectives of the Performance Incentive Plan are outlined in Section 2.

~~(b) The Performance Incentive Plan restates and supercedes the UTIMCO Performance Compensation Plan, which was effective September 1, 2000 ("Prior Plan"). The effective date of this restated Performance Incentive Plan is September 1, 2004 (the "Effective Date").~~

5.2. Performance Period

(a) For purposes of the Performance Incentive Plan, the **"**Performance Period**"** begins on July 1 of each year and ends the following June 30.

(b) Except as otherwise provided under ~~Section~~**Sections** 5.8 and ~~Section~~ 5.9, performance for ~~a~~**each** year in the historical performance period will be measured between July 1 and the following June 30 of the applicable year for gauging achievement of the Entity and Asset Class Performance Goals.

5.3. Eligibility and Participation

(a) Each employee ~~(and only such an employee) who~~**of UTIMCO will be a "Participant" in the Performance Incentive Plan for a Performance Period if (and only if) he or she** is **both** (i) employed by UTIMCO in an **employment position that is designated as an** "Eligible Position" **for that Performance Period** and (ii) selected by the Board as eligible to participate in the Performance Incentive Plan ~~will become a "Participant."~~**for that Performance Period.** "Eligible Positions" **for a Performance Period** include senior management, investment staff, and other key positions as ~~determined from time to time~~**designated** by the President and CEO~~, subject to approval by the Board. Eligible Positions will be confirmed by the Board within the first 60 days~~ **and approved by the Board as Eligible Positions for that Performance Period. An employment position that is an Eligible Position in one Performance Period is not automatically an Eligible Position in any subsequent Performance Period, and each Eligible Position must be confirmed or reconfirmed by the Board as being an "Eligible Position" for the applicable Performance Period. Similarly, an employee who is eligible to participate in the Performance Plan in one Performance Period is not automatically eligible to participate in any subsequent Performance Period (notwithstanding that such employee may be employed in an Eligible Position in that subsequent Performance Period), and each employee must be designated or redesignated by the Board as being eligible to participate in the Performance Incentive Plan**

for the applicable Performance Period. The Board will confirm the Eligible Positions and designate the eligible employees who will become Participants for a Performance Period within the first 90 days of the Performance Period or, if later, as soon as administratively feasible after the start of the Performance Period. The Board in its discretion may also designate **the employment position of** a newly hired or promoted employee ~~to be in an Eligible Position during a Performance Period. An Eligible Position in one Performance Period is not automatically an Eligible Position in any subsequent Performance Period~~**as an "Eligible Position" and may designate such newly hired or promoted employee as eligible to participate in the Performance Incentive Plan for a Performance Period (or remainder of a Performance Period) within 30 days of such hire or promotion or, if later, as soon as administratively feasible after such hire or promotion**. A list of Eligible Positions for ~~the 2004/2005~~**each** Performance Period is set forth ~~on the table in Section 5.5(b).~~ **in Table 1, which is attached as Appendix C. Table 1 will be revised each Performance Period to set forth the Eligible Positions for that Performance Period as soon as administratively practicable after confirmation of such Eligible Positions by the Board for such Performance Period, and such revised Table 1 will be attached as Appendix C.**

(b) An employee in an Eligible Position who has been selected by the Board to participate in the **Performance Incentive** Plan will become a Participant ~~in the Plan~~ on the ~~latest~~**later** of (i) the date he or she is employed in an Eligible Position~~,~~ **or** (ii) the date he or she is selected by the Board to participate in the **Performance Incentive** Plan~~, or (iii) any later date as designated by the Board~~; provided, however, that ~~an employee may not commence participation in the Plan and first become a Participant during the last six months of any Performance Period~~**the Board in its discretion may designate any earlier or later date (but not earlier than such employee's date of hire and not later than such employee's date of termination of employment) upon which such employee will become a Participant, and such employee will instead become a Participant on such earlier or later date. The preceding notwithstanding**, except when compelling individual circumstances justify a shorter period of time and such circumstances are recorded in the minutes of a meeting of the Board~~. If~~, **an employee may not commence participation in the Performance Incentive Plan and first become a Participant** during the last six months of any Performance Period, **and, if** an employee ~~has been~~**is** selected by the Board to participate in the **Performance Incentive** Plan or becomes employed in an Eligible Position **during the last six months of any Performance Period**, participation **of such employee** in the **Performance Incentive** Plan will be delayed until the first day of the next Performance Period (assuming such employee is employed by UTIMCO in an Eligible Position on such date).

(c) An employee will cease to be a Participant in the **Performance Incentive** Plan on the earliest to occur of: (i) the date such employee is no longer employed in an Eligible Position; (ii) the date of termination of such employee's employment with UTIMCO for any reason (including voluntary and involuntary termination, death, and disability); (iii) the date of termination of the **Performance Incentive** Plan; (iv) the date such employee commences a leave of absence; (v) the date such employee begins participation in any other UTIMCO incentive program; (vi) the date the Board designates that such employee's employment position is not an Eligible Position **(or fails to designate the employee's employment position as an Eligible Position with respect to a Performance Period)**; or (vii) any date designated by the Board as the date on which such employee is no longer a Participant.

(d) Except as provided in Sections 5.10(b), (c), and (d), only **individuals who are** Participants **on the last day of a Performance Period** are eligible to receive Performance Incentive Awards under the Performance Incentive Plan **for that Performance Period**.

5.4. Performance Goals

(a) Within the first 60 days of each Performance Period, the President and CEO will recommend goals ("Performance Goals") for each Participant (other than the Performance Goals for the President and CEO, which are determined as provided in Section 5.4(c), and the Performance Goals for employees who are hired or promoted **later** during a Performance Period) subject to approval by the Compensation Committee within the first 90 days of the Performance Period. The President and CEO will also recommend Performance Goals for employees who are hired or promoted during the Performance Period and become Participants ~~(~~**at the time those employees are designated as Participants (with such Performance Goals** subject to confirmation by the Compensation Committee~~) at the time those employees are designated as Participants~~ **as soon as administratively feasible after such Performance Goals are recommended)**.

(b) There are three ~~types~~**categories** of Performance Goals:

(1) Entity Performance (~~i.e., performance of the Total Endowment Assets~~**described in Section 5.8(a)**)

(2) Asset Class Performance (~~e.g., US public equity, international equity, private capital, fixed income, etc.~~**described in Section 5.8(b)**)

(3) Individual Performance **(described in Section 5.8(c))**

Except for the President and CEO, Individual Performance Goals will be defined jointly by each Participant and his or her supervisor. These Individual Performance Goals will be ~~measurable~~**measured** and ~~subject to approval~~**approved** by the President and CEO ~~as well as~~**subject to approval**

by the Compensation Committee. Individual Performance Goals may be established in one or more of the following areas:

- Leadership
- Implementation of operational goals
- Management of key strategic projects
- Effective utilization of human and financial resources

(c) The President and CEO's Performance Goals will be determined and approved by the Board.

(d) Each Performance Goal ~~is assigned a weight as illustrated in the table in Section 5.5(b), which shows the weightings~~ for each Eligible Position **is assigned a weight** for the ~~2004/2005~~ Performance Period. For each Performance Period, the Compensation Committee will approve **(or adjust as it deems appropriate)** the weightings of the Performance Goals at the same time it approves the Performance Goals. **The weightings for each Eligible Position are set forth in Table 1, which is attached as Appendix C. Table 1 will be revised each Performance Period to set forth the weightings for the Eligible Positions for that Performance Period as soon as administratively practicable after such weightings are approved by the Compensation Committee for such Performance Period. Notwithstanding the identified weighting for an Eligible Position, the Compensation Committee may adjust the weightings (up or down) for any Participant for a Performance Period where it considers the assigned weighting for a Performance Goal to be inappropriate for such Participant because of his or her length of service with UTIMCO, his or her tenure in the respective Eligible Position, or his or her prior work experience. The weightings for the Performance Goals for each Performance Period are subject to approval by the Board.**

5.5. Incentive Award Opportunity Levels and Performance Incentive Awards

(a) At the beginning of each Performance Period, each ~~Participant~~**Eligible Position** is assigned an "Incentive Award Opportunity" for each Performance Goal~~. The~~ **for the Participants in that Eligible Position. Each** Incentive Award Opportunity is determined by the ~~Board~~**Compensation Committee (and subject to approval by the Board)** and is expressed as a percentage of base salary earned during the Performance Period. The Incentive Award Opportunities include a threshold, target, and maximum award for achieving commensurate levels of performance of the respective Performance Goal.

(b) Incentive Award Opportunities for ~~the 2004/2005~~**each** Performance Period are set forth in ~~the following table:~~ **Table 1, which is attached as Appendix C. Table 1 will be revised each Performance Period to set forth the**

Incentive Award Opportunities for that Performance Period as soon as administratively practicable after approval of the Incentive Award Opportunities by the Board for such Performance Period, and such revised Table 1 will be attached as Appendix C.

(c) Actual "Performance Incentive Awards" are the amounts that are actually awarded to Participants for the respective Performance Period. Actual Performance Incentive Awards will range from zero (if a Participant performs below threshold on all Performance Goals) to the maximum Incentive Award Opportunity (if a Participant performs at or above maximum on all Performance Goals) depending on performance relative to objectives. Awards are capped at maximum levels regardless of whether a Participant exceeds the stated maximum Performance Goals.

(d) Following the end of each Performance Period, the Compensation Committee will review the actual performance of each Participant against the Performance Goals of the respective Participant and determine the Participant's level of achievement of his or her Performance Goals. The Compensation Committee will seek, and may rely on, the independent confirmation of the level of Performance Goal achievement from an external investment consultant to evaluate Entity Performance and Asset Class Performance. The President and CEO will submit a written report to the Compensation Committee, which documents the Participant's performance relative to the Participant's Performance Goals set at the beginning of the Performance Period**,** and upon which the Compensation Committee may rely in evaluating the Participant's performance. The Board will determine the President and CEO's level of achievement relative to the President and CEO's Performance Goals.

(e) Performance Incentive Awards will be calculated for each Participant based on the percentage achieved of each Performance Goal, taking into account the ~~weighting~~**weightings** for the Participant's Entity Performance, Asset Class Performance, and Individual Performance Goals and each Participant's Incentive Award Opportunity. The ~~Compensation Committee will review all Performance Incentive Award calculations, based on the certification of its advisors, and submit its recommendations to the Board for approval.~~ **methodology for calculating Incentive Award Opportunities and Performance Incentive Awards is presented on Appendix A. Performance Incentive Awards will be interpolated in a linear fashion between threshold and target as well as between target and maximum.**

(f) ~~The methodology for calculating Incentive Award Opportunities and Performance Incentive Awards is presented in Appendix A.~~**Within 150 days following the end of a Performance Period, the Compensation Committee will review all Performance Incentive Award calculations, based on the certification of its advisors, and make any changes it deems appropriate. The Compensation Committee will submit its**

recommendations to the Board for approval. Subject to the provisions of Section 7.1, the Board will approve Performance Incentive Awards.

~~(g) Within 150 days following the end of a Performance Period, the Compensation Committee will review and make recommendations concerning Performance Incentive Awards to Participants whom it determines to have met or exceeded the performance benchmarks for the Performance Period. Subject to the provisions of 7.1(a), the Board will approve Performance Incentive Awards.~~

(g) ~~(h)~~ Following the approval of a Performance Incentive Award~~,~~ **by** the Board ~~will promptly notify~~**,** each Participant **will be notified** as to the amount, if any, of ~~the~~**his or her** Performance Incentive Award as well as the terms, provisions, conditions**,** and limitations of the Nonvested Deferred Award~~, if any~~ **portion of such Performance Incentive Award**.

5.6. Form and Timing of Payouts of Performance Incentive Awards

Approved Performance Incentive Awards will be paid as follows:

(a) Seventy percent of the Performance Incentive Award will be paid to the Participant ("Paid Performance Incentive Award") within 150 days of the completion of the Performance Period **(and in no event later than the 15th day of the third month following the later of (i) the last day of the calendar year in which the Performance Incentive Award is determined or (ii) the last day of the fiscal year of UTIMCO in which the Performance Incentive Award is determined)**, and

(b) ~~Thirty percent of the Performance Incentive Award will be treated as a "Nonvested Deferred Award" subject to the terms of Section 5.7 and paid in accordance with that Section.~~

Thirty percent of the Performance Incentive Award will be treated as a "Nonvested Deferred Award" subject to the terms of Section 5.7 and paid in accordance with that Section.

*5.7. **Nonvested** Deferred Awards*

(a) ~~Nonvested Deferred Awards will be credited to~~**For each Performance Period,** a hypothetical account on UTIMCO's books ~~in the individual Participants' names~~ ("Nonvested Deferred Award Account~~(s)") as~~**") will be established for each Participant. As** of the date that the corresponding Paid Performance Incentive ~~Awards are transmitted to Participants. For each~~**Award is paid to the Participant, each Participant's Nonvested Deferred Award for a** Performance Period~~, a~~ **will be credited to his or her** Nonvested Deferred Award Account ~~will be established for each Participant to which will be credited the Nonvested Deferred Award of such Participant for such Performance Period.~~ **established for that Performance Period; provided, however, that, in the case of any Participant who is not employed by UTIMCO on the date such Nonvested Deferred Award would be so credited to his or her Nonvested Deferred Award Account,**

such Nonvested Deferred Award will not be credited to such Participant's Nonvested Deferred Award Account but will instead be forfeited. The Nonvested Deferred Award Accounts will be credited (or debited) monthly with an amount equal to the net investment returns of the Total Endowment Assets ("Net Returns") for the month multiplied by the balance of the respective Participant's Nonvested Deferred Award Account(s) as of the last day of the month. When the Nonvested Deferred Award is initially credited to the Nonvested Deferred Award Account, the Nonvested Deferred Award Account will be credited (or debited) with Net Returns for the month of the initial credit of a Nonvested Deferred Award, but the Net Returns will be prorated to reflect the number of days of the month during which the amounts were credited to the Nonvested Deferred Award Account. Participants are not entitled to their Nonvested Deferred ~~Awards~~**Award Accounts** unless **and until** they become vested in those ~~awards~~**accounts in accordance with Section 5.7(b)**.

(b) Assuming **and contingent upon** continued employment with UTIMCO, except as provided in Section 5.10(c), **a Participant will become vested in, and entitled to payment of, his or her** Nonvested Deferred ~~Awards~~**Award Account** for each respective Performance Period ~~will vest and become payable~~ according to the following schedule:

(1) On the first anniversary of the ~~end~~**last day** of the Performance Period for which the Nonvested Deferred Award was earned, one third of the ~~Nonvested Deferred Award Account~~**amount** then credited to the Participant**'s Nonvested Deferred Award Account for that Performance Period** will be vested and paid to the Participant.

(2) On the second anniversary of the end of the Performance Period for which the Nonvested Deferred Award was earned, one half of the **amount then credited to the Participant's** Nonvested Deferred Award Account ~~then credited to the Participant~~**for that Performance Period** will be vested and paid to the Participant.

(3) On the third anniversary of the end of the Performance Period for which the Nonvested Deferred Award was earned, the remaining **amount then credited to the Participant's** Nonvested Deferred Award Account for that Performance ~~period then credited to the Participant~~**Period** will be vested and paid to the Participant.

~~(c) Notwithstanding the provisions of paragraphs (a) and (b) of this Section 5.7, upon execution of an "Election to Defer Payment of Vested Deferred Awards" form authorized by the Compensation Committee, a Participant may elect to defer payment of all or part of his or her Nonvested Deferred Awards that have become vested in accordance with Section 5.7(b) (including credited Net Returns) ("Vested Deferred Awards"). Such election must be made within 30 days prior to the date such amounts become vested. Vested Deferred Awards will be credited to a hypothetical account on UTIMCO's books in the individual~~

~~Participants' names ("Vested Deferred Award Account(s)") as of the date that such amounts become vested. Net Returns will be determined for each Vested Deferred Award Account at the end of each calendar year (or any earlier day in the calendar year on which the Participant terminates employment with UTIMCO) and will be allocated to a subaccount of the Participant's Vested Deferred Award Account ("Net Return Subaccount") established for the Participant each year. A Participant may elect to be paid all or any portion of his or her Vested Deferred Awards (but not amounts credited to his or her Net Return Subaccounts) allocated to his or her Vested Deferred Award Account at any time subject to reasonable administrative procedures established by UTIMCO; provided, however, that if the total balance of a Participant's Net Return Subaccounts is negative at the time he or she makes such an election, the Participant will not be able to withdraw more than the amount of his or her Vested Deferred Awards net of such negative balance. Any such Vested Deferred Awards elected to be withdrawn will be paid as soon as reasonably practicable after the Performance Measurement Date of the month during which the Participant makes the election. Each Net Return Subaccount of a Participant will be distributed to the Participant on the third anniversary of the date of allocation of such amounts to such subaccount, and the Participant will not be able to receive any amounts from his or her Net Return Subaccount prior to such time; provided, however, that if a Net Return Subaccount has a negative balance on such third anniversary, distribution of such subaccount will be made on the next following anniversary on which such Net Return Subaccount has a positive balance. Participants are responsible for all income tax consequences associated with Participant's Vested Deferred Award Account and Net Return Subaccounts.~~

~~(d) Notwithstanding the provisions of Section 5.7(c), each Participant who terminates employment with UTIMCO for any reason will be paid (or, in the case of a deceased Participant, his or her estate will be paid) the balance of his or her Vested Deferred Award Account, increased or decreased by the positive or negative balance of his or her Net Return Subaccounts. Such amounts will be paid as soon as reasonably practicable after the Performance Measurement Date of the month during which the Participant terminates employment with UTIMCO.~~

~~(e) Notwithstanding any provision of the Plan to the contrary, at any time prior to the time such amounts would otherwise be distributed under paragraphs (c) or (d) of this Section 5.7, the Board in its discretion may distribute to a Participant the balance of the Participant's Vested Deferred Award Account, increased or decreased by the positive or negative balance of his or her Net Return Subaccounts.~~

(4) Nonvested Deferred Award Accounts payable under the above paragraphs of this Section 5.7(b) will be paid as soon as administratively practicable after the applicable portion of any such Nonvested Deferred Award Account becomes vested and in no event later than the 15th day of the third month following the later of (i) the last day of the calendar year in which the applicable portion of such Nonvested Deferred Award Account becomes

vested or (ii) the last day of the fiscal year of UTIMCO in which the applicable portion of such Nonvested Deferred Award Account becomes vested.

5.8. ~~Performance Standards~~Performance Measurement Standards

(a) Entity Performance

(1) Entity Performance for purposes of the Performance Incentive Plan is the performance of the Total Endowment Assets~~. Entity Performance under the Performance Incentive Plan is based on performance relative to a Peer Group. Except as provided in Section 5.9, performance relative to the Peer Group will be measured based on 3-year rolling historical performance.~~ **(weighted at 85%) and the Intermediate Term Fund (weighted at 15%).**

(2) **The performance of the Total Endowment Assets is measured based on the TEA's performance relative to the Peer Group.** The Board's chosen investment advisor will determine the performance of the Peer Group annually for the Performance Period. **Performance of the Total Endowment Assets is measured net of fees, meaning performance is measured after factoring in all administrative and other fees incurred for managing the Total Endowment Assets.** The Board's investment advisor will calculate a percentile rank for ~~Entity Performance~~**the performance of the Total Endowment Assets** relative to the Peer Group, with the 100th percentile representing the highest rank, the 50th percentile representing the median**,** and the 0th percentile representing the lowest rank. ~~Threshold awards will be earned for reaching the 40th percentile, target awards will be earned for reaching the 60th percentile, and maximum awards will be earned for reaching the 75th percentile, with Performance Incentive Awards interpolated in a linear fashion between threshold and target as well as between target and maximum.~~

(3) The performance of the Intermediate Term Fund will be measured based on the performance of the ITF relative to the Policy Portfolio Return (benchmark). The performance standards related to the Intermediate Term Fund for the Performance Period beginning July 1, 2006, are reflected in Table 4 on Appendix D. Performance standards related to the ITF for each Performance Period beginning after June 30, 2007, will be set forth on a revised table for each such Performance Period and set forth on Appendix D as soon as administratively practicable after such standards are determined. Performance of the Intermediate Term Fund is measured net of fees, meaning performance is measured after factoring in all administrative and other fees incurred for managing the ITF.

(4) **Except as provided in Section 5.9, performance of the Total Endowment Assets and the Intermediate Fund will be measured based on a three-year rolling historical performance of each such fund.**

(b) Asset Class Performance

(1) ~~Except as provided in subparagraph~~**Asset Class Performance is the performance of specific asset classes within the Total Endowment Assets and the Intermediate Term Fund (such as US public equity, private capital, etc.) based on the standards set forth in this Section 5.8(b). Except as provided in paragraph** (2) below and Section 5.9, Asset Class Performance will be measured relative to the appropriate benchmark based on ~~3~~**three**-year rolling historical performance. Performance standards for each asset class will vary depending on the ability to outperform the respective benchmark. ~~The following table~~**Table 2 below** identifies the benchmarks for each asset class as well as threshold, target, and maximum performance standards~~.~~ ~~Performance Incentive Awards will be interpolated in a linear fashion between threshold and target as well as between target and maximum.~~ **for the Performance Periods ending June 30, 2003, 2004, and 2005 and includes July 2005 and August 2005. Table 3 below identifies the benchmarks for each asset class as well as threshold, target, and maximum performance standards beginning September 1, 2005, through the Performance Period ending June 30, 2006. The benchmarks for each asset class as well as threshold, target, and maximum performance standards for the Performance Period beginning July 1, 2006, will be set forth in Table 4, which is attached as Appendix D. The benchmarks for each asset class as well as threshold, target, and maximum performance standards for Performance Periods beginning after June 30, 2007, will be set forth in a revised table for each such Performance Period as soon as administratively practicable after such benchmarks and standards are set, and such revised table will be attached as Appendix D.**

TABLE 2 (7/1/04 through 8/31/05)

Asset Class	Benchmark	Policy Portfolio Weights (% of Portfolio)	Performance Standards Threshold	Target	Maximum
Entity: Peer goup	Peer group (Endowments w/ >$ 1 B assets)	n/a	40th %ile	60th %ile	75th %ile
US Public Equity	Russell 3000	20.0%	+0 bps	+31 bps	+62 bps
International Equity	MSCI All Country World Index, Ex US	17.0%	+0 bps	+52.5 bps	+105 bps
Fixed Income	Lehman Brothers Aggregate Bond Index	10.0%	+0 bps	+12.5 bps	+25 bps
Private Capital	Roll up of Private Equity & Venture Capital	15.0%			
Private Equity	Venture Economics Private Equity Database	--	+0 bps	+100 bps	+200 bps
Venture Capital	Venture Economics Venture Capital Database	--	+0 bps	+112.5 bps	+225 bps
Absolute Return Hedge Funds	91-Day T-Bill	15.0%	+300 bps	+350 bps	+400 bps
Equity Hedge Funds	91-Day T-Bill	10.0%	+400 bps	+465 bps	+530 bps
Inflation Hedge	Roll up of Commodities, TIPS & REITS	13.0%			
Commodities	Goldman Sachs Commodity Index	3.0%	-100 bps	-15 bps	+0 bps
TIPS	Lehman Brothers US TIPS Index	5.0%	+0 bps	+2.5 bps	+5 bps
REITS	Dow Jones Wishire Real Estate Securities Index	5.0%	+0 bps	+37.5 bps	+75 bps
Cash	91-Day T-Bill	0.0%	+0 bps	+0 bps	+0 bps
Short Intermediate Term Fund	SITF Policy Statement	--	+0 bps	+5 bps	+10 bps

TABLE 3 (9/1/05 through 6/30/06)

Asset Class	Benchmark	Policy Portfolio Weights (% of Portfolio)	Performance Standards Threshold	Target	Maximum
Entity: Peer Group	Peer group (Endowments w/>$1 B assets)	n/a	40th %ile	60th %ile	75th %ile
US Public Equity	Russell 3000 Index	20%	+0 bps	+31 bps	+62 bps
Non-US Developed Equity	MSCI EAFE Index with net dividends	10%	+0 bps	+37.5 bps	+75 bps
Emerging Markets Equity	MSCI Emerging Markets Index with net dividends	7%	+0 bps	+75 bps	+150 bps
Directional Hedge Funds	Combination index: 50% S&P Event-Driven Hedge Fund Index plus 50% S&P Directional/Tactical Hedge Fund Index	10%	+0 bps	+65 bps	+130 bps
Absolute Return Hedge Funds	Combination index: 66.7% S&P Event-Driven Hedge Fund Index plus 33.3% S&P Arbitrage Hedge Fund Index	15%	+0 bps	+50 bps	+100 bps
Private Equity	Custom Benchmark Created from Venture Economics Database	11%	+0 bps	+103.5 bps	+207 bps
Venture Capital	Custom Benchmark Created from Venture Economics Database	4%	+0 bps	+103.5 bps	+207 bps
REITS	Dow Jones Wilshire Real Estate Securities Index	5%	+0 bps	+37.5 bps	+75 bps
Commodities	Combination index: 66.7% Goldman Sachs Commodity Index minus .5% plus 33.3% DJ-AIG Commodity Index	3%	+0 bps	+17.5 bps	+35 bps
TIPS	Lehman Brothers US TIPS Index	5%	+0 bps	+2.5 bps	+5 bps
Fixed Income	Lehman Brothers Aggregate Bond Index	10%	+0 bps	+12.5 bps	+25 bps
Cash	90 day t-bills	0%	+0 bps	+0 bps	+0 bps
Short Intermediate Term Fund	SITF Policy Statement	--	+0 bps	+5 bps	+10 bps

(2) Performance for the private capital asset class is calculated differently ~~than~~**from** other asset classes due to its longer investment horizon and illiquidity of assets. Performance of the private capital asset class is determined based on the performance of partnership commitments made by the current private capital team since 2001 based on internal rates of return (IRR's) relative to the respective Venture Economics benchmarks.

(c) Individual Performance

Individual Performance **of each Participant** will be measured based on **that Participant's** performance **of the duties of his or her employment position** during the Performance Period.

5.9. ~~*Modification of Performance Standards for Newly Hired Employees*~~***Modifications of Measurement Period for Measuring Equity and Asset Class Performance Goals***

Although **generally** Entity Performance and most Asset Class Performance are measured based on three-year rolling historical performance, newly hired Participants will be phased into the **Performance Incentive** Plan so that Entity **Performance** and Asset Class Performance are measured over a period of time consistent with each Participant's tenure at UTIMCO. This provision ensures that ~~Participants are~~**a Participant is** measured and rewarded over a period of time consistent with **the period during** which ~~they~~**he or she** influenced the performance of the entity or a particular asset class. In the Performance Period in which a Participant begins participation in the **Performance Incentive** Plan, the Entity **Performance** and Asset Class Performance ~~component~~**components** of the Incentive Award Opportunity will be based on one full year of historical performance (i.e., the performance for the Performance Period during which the Participant commenced **Performance Incentive** Plan participation). During a Participant's second year of **Performance Incentive** Plan participation, the Entity **Performance** and Asset Class Performance ~~component~~**components** of the Incentive Award Opportunity will be based on two full years of historical performance. In the third year of a Participant's **Performance Incentive** Plan participation and beyond, the Entity and Asset Class Performance ~~component~~**components** of the Incentive Award Opportunity will be based on the three full years of rolling historical performance. This provision will apply to Participants who are ~~current~~ UTIMCO employees ~~and were~~ hired after July 1, 2001.

(a) **For purposes of measuring the Intermediate Term Fund component of Entity and Asset Class Performance, the three-year historical performance cycle will not be utilized until the Intermediate Term Fund has three years of historical performance as part of the Performance Incentive Plan and, until that time, the actual years of historical performance will be used as the measurement period. The Intermediate Term Fund was formed on February 1, 2006, and is added as a measurement of performance under the Performance Incentive Plan effective July 1, 2006. Therefore, as of June 30, 2007, the ITF will have one year of historical performance that will be measured for purposes of determining Equity and Asset Class Performance; as of June 30, 2008, the ITF will have two consecutive years of historical performance that will be measured for purposes of determining Equity and Asset Class Performance; and as of June 30, 2009, and for each Performance Period thereafter, three consecutive years of historical performance will be**

utilized for purposes of measuring the ITF prong of Equity and Asset Class Performance.

5.10. Termination Provisions

(a) Except as otherwise provided in this Section 5.10, any Participant who ceases to be a Participant (either because of termination of employment with UTIMCO or for any other reason stated in Section 5.3(c)) prior to the end of a Performance Period will not be eligible to receive payment of any Performance Incentive Award for that or any subsequent Performance Periods. In addition, a Participant will only continue to vest in Nonvested Deferred Awards while he or she is employed with UTIMCO and will forfeit any Nonvested Deferred Awards at termination of employment with UTIMCO.~~ Unless distributed earlier under the terms of the Plan and subject to Sections 7.6 and 7.8, all Vested Deferred Awards are payable at termination of employment in accordance with Section 5.7(d).~~

(b) If a Participant ceases to be a Participant in the **Performance Incentive** Plan under Section 5.3(c) prior to the end of a Performance Period because his or her employment position is no longer an Eligible Position (but such employee continues to be employed with UTIMCO), such Participant's Performance Incentive Award for the current Performance Period, if any, will be calculated on a prorated basis from the first day of the Performance Period to the Performance Measurement Date immediately preceding or, if applicable, coinciding with the date the Participant ceases to be in an Eligible Position, and such individual will not be entitled to any Performance Incentive Awards for any Performance Period thereafter (unless he or she again becomes a Participant in accordance with Sections 5.3(a) and (b)). All Nonvested Deferred Awards continue to vest **and be paid** subject to the provisions of Section 5.7(b).

(c) If a Participant ceases to be a Participant in the **Performance Incentive** Plan under Section 5.3(c) prior to the end of a Performance Period because his or her employment with UTIMCO terminates due to death or ~~disability (as defined in the Internal Revenue Code §22(e)(3))~~**Disability**, the Participant's Performance Incentive Award for the Performance Period in which termination occurs will be paid at target on a prorated basis from the first day of the Performance Period to the Performance Measurement Date immediately preceding or, if applicable, coinciding with the date of the Participant's death or ~~disability~~**Disability**, and such individual will not be entitled to any Performance Incentive Awards for any Performance Period thereafter (unless he or she again becomes a Participant in accordance with Sections 5.3(a) and (b)). All Nonvested Deferred ~~Awards~~**Award Accounts** will vest immediately and be paid **as soon as administratively practicable after such termination and in no event later than the 15th day of the third month following the later of (i) the last day of the calendar year in which such termination occurs or (ii) the last day of the fiscal year of UTIMCO in which such termination occurs**. Payments under this provision will be made to the estate or designated beneficiaries of the deceased Participant or to the disabled Participant, as applicable~~, in accordance with Section 5.7(d) within 60 days of the date of termination of employment.~~ **.**

(d) If a Participant ceases to be a Participant in the **Performance Incentive** Plan under Section 5.3(c) prior to the end of a Performance Period because he or she commences a ~~Compensation Committee-approved~~ leave of absence, such Participant's Performance Incentive Award for the current Performance Period, if any, will be calculated on a prorated basis from the first day of the Performance Period to the Performance Measurement Date immediately preceding or coinciding with the date the Participant commences such leave of absence, and such individual will not be entitled to any Performance Incentive Awards for any Performance Period thereafter (unless he or she again becomes a Participant in accordance with Sections 5.3(a) and (b)). **All Nonvested Deferred Awards continue to vest and be paid subject to the provisions of Section 5.7(b).**

(e) In the case of any Participant who ceases to be a Participant in the Performance Incentive Plan prior to the end of Performance Period and is entitled to a Performance Incentive Award or a prorated Performance Incentive Award under this Section 5.10, such Performance Incentive Award will be calculated at the time and in the manner provided in Section 5.5 and Appendix A and paid in accordance with Section 5.6 and will not be calculated or paid prior to such time.

6. ~~PLAN~~COMPENSATION PROGRAM AUTHORITY AND RESPONSIBILITY

6.1. Board as Plan Administrator

~~(a)~~ Except as otherwise specifically provided in this Compensation Program with respect to powers, duties, and obligations of the Compensation Committee, the Compensation Program will be administered by the Board.

6.2. Powers of Board

~~(b)~~ The Board has all powers **specifically vested herein and all powers** necessary or advisable to administer the ~~Plan~~**Compensation Program** as it determines in its discretion, including, without limitation, the authority to:

(1) Establish the conditions for the determination and payment of compensation by establishing the provisions of the Performance Incentive Plan.

(2) Select the employees who are eligible to be Participants **in the Performance Incentive Plan**.

~~(3) Subject to the terms of the Plan, determine the amount and timing of Performance Incentive Awards under the Plan.~~

~~(4) Establish the base salaries, Performance Incentive Opportunity Levels and Performance Incentive Awards.~~

(3) ~~(5)~~ Delegate to any other person, committee, or entity any of its ministerial powers and/or duties under the ~~Plan~~**Compensation Program** as long as any such delegation is in writing and complies with the UTIMCO Bylaws.

7. ~~PERFORMANCE INCENTIVE PLAN~~COMPENSATION PROGRAM INTERPRETATION

7.1. Board Discretion

(a) Consistent with the provisions of the ~~Plan~~**Compensation Program**, the Board has the discretion to interpret the ~~Plan~~**Compensation Program** and may from time to time adopt such rules and regulations that it may deem advisable to carry out the ~~Plan~~**Compensation Program**. All decisions made by the Board in selecting the Participants approved to receive Performance Incentive Awards, including the amount thereof, and in construing the provisions of the ~~Plan or~~**Compensation Program, including without limitation** the terms of any Performance Incentive Awards**,** are final and binding on all Participants.

(b) Notwithstanding any provision of the ~~Plan~~**Compensation Program to the contrary** and subject to the ~~requirements~~**requirement** that the approval of Performance Incentive Awards that will result in an increase of 5% or more in the total Performance Incentive Awards ~~calculating~~**calculated** using the methodology set out ~~in~~**on** Appendix A must have the prior approval of the U.T. System Board of Regents, the Board ~~shall have~~**has** the discretion and authority to make changes in the terms of the ~~Plan~~**Compensation Program** in determining a Participant's eligibility for, or amount of, a Performance Incentive Award for any Performance Period whenever it considers that circumstances have occurred during the Performance Period so as to make such changes appropriate in the opinion of the Board, provided**,** however, **that** any such change ~~shall~~**will** not deprive or eliminate ~~a Vested Deferred Award~~**an award** of a Participant **after it has become vested** and that such circumstances are recorded in the minutes of a meeting of the Board.

*7.2. Duration, Amendment**,** and Termination*

The Board ~~shall have~~**has** the right in its discretion to amend the ~~Plan~~**Compensation Program** or any portion thereof from time to time, to suspend it for a specified period, or to terminate it entirely or any portion thereof. However, if the **Performance Incentive** Plan is suspended or terminated during a Performance Period, Participants will receive a prorated Performance Incentive Award based on performance achieved and base salary earned through the

Performance Measurement Date immediately preceding such suspension or termination. The ~~Plan shall~~**Compensation Program will** be in effect until suspension or termination by the Board; provided, however, that if the Board so determines at the time of any suspension or termination **of the Performance Incentive Plan**, Nonvested Deferred Awards credited to Participants' Nonvested Deferred Award Account(s) as of the effective date of such suspension or termination will continue to be administered under the terms of the **Performance Incentive** Plan after any suspension or termination, except as the Board otherwise determines in its discretion at the time of such suspension or termination.

7.3. ~~Record Keeping~~Recordkeeping and Reporting

(a) All records for the Compensation Program ~~shall~~**will** be maintained by the Managing Director of Accounting, Finance**,** and Administration at UTIMCO. Relative performance data and calculations ~~shall~~**will** be reviewed by UTIMCO's external ~~investment consultant~~**auditor** before Performance Incentive Awards are finalized and approved by the Board.

(b) UTIMCO will provide all Participants with a comprehensive report of the current value of their respective Nonvested ~~and Vested~~ Deferred Award Account balances, including a complete vesting status of those balances, on at least a quarterly basis.

~~7.4.~~ *Continued Employment*

Nothing in the adoption of ~~this Plan~~**the Compensation Program** or the awarding of Performance Incentive Awards ~~shall~~**will** confer on any employee the right to continued employment with UTIMCO or affect in any way the right of UTIMCO to terminate his or her employment at any time.

~~7.5.~~ *7.5. Non-transferability of Awards*

Except for the rights of the estate or designated beneficiaries of Participants to receive payments, as set forth herein, Performance Incentive Awards under the ~~Plan~~**Performance Incentive Plan, including both the Paid Performance Incentive Award portion and the Nonvested Deferred Award portion,** are non-assignable and non-transferable and are not subject to anticipation, adjustment, alienation, encumbrance, garnishment, attachment**,** or levy of any kind. The preceding notwithstanding, the ~~Plan will pay a Vested Deferred Award~~**Compensation Program will pay any portion of a Performance Incentive Award that is or becomes vested** in accordance with an order that meets the requirements of a "qualified domestic relations order" as set forth in Section 414(p) of the *Internal Revenue Code* and Section 206(d) of ERISA.

~~7.6.~~ *7.6. Unfunded Liability*

(a) Neither the establishment of ~~this Plan~~**the Compensation Program**, the ~~awarding~~**award** of **any** Performance Incentive Awards~~, the creation of~~

~~Nonvested Deferred Awards Accounts~~, nor the creation of ~~Vested~~**Nonvested** Deferred Awards Accounts ~~shall~~**will** be deemed to create a trust. The ~~Plan shall~~**Compensation Program will** constitute an unfunded, unsecured liability of UTIMCO to make payments in accordance with the provisions of the ~~Plan.~~ **Compensation Program.** Any amounts set aside by UTIMCO to assist it in the payment of Performance Incentive Awards or other benefits under the ~~Plan~~**Compensation Program**, including without limitation, amounts set aside to pay for Nonvested Deferred Awards~~ and Vested Deferred Awards, shall~~**, will** be the assets of UTIMCO, and no Participant ~~shall~~**will** have any security or other interest in any assets of UTIMCO or the **U.T. System** Board of Regents ~~of The University of Texas System~~ by reason of the ~~Plan~~**Compensation Program**.

(b) Nothing contained in the ~~Plan shall~~**Compensation Program will** be deemed to give any Participant, or any personal representative or beneficiary, any interest or title to any specific property of UTIMCO or any right against UTIMCO other than as set forth in the ~~Plan~~**Compensation Program**.

~~7.7.~~ *7.7.* *Compliance with State and Federal Law*

No portion of the ~~Plan shall~~**Compensation Program will** be effective at any time when such portion violates an applicable state or federal law, regulation**,** or governmental order or directive.

~~7.8.~~ *7.8.* *Federal, State**,** and Local Tax and Other Deductions*

All Performance Incentive Awards under the ~~Plan shall~~**Compensation Program will** be subject to any deductions (1) for tax and withholding required by federal, state, or local law at the time such tax and withholding is due (irrespective of whether such Performance Incentive Award is deferred and not payable at such time) and (2) for any and all amounts owed by the Participant to UTIMCO at the time of payment of the Performance Incentive Award. UTIMCO ~~shall~~**will** not be obligated to advise an employee of the existence of the tax or the amount that UTIMCO will be required to withhold.

~~7.9.~~ *7.9.* *Prior Plan*

(a) ~~The Performance Incentive Plan restates and supercedes the Prior Plan.~~**Except as provided in the following paragraphs of this Section 7.9, this restatement of the Compensation Program amends and supersedes any prior version of the Compensation Program ("Prior Plan").**

(b) All nonvested deferred awards under ~~the~~**a** Prior Plan will retain the vesting schedule ~~defined~~**in effect** under the Prior Plan~~. However~~ **at the time such awards were allocated to the respective Participant's account. In all other respects**, as of the Effective Date, those nonvested deferred amounts will **(1)** be credited or debited with the Net Returns over the remaining deferral period in accordance with Section 5.7(a)~~. Nonvested deferred balances earned under the Prior Plan will~~ **and (2)** be subject to the terms and conditions for Nonvested Deferred Awards under the ~~Plan, except the vesting period which will remain the same as it was under the Prior Plan, and when such amounts become vested, they will be subject to the terms and conditions for Vested Deferred Awards under the Plan~~**Performance Incentive Plan as set forth in this restated document**.

8. DEFINITION OF TERMS

8.1. **Asset Class Performance** is the performance of specific asset classes within the Total Endowment Assets **and the Intermediate Term Fund** (such as US public equity, private capital, etc.) based on the standards set forth in Section 5.8(b)~~(1)~~.

8.2. **Board** is the UTIMCO Board of Directors.

8.3. **Compensation Committee** is the Compensation Committee of the UTIMCO Board of Directors.

8.4. **Compensation Program** is defined in Section 1.

8.5. Disability means a condition whereby a Participant either (i) is unable to engage in any substantial gainful activity by reason of a medically determinable physical or mental impairment that is expected either to result in death or to last for a continuous period of not less than 12 months or (ii) is, by reason of a medically determinable physical or mental impairment that is expected to last for a continuous period of not less than 12 months, receiving income replacement benefits for a period of not less than three months under a disability plan maintained or contributed to by UTIMCO for the benefit of eligible employees.

8.6. ~~8.5.~~ **Effective Date** is defined in Section ~~5.1(b).~~**1.**

8.7. ~~8.6.~~ **Eligible Position** is defined in Section 5.3(a).

8.8. ~~8.7.~~ **Entity Performance** represents the performance of the Total Endowment Assets **and the Intermediate Term Fund** (based on the **measurement** standards set forth in Section 5.8(a)).

8.9. ~~8.8. **Incentive Award Opportunity** is defined in Section 5.5(a).~~**Incentive Award Opportunity is defined in Section 5.5(a).**

8.10. Intermediate Term Fund or ITF is The University of Texas System ("U.T. System") Intermediate Term Fund established by the U.T. System Board of Regents as a pooled fund for the collective investment of operating funds and other intermediate and long-term funds held by the U.T. System institutions and U.T. System Administration. Performance of the Intermediate Term Fund is measured net of fees, meaning performance is measured after factoring in all administrative and other fees incurred for managing the Intermediate Term Fund.

8.11. ~~8.9.~~ **Net Returns** is the investment performance return of the Total Endowment Assets, net of fees. Net of fees factors in all administrative and other fees for managing the Total Endowment Assets. The net investment return will be calculated as follows:

$$\frac{\text{Permanent University Fund Beginning Net Asset Value}}{\text{Total Endowment Beginning Net Asset Value}} \times \text{Permanent University Fund Net Investment Return}$$

Plus

$$\frac{\text{General Endowment Fund Beginning Net Asset Value}}{\text{Total Endowment Beginning Net Asset Value}} \times \text{General Endowment Fund Net Investment Return}$$

8.12. ~~8.10.~~ **Nonvested Deferred Award** is defined in Section ~~5.6.~~**5.6(b).**

8.13. ~~8.11.~~ **Nonvested Deferred Award Account** is defined in Section 5.7(a).

8.14. ~~8.12.~~ **Paid Performance Incentive Award** is defined in Section 5.6(a).

8.15. ~~8.13.~~ **Participant** is defined in Section 5.3(a).

8.16. ~~8.14.~~ **Peer Group** is a peer group of endowment funds maintained by the Board's external investment advisor that is ~~composed~~**comprised** of all endowment funds with assets greater than $1 billion ~~at~~**on** the ~~beginning~~**last day** of each **of the three immediately preceding** Performance ~~Period~~**Periods** and ~~is~~ set forth on Appendix B~~, as such Appendix B is amended from time to time.~~ **; provided, however, that** Harvard University**'s endowment fund**, Yale University**'s endowment fund,** and Total Endowment Assets are excluded from ~~this peer group~~**the Peer Group**. The ~~peer group~~**Peer Group** will be updated ~~annually at the beginning of each Performance Period~~**from time to time as deemed appropriate by the Board**, and Appendix B will be amended accordingly.

8.17. ~~8.15.~~ **Performance Goals** are defined in Section 5.4.

8.18. ~~8.16.~~ **Performance Incentive Award** is the component of a Participant's total compensation that is based on specific performance goals and awarded as current income or deferred at the end of a Performance Period in accordance with Section 5 and Appendix A.

8.19. ~~8.17.~~ **Performance Incentive Plan** is **as** defined in Section **1 and described more fully in Section** 5.

8.20. ~~8.18.~~ **Performance Measurement Date** is the close of the last business day of the month.

8.21. ~~8.19.~~ **Performance Period** is defined in Section 5.2.

8.22. Policy Portfolio Return is the benchmark return for the Intermediate Term Fund policy portfolio and is calculated by summing the neutrally weighted index returns (percentage weight for each asset class multiplied by the benchmark return for the asset class) for the various asset classes in the Intermediate Term Fund portfolio for the Performance Period.

8.23. ~~8.20.~~ **Prior Plan** is ~~the UTIMCO Performance Compensation Plan, effective September 1, 2000.~~**defined in Section 7.9.**

8.24. ~~8.21.~~ **Salary Structure** is described in Section 4.1.

8.25. ~~8.22.~~ **Total Endowment Assets or TEA** means the combination of the Permanent University Fund and the General Endowment Fund, but does not include any other endowment funds monitored by UTIMCO such as the Separately Invested Fund. Performance of the Total Endowment Assets is measured net of fees, meaning performance is measured after factoring in all administrative and other fees incurred for managing the Total Endowment Assets.

~~8.23. **Vested Deferred Award** is defined in Section 5.7(c).~~

~~8.24. **Vested Deferred Award Account** is defined in Section 5.7(c).~~

Appendix A
~~UTIMCO Compensation Program~~

Performance Incentive Award Methodology
(for Performance Periods beginning on or after July 1, 2006)

I. Determine "Incentive Award Opportunities" for Each Participant[1]

~~1.~~ **Step 1.** Identify the weights to be allocated to each of the three Performance Goals for each Participant's Eligible Position. The weights vary for each Eligible Position **each Performance Period** and are set forth ~~on the chart in Section 5.5(b). For example, for the President and CEO,~~**in Table 1 on Appendix C for the applicable Performance Period. The total of the weights ascribed to the three Performance Goals must add up to 100% for each Participant. For example, Table 1 on Appendix C may reflect for a Performance Period for the President and CEO that** the weight allocated to the Entity Performance Goal is 70%, the weight allocated to the Asset Class Performance Goal is 0%, and the weight allocated to the Individual Performance Goal is 30%. ~~The total of the weights ascribed to the three Performance Goals must add up to 100% for each Participant.~~

~~2.~~ **Step 2.** Identify the percentage of base salary for the Participant's Eligible Position that determines the Performance Incentive Award for achievement of the Threshold, Target, and Maximum levels of the Performance Goals. The percentages vary for each Eligible Position **each Performance Period** and are set forth in ~~the chart in Section 5.5(b)~~**Table 1 on Appendix C for the applicable Performance Period**. For example, **Table 1 on Appendix C may show that for a Performance Period the applicable percentages for determining** the Performance Incentive Award for the President and CEO ~~is~~**are** 18% of his or her base salary for achievement of Threshold level performance of all three Performance Goals, 90% of his or her base salary for achievement of Target level performance of all three Performance Goals, and 180% of his or her base salary for achievement of Maximum level performance of all three Performance Goals.

~~3.~~ **Step 3.** Calculate the dollar amount of the **potential** Threshold, Target, and Maximum awards **(the "Incentive Award Opportunities")** for each Participant by multiplying the Participant's base salary for the Performance Period by the applicable percentage ~~in~~**(from** Step #2 above**)**. For example, assuming the President and CEO has a base salary of $~~450,000 for the year~~**495,000 for a Performance Period, based on the assumed**

[1] These Incentive Award Opportunities represent amounts that each Participant will be awarded if he or she achieves his or her Performance Goals at varying levels and are calculated at the beginning of each Performance Period **or, if later, the date such Participant commences participation in the Performance Incentive Plan**.

percentages set forth in Step 2 above, the President and CEO will be eligible for ~~an award of~~ a total **award** of $~~81,000~~**89,100** (18% of his or her base salary) if he or she achieves Threshold level performance of all three Performance Goals, $~~405,000~~**445,500** (90% of his or her base salary) if he or she achieves Target level performance of all three Performance Goals, and $~~810,000~~**891,000** (180% of his or her base salary) if he or she achieves Maximum level performance of all three Performance Goals.

~~4.~~ **Step 4.** Because a Participant may achieve different levels of performance in different Performance Goals and be eligible for different levels of awards for that achievement (e.g., he or she may achieve Target performance in the Entity Performance Goal and be eligible to receive a Target award for that goal and achieve Maximum performance in the Individual Performance Goal and be eligible to receive a Maximum award for that Performance Goal), it is necessary to determine the ~~dollar amount (the "~~Incentive Award Opportunity~~")~~ of the Threshold, Target, and Maximum award for each separate Performance Goal **(and, because achievement of the Equity Performance Goal is determined in part by achievement of the Total Endowment Assets and in part by achievement of the Intermediate Term Fund, a Threshold, Target, and Maximum Incentive Award Opportunity separately for the TEA and the ITF must be determined)**. This is done by multiplying the dollar amount of the Threshold, Target, and Maximum awards for the performance of all three Performance Goals calculated in Step ~~#~~3 above for the Participant by the weight allocated for that Participant to the particular Performance Goal~~. For example, as determined in Step #3 above, the President and CEO will receive a Performance Incentive Award of $405,000 if he or she achieves Target level performance of all three Performance Goals. This $405,000 is broken up per Performance Goal as follows: If the President and CEO achieves Target level performance in the Entity Performance Goal, he or she will be awarded $283,500 (his or her weight allocation of 70% for this Performance Goal multiplied by the $405,000), and if he or she achieves Target level performance in his or her Individual Performance Goal, he or she will be awarded $121,500 (his or her weight allocation of 30% for this Performance Goal multiplied by the $405,000). Note that, because no weight allocation is given to the President and CEO for the Asset Class Performance Goal, no amount of the $405,000 is allocated to the achievement of that Performance Goal.~~ **(and, further, by multiplying the Incentive Award Opportunity for the Equity Performance by the weight ascribed to achievement of the Total Endowment Assets (85%) and by the weight ascribed to achievement of the Intermediate Term Fund (15%)).**

~~5.~~ **Step 5.** After ~~Step #~~**Steps 3 and** 4 above ~~is~~**are** performed for each of the three levels of performance for each of the three Performance Goals, there will be ~~nine~~**12** different Incentive Award Opportunities for each Participant. For example, for the President and CEO (based on ~~a Base Salary of $450,000 for the year), the nine~~**an assumed base salary of $495,000, the assumed weights for the Performance Goals set forth in Step 1 above,**

and the assumed percentages of base salary for the awards set forth in Step 2 above), the 12 different Incentive Award Opportunities for achievement of the Performance Goals for the Performance Period are as follows:

Incentive Award Opportunities for President and CEO
(based on assumed base salary of $495,000)

Performance Goal~~/Weight~~	**Weight**	Threshold Level Award	Target Level Award	Maximum Level Award
Entity (~~70%~~**TEA v. Peer Group)**	**59.5% (.85 x .70)**	$~~56,700~~**53,015**	$~~283,500~~**265,073**	$~~567,000~~**530,145**
Entity (ITF v. Policy Portfolio Return)	**10.5% (.15 x .70)**	**$9,356**	**$46,778**	**$93,555**
Asset Class ~~(0%)~~	**0%**	$0	$0	$0
Individual ~~(30%~~	**30%**	$~~24,300~~**26,730**	$~~121,500~~ **133,650**	$~~243,000~~**267,300**
Total ~~(100%)~~	**100%**	$~~81,000~~**89,100** (18% of salary)	$~~405,000~~**445,500** (90% of salary)	$~~810,000~~**891,000** (180% of salary)

II. Calculate Performance Incentive Award for Each Participant

~~6.~~ ~~Determine~~**Step 6. Identify** the achievement ~~percentages~~**percentiles or achieved basis points** that divide the Threshold, Target, and Maximum levels for each Performance Goal. These divisions ~~are set forth in the chart in Section 5.8(b)(1)~~ for **the level of achievement of** the Entity and Asset Class Performance Goals~~. For example, as shown on the chart, achievement of the Entity Performance Goal in the 40th percentile is the Threshold performance level, achievement of the Entity Performance Goal in the 60th percentile is the Target performance level, and achievement of the Entity Performance Goal in the 75th percentile is the Maximum performance level. As shown on the chart, the achievement percentile for the Asset Class Performance Goal is based on the attained basis points for a particular type of investment. Thus the measurement of the level of achievement (i.e., Threshold, Target, or Maximum) for the Asset Class Performance Goal differs for each Participant depending on the assets under that Participant's investment control~~ **are set forth in the table for the applicable Performance Period (i.e., Table 2, Table 3, Table 4, or any later table set forth on Appendix D, as applicable)**. The measurement for the level of achievement (i.e., Threshold, Target, or Maximum) for the Individual Performance Goal is initially determined each Performance Period by the Participant's supervisor, if any, and then is approved (or adjusted) by the Compensation Committee as it deems appropriate in its discretion. If the Participant has no supervisor, the measurement for the level of achievement for the Individual Performance Goal is determined each Performance Period by the Compensation Committee. **The Board will determine the President and CEO's level of achievement relative to the President and CEO's Performance Goals.**

~~7.~~ **Step 7.** Determine the percentile **or basis points** achieved ~~of~~**for** each ~~of the~~ Performance ~~Goals~~**Goal** for each Participant using the standards set forth in Sections 5.5 and 5.8 of the ~~Plan~~**Compensation Program**, as modified in the case of new hires in Section 5.9. **Determine the level of achievement of each Participant's Individual Performance Goal.**

~~8. Calculate the amount of each Participant's award attributable to each Performance Goal by determining the Incentive Award Opportunity amount for the applicable percentile of the Participant's level of achievement for each Performance Goal as determined in Step #4 and Step #5 above. That is, achievement of the Entity Performance Goal in the 40th percentile is the Threshold performance level and merits a Threshold level award, achievement in the 60th percentile is the Target performance level and merits a Target level award, and achievement in the 75th percentile is the Maximum performance level and merits a Maximum level award. For example, if the President and CEO achieved 100% of his or her Individual Performance Goal, he or she would have earned an award of $243,000 (Maximum award) for that Performance Goal for the Performance Period, and if the Entity Performance Goal of the 40th percentile is achieved, he or she would have~~

~~earned an award of $56,700 (Threshold award) for that Performance Goal for the Performance Period.~~

~~9.~~ **Step 8. Calculate the amount of each Participant's award attributable to each Performance Goal by identifying the Incentive Award Opportunity amount for each Performance Goal (e.g., as assumed and set forth for the President and CEO in the table in Step 5 above) commensurate with the Participant's level of achievement for that Performance Goal (determined in Steps 6 and 7 above).** An award for achievement percentiles in between the stated Threshold, Target, and Maximum levels is determined by linear interpolation. For example, if the ~~54~~**65**th percentile **of the Total Endowment Assets portion** of the Entity Performance Goal has been achieved, ~~it~~**that percentile** is between the ~~Threshold (40~~**Target (60**th percentile) and the ~~Target (60~~**Maximum (75**th percentile) levels~~. To~~**, so to** determine the amount of the award attributable to ~~a 54~~**the 65**th percentile achievement **of the TEA portion** of the Entity Performance Goal, perform the following steps: (i) subtract the difference between the dollar ~~amount~~**amounts** of the ~~Threshold and~~ Target **and Maximum** Incentive Award Opportunities for the Participant (e.g., for the President and CEO, as illustrated in the ~~above~~ table~~,~~ **in Step 5,** the difference is $~~226,800 ($283,500 - $56,700~~**265,072 ($530,145-$265,073**)); (ii) divide ~~14~~**5** (the percentile difference between the ~~Threshold~~**Target** level of ~~40~~**60**th percentile and the attained level of ~~54~~**65**th percentile) by ~~20~~**15** (the percentile difference between the ~~Threshold level and the Target level)~~**Target level and Maximum level) to get the fraction 5/15 to determine the pro rata portion of the difference between Target and Maximum actually achieved**; (iii) multiply the amount determined in the preceding Step (i) by the ~~percentage~~**fraction** determined in the preceding Step (ii)~~;~~ **($265,072 x 5/15 = $88,357); and** (iv) add the amount determined in the preceding Step (iii) to the ~~Threshold~~ **Target** Incentive Award Opportunity for the Participant to get the actual award for the Participant attributable to each Performance Goal~~.~~ **($88,357 + $265,073 = $353,430).**

Step 9. In determining the award attributable to the Equity Performance Goal, achievement of the Total Endowment Assets portion of the Entity Performance Goal (and the commensurate award) is weighted at 85% (and then multiplied by the weight assigned to the Entity Performance Goal for the Participant), and achievement of the Intermediate Term Fund portion of the Equity Performance Goal (and commensurate award) is weighted at 15% (and then multiplied by the weight assigned to the Entity Performance Goal for the Participant). For example, assuming a base salary of $495,000, if the President and CEO achieved the Target level (60th percentile) of the Total Endowment Assets portion of the Entity Performance Goal and achieved the Maximum level (+65 bps) of the Intermediate Term Fund portion of the Entity Performance Goal, he or she would have earned an award of $358,628 for his or her level of achievement of the Equity Performance Goal as follows: $265,073 for Target level of achievement of the TEA portion of the Equity Performance Goal (.85 x .70 x $445,500); plus $93,555 for

Maximum level of achievement of the ITF portion of the Equity Performance Goal (.15 x .70 x 891,000).

~~10.~~ Step 10. No award is given for an achievement percentile below Threshold, and no award above the Maximum award is given for an achievement percentile above the Maximum level. ~~For example, if the 38th percentile of the Entity Performance Goal has been achieved for the Performance Period, no award is given for that Performance Goal. If the 85th percentile of the Entity Performance Goal has been achieved for the Performance Period, no award in excess of the Maximum Incentive Award Opportunity for that goal is given.~~

~~11. Add~~Step 11. Subject to any applicable adjustment in Step 12 below, add the awards determined in ~~Step #~~Steps 8 and~~/or Step #~~ 9 above for each Performance Goal (as modified by Step 10) together to determine the total amount of the Participant's Performance Incentive Award for the Performance Period.

Step 12. In the case of any Participant who becomes a Participant in the Performance Incentive Plan after the first day of the applicable Performance Period, such Participant's Performance Incentive Award (determined in Step 11) will be prorated to reflect the actual portion of the Performance Period in which he or she was a Participant. In the case of a Participant who ceases to be a Participant prior to the end of a Performance Period, his or her entitlement to any Performance Incentive Award is determined under Section 5.10 and, in the case of such entitlement, such Participant's Performance Incentive Award, if any, will be prorated and adjusted as provided in Section 5.10.

~~APPENDIX~~Appendix B

UTIMCO ~~PEER GROUP~~Peer Group

- Brown University
- California Institute of Technology
- Case Western Reserve University
- Columbia University
- Cornell University
- Dartmouth College
- Duke University
- Emory University
- Grinnell College
- Johns Hopkins University
- Massachusetts Institute of Technology
- New York University
- Northwestern University
- Ohio State University and Foundation
- Princeton University
- Purdue University
- Rice University
- Stanford University
- The Rockefeller University
- The Texas A&M University System and Foundations
- UNC at Chapel Hill and Foundations
- University of California
- University of Chicago
- University of Michigan
- University of Minnesota and Foundation
- University of Notre Dame
- University of Pennsylvania
- University of Pittsburgh
- University of Rochester
- University of Southern California
- University of Virginia
- University of Washington
- Vanderbilt University
- Washington University
- Wellesley College
- Williams College

Source: Cambridge Associates. Represents University endowments (excluding Harvard, Yale, and Total Endowment Assets) with total assets in excess of $1 billion as of each fiscal year end June ~~2003.~~**2003, 2004, 2005.**

Appendix C

Eligible Positions
Weightings
Incentive Award Opportunities for each Eligible Position
(for each Performance Period)

TABLE 1 (2005/2006 Performance Period)

Eligible Position	Weighting: Entity	Weighting: Asset Class	Weighting: Individual	Incentive Award Opportunity (% of Salary): < Threshold	Threshold	Target	Maximum
		Investment Professionals					
President, CEO & CIO	70%	0%	30%	0%	18%	90%	180%
Deputy CIO & MD of Marketable Alt. Invest.	40%	40%	20%	0%	13%	65%	130%
Risk Manager	70%	0%	30%	0%	12%	60%	120%
MD, Public Markets Invest.	20%	60%	20%	0%	12%	60%	120%
MD, Inflation Hedging Assets	20%	60%	20%	0%	12%	60%	120%
Co-MD, Non-Marketable Alt Inv (n=2)	30%	50%	20%	0%	12%	60%	120%
Manager of Operating Fund Investments	20%	60%	20%	0%	10%	50%	100%
Portfolio Manager, Equity Invest.	20%	60%	20%	0%	10%	50%	100%
Sr. Portfolio Mgr., Fixed Income Invest.	20%	60%	20%	0%	10%	50%	100%
Portfolio Manager, Fixed Income Invest.	20%	60%	20%	0%	10%	50%	100%
Analytical Support-Investment	20%	60%	20%	0%	5%	25%	50%
Analytical Support-Risk Management	70%	0%	30%	0%	5%	25%	50%
		Operations/Support Professionals					
MD, Accounting, Finance & Admin.	20%	0%	80%	0%	10%	50%	100%
MD, Information Technology	20%	0%	80%	0%	10%	50%	100%
Manager, Finance & Administration	20%	0%	80%	0%	5%	25%	50%
Manager, Investment Reporting	20%	0%	80%	0%	5%	25%	50%
Manager, Portfolio Accounting & Ops.	20%	0%	80%	0%	5%	25%	50%

UPDATED TABLE 1 (For the Performance Periods beginning after June 30, 2006)

Eligible Position	Weighting: Entity	Weighting: Asset Class	Weighting: Individual	Incentive Award Opportunity (% of Salary): < Threshold	Threshold	Target	Maximum
		Investment Professionals					
President, CEO & CIO	70%	0%	30%	0%	20%	100%	200%
Deputy CIO & MD of Marketable Alt. Invest.	40%	40%	20%	0%	18%	90%	190%
Risk Manager	70%	0%	30%	0%	18%	90%	190%
MD, Public Markets Invest.	20%	60%	20%	0%	18%	90%	190%
MD, Inflation Hedging Assets	20%	60%	20%	0%	18%	90%	190%
MD, Non-Marketable Alt Inv	30%	50%	20%	0%	18%	90%	190%
Sr. Portfolio Mgr., Fixed Income Invest.	20%	60%	20%	0%	10%	50%	140%
Portfolio Manager, Fixed Income Invest.	20%	60%	20%	0%	10%	50%	140%
Director, Public Markets	20%	60%	20%	0%	8%	40%	80%
Director, Marketable Alternative	20%	60%	20%	0%	8%	40%	80%
Director, Inflation Hedging Assets	20%	60%	20%	0%	8%	40%	80%
Director, Non-Marketable Alternative	20%	60%	20%	0%	8%	40%	80%
Director, Risk Management	70%	0%	30%	0%	8%	40%	80%
Associate, Public Markets	20%	60%	20%	0%	6%	30%	70%
Associate, Marketable Alternative	20%	60%	20%	0%	6%	30%	70%
Associate, Inflation Hedging Assets	20%	60%	20%	0%	6%	30%	70%
Associate, Non-Marketable Alternative	20%	20%	60%	0%	6%	30%	70%
Associate, Risk Management	70%	0%	30%	0%	6%	30%	70%
Analyst, Public Markets	20%	60%	20%	0%	6%	30%	50%
Analyst, Marketable Alternative	20%	60%	20%	0%	6%	30%	50%
Analyst, Inflation Hedging Assets	20%	60%	20%	0%	6%	30%	50%
Analyst, Non-Marketable Alternative	20%	20%	60%	0%	6%	30%	50%
Analyst, Risk Management	70%	0%	30%	0%	6%	30%	50%
		Operations/Support Professionals					
MD, Accounting, Finance & Admin.	20%	0%	80%	0%	10%	50%	140%
MD, Information Technology	20%	0%	80%	0%	10%	50%	140%
Manager, Finance & Administration	20%	0%	80%	0%	8%	40%	80%
Manager, Investment Reporting	20%	0%	80%	0%	8%	40%	80%
Manager, Portfolio Accounting & Ops.	20%	0%	80%	0%	8%	40%	80%
Manager, Client Services	20%	0%	80%	0%	8%	40%	80%

Appendix D

Benchmarks for Asset Class
Threshold, Target, and Maximum Performance Standards
(for Performance Periods beginning on or after July 1, 2006)

Performance Standards for Intermediate Term Fund
(for Performance Periods beginning on or after July 1, 2006)

TABLE 4 (7/1/06 through 6/30/07)

		Policy Portfolio Weights		Performance Standards		
		Total Endowment Assets	ITF			
Asset Class	**Benchmark**	**(% of Portfolio)**	**(% of Portfolio)**	**Threshold**	**Target**	**Maximum**
Entity: Peer Group (Total Endowment Funds)	Peer group (Endowments w/>$1 B assets)	n/a	n/a	40th %ile	60th %ile	75th %ile
Entity: Benchmark (Intermediate Term Fund)	Policy Portfolio	n/a	n/a	+0 bps	+32.5 bps	+65 bps
US Public Equity	Russell 3000 Index	20%	15%	+0 bps	+31 bps	+62 bps
Non-US Developed Equity	MSCI EAFE Index with net dividends	10%	5%	+0 bps	+37.5 bps	+75 bps
Emerging Markets Equity	MSCI Emerging Markets Index with net dividends	7%	5%	+0 bps	+75 bps	+150 bps
Directional Hedge Funds	Combination index: 50% S&P Event-Driven Hedge Fund Index plus 50% S&P Directional/Tactical Hedge Fund Index	10%	12.5%	+0 bps	+65 bps	+130 bps
Absolute Return Hedge Funds	Combination index: 66.7% S&P Event-Driven Hedge Fund Index plus 33.3% S&P Arbitrage Hedge Fund Index	15%	12.5%	+0 bps	+50 bps	+100 bps
Private Equity	Custom Benchmark Created from Venture Economics Database	11%	0%	+0 bps	+103.5 bps	+207 bps
Venture Capital	Custom Benchmark Created from Venture Economics Database	4%	0%	+0 bps	+103.5 bps	+207 bps
REITS	Dow Jones Wilshire Real Estate Securities Index	5%	10%	+0 bps	+37.5 bps	+75 bps
Commodities	Combination index: 66.7% Goldman Sachs Commodity Index minus .5% plus 33.3% DJ-AIG Commodity Index	3%	5%	+0 bps	+17.5 bps	+35 bps
TIPS	Lehman Brothers US TIPS Index	5%	10%	+0 bps	+2.5 bps	+5 bps
Fixed Income	Lehman Brothers Aggregate Bond Index	10%	25%	+0 bps	+12.5 bps	+25 bps
Cash	90 day t-bills	0%	0%	+0 bps	+0 bps	+0 bps

15. U. T. System Board of Regents: Approval of the Annual Budget, including the capital expenditures budget, and Annual Fee and Allocation Schedule for The University of Texas Investment Management Company (UTIMCO)

RECOMMENDATION

The University of Texas Investment Management Company (UTIMCO) Board of Directors recommends that the U. T. System Board of Regents approve the proposed Annual Budget as set forth on Page 100, the capital expenditures budget as set forth on Page 103, and the Annual Fee and Allocation Schedule for the fiscal year ending August 31, 2007, as set forth on Page 104.

BACKGROUND INFORMATION

A proposed Annual Budget of $56.7 million for Fiscal Year 2007 was approved by actions of the UTIMCO Board on July 13, 2006, and July 25, 2006. The proposed Budget is an increase of $8.1 million or 16.8% from the approved Fiscal Year 2006 Budget. The majority of the increase relates to a budgeted increase in external management fees. The capital expenditures budget totaling $167,000 is presented separately with the total Annual Budget. The proposed Budget includes increased budgeting for incentive performance award opportunities approved by the UTIMCO Board on July 25, 2006.

The proposed Annual Fee and Allocation Schedule on Page 104 allocates proposed budgeted expenses among U. T. System funds, to be paid quarterly.

Background materials prepared by UTIMCO President, Chief Executive Officer, and Chief Investment Officer Bob Boldt are on Pages 99 - 103.

The U. T. System Investment Oversight staff Fiscal Year 2007 UTIMCO Budget Review is on Pages 105 - 119 and the Total Investment Management Cost Analysis is on Pages 120 - 123.

Budget materials prepared by UTIMCO

UTIMCO Budget Analysis and Recommendation

The Investment Management Services Agreement between the U. T. Board of Regents and UTIMCO requires that UTIMCO submit its annual operating budget, capital budget and management fee schedule to the Board of Regents for approval. The Total Operating Budget consists of UTIMCO's management fee (the UTIMCO Services Budget) plus the budget for the direct expenses to the Funds, the Direct Funds Budget.

As indicated above, the UTIMCO related operating budget for management of the endowment and operating funds is comprised of two distinct elements. The "UTIMCO Services Budget" provides for all expenses directly associated with UTIMCO operations including staff compensation and benefits, general operating expenses such as travel and computer equipment, office expenses, and professional fees including general legal and accounting expenses. The "Direct Funds Budget" provides for all expenses directly related to the external management of assets of the endowment and operating funds. These expenses include external management fees, custodian fees, analytical resources expenses, general consulting expenses (including Cambridge Associates), and individual investment related legal and accounting expenses. The sum of the UTIMCO Services Budget and the Direct Funds Budget equals the Total Budget for the August 2007 fiscal year. Fiscal year 2007's budget reflects a full year of expenses related to the Intermediate Term Fund, the new investment pool created to manage U. T. System's operating funds.

UTIMCO management has direct control of the UTIMCO Services budget and expenses. The Services budget is developed through a decentralized process with each Managing Director having some level of budgetary responsibility. Actual expense performance relative to the budget is an element of the qualitative performance compensation review for each Managing Director and Manager at UTIMCO.

In contrast, because the Direct Funds expenses are affected significantly by price changes in the capital markets and by the level of activity in external manager accounts operating under full discretion, UTIMCO management has only limited control of the Direct Funds Budget and expenses. UTIMCO control is limited to selecting the types of external managers to be hired (active versus passive or partnership versus agency account, for example) and negotiating the best and most advantageous contract terms. Although the performance of actual Direct Fund expenses relative to budget is not a part of qualitative incentive compensation considerations for UTIMCO management, because all Services and Direct Funds expenses reduce the net returns earned by the endowment and operating funds, UTIMCO management has clear incentive to manage Direct costs so as to maximize net investment returns. Note that this does not necessarily mean that attempting to minimize Direct (or Services) costs is the best approach. What is important both to UTIMCO management and the funds is maximizing net returns.

In addition, UTIMCO is required to submit annually its capital expenditures budget. This is a new requirement added to the Master Investment Management Services Agreement between the U. T. System Board of Regents and the UTIMCO Board of Directors. The amount of the capital expenditures budget is included in the annual budget amount but is provided separately.

On July 13, 2006, the UTIMCO Board of Directors unanimously approved the proposed UTIMCO's 2006-2007 Operating Budget, Capital Budget, and Management Fee Schedule, with the acknowledgment that the bonus compensation of the UTIMCO Services Budget would be further reviewed by the UTIMCO Board at a special called meeting. This special called meeting was held July 25, 2006, and the proposed budget includes the effect of the UTIMCO Board's approval of the bonus compensation at its July 25, 2006 meeting. These recommended Fiscal Year 2006-2007 UTIMCO Services and Direct Funds Budget totals are presented below:

Budget Comparisons	Fiscal Year 2006-2007 Budget	Fiscal Year 2005-2006 Budget	Increase (Decrease)	% Change
UTIMCO Services	$ 13,272,068	$ 11,434,302	$ 1,837,766	16.1%
Direct Costs to Funds	43,419,269	37,111,691	6,307,578	17.0%
Total Proposed Budget	$ 56,691,337	$ 48,545,993	$ 8,145,344	16.8%
As a Percent of Assets Managed	0.293%	0.277%	0.016%	

With this overview of the recommended budgets, the following sections focus on the UTIMCO Services and Direct Funds Budgets separately. In addition, a new section related to the capital budget request is included.

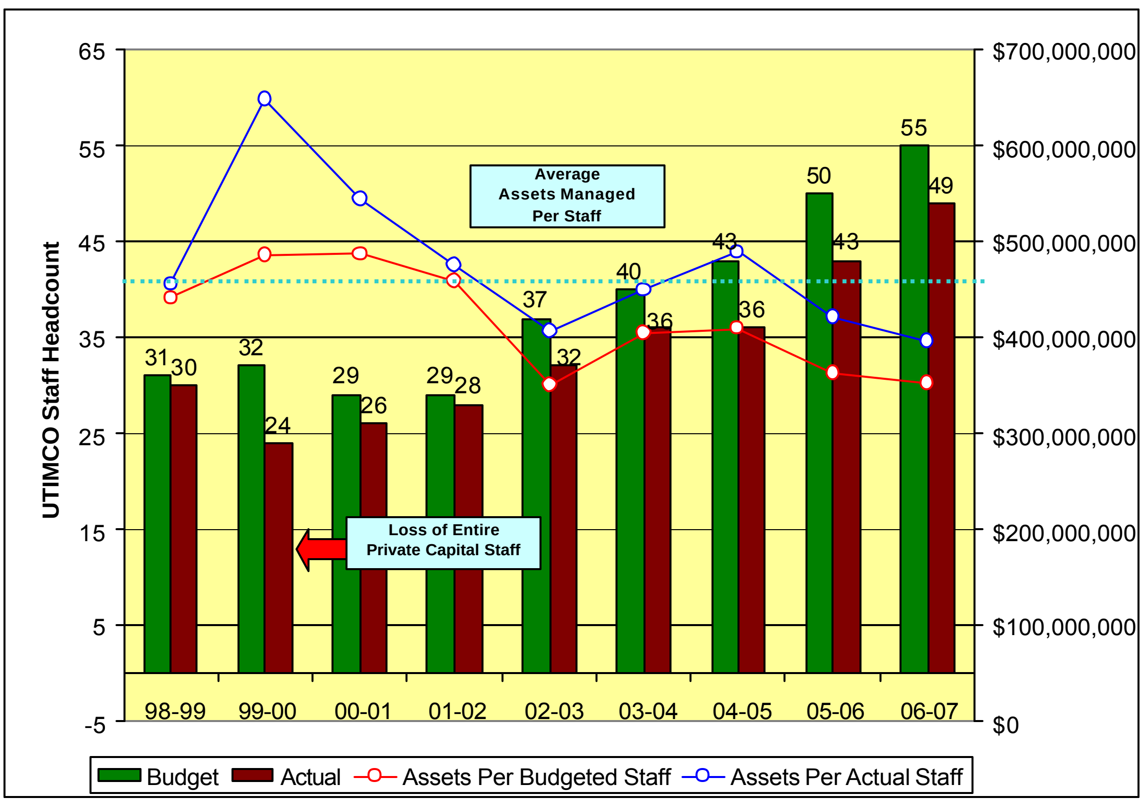
UTIMCO Services Budget

The primary items affecting the increase in the UTIMCO Services budget are salary increases for existing staff and new additions to the staff and lease costs.

Salary Increases for Existing Staff: UTIMCO's compensation policy is to pay competitive base salaries. Competitive base salaries are defined to be salaries within a plus or minus 20% band centered on the market median salary for a similar position in an endowment fund or investment management organization. UTIMCO's Compensation Committee selected Mercer Human Resource Consulting (Mercer) as UTIMCO's compensation consultant. The Compensation Committee hired Mercer to provide competitive compensation information for key management, investment, and operations positions based on a benchmarking study. Salary levels for other staff positions are based on local competition in similar organizations. Overall staff salaries increased by 4.6%. However, the Mercer survey indicated that potential incentive compensation at UTIMCO lagged those of its competition, and adjustments were warranted. As a result of these adjustments, budgeted incentive compensation increased 39.9% versus the calculations under the prior plan. The Compensation Committee of the UTIMCO Board reviewed and approved the staff salaries of the eligible compensation plan participants and potential incentive awards included in the budget request. The UTIMCO Board considered and approved the recommended salary for the President and Chief Executive Officer of UTIMCO.

New Additions to Staff: Four new positions were added to the staff. Two staff positions are being added to the Public Markets area. One is an analyst for assisting with the research, analysis, and recommendation of active managers and investment ideas that will facilitate the growth and success of the Intermediate Term Fund. The second position is a senior quantitative analyst dedicated to specifically research, synthesize, and structure potential internally managed investments on behalf of the U. T. endowments. Two additional staff positions are being added to the Accounting, Finance and Administration area. One position is devoted to compliance. This position was recommended by the U. T. System Audit Office and the duties and responsibilities include updating of the investment risk assessment and testing, development and updating of compliance policies, monitoring compliance of investment policies and investment guidelines, and compliance with external manager contracts. These functions are currently performed by accounting staff in addition to their full time accounting responsibilities. The second position is an administrative assistant position to provide advance word processing and computer skills necessary to prepare and maintain the various accounting and performance reports, including the financial statements for the funds.

Although the budgeted headcount has increased substantially since the ebb in Fiscal Year 2000, current and projected assets managed per staff are near the long term average indicated by the dashed line in the figure below:



The increase in staff count from 2000 is due to two factors: first, 2000 was an artificially low starting point, the staff was dangerously thin after the loss of the Private Capital team, necessitating a multimillion dollar payment to Cambridge Associates to monitor existing investments; and second, our current high return potential, specialist structure requires both a more experienced and larger team to monitor the more sophisticated investments we need to make to earn high value added returns.

Lease Fees: Lease fees increased due to the lease costs in the new facility, where we had limited lease costs in the current fiscal year because we negotiated free occupancy in the new lease agreement.

Direct Funds Budget

The details of the Direct Funds Budget are shown below:

Direct Funds Budget	Fiscal Year 2006-2007 Budget	Fiscal Year 2005-2006 Budget	Increase (Decrease)	% Change
External Base Management Fees	$ 16,847,098	$ 20,421,000	$ (3,573,902)	-17.5%
External Performance Management Fees	20,585,849	10,391,371	10,194,478	98.1%
Total External Management Fees	37,432,947	30,812,371	6,620,576	21.5%
Custodian Fees	1,260,072	2,356,175	(1,096,103)	-46.5%
Performance Measurement	530,599	621,169	(90,570)	-14.6%
Analytical Tools	386,700	289,570	97,130	33.5%
Risk Measurement	850,000	803,121	46,879	5.8%
Total Custodian and Analytical Costs	3,027,371	4,070,035	(1,042,664)	-25.6%
Consultant Fees	1,356,000	1,100,000	256,000	23.3%
Auditing	205,000	213,920	(8,920)	-4.2%
Controls Assessment (Sarbanes Oxley)	124,000	136,500	(12,500)	-9.2%
Printing	182,250	150,665	31,585	21.0%
Bank fees	-	6,000	(6,000)	-100.0%
Legal Fees	985,000	555,000	430,000	77.5%
Background Searches & Other	106,700	67,200	39,500	58.8%
Total Other Expenses	2,958,950	2,229,285	729,665	32.7%
Total Direct Costs to Funds	$ 43,419,267	$ 37,111,690	$ 6,307,576	17.0%
As a Percent of Average Assets	0.224%	0.211%	0.013%	

As indicated earlier in the overview of the entire budget, the total Direct Funds Budget is expected to expand 17.0% on a dollar basis and increase slightly as a percentage of Assets Managed. Other key points to note:

- The increase in the External Management fees of $6,620,576 is more than the total increase of the direct costs. The increase is related to three factors: 1) The budgeted amount has increase because of the ITF's existence for the full budget year. The prior budget only had a partial year estimate for these expenses; 2) With the departure of the REITS Internal Manager, an external manager was hired, resulting in a management fee increase of approximately $2.4 million; and 3) The methodology of estimating the performance-based external manager fees has been enhanced that results in a higher, though more accurate, estimate of these performance fees.

- A cost reduction of $1,042,664 has occurred in the Custodian and Analytical Costs. Custodian fees and performance measurement fees decreased as a result of the custodian service review and the pooling of the marketable alternative investments.

- $729,665 or 12% of the increase in Total Other Expenses is mainly the result of two factors: 1) Consultant fees increased due to the addition of a proposed Risk Consultant and an advisor to the Marketable Alternatives Staff, and 2) Legal fees have increased as a result of more complex transactions, increasing the cost per investment and the number of investment opportunities has increased significantly.

Capital Expenditures Budget

The detail of the Capital Expenditures Budget is as follows:

Capital Expenditures for 2006-2007		
Computer Server Replacements and Related Software Licenses	$	75,000
Staff Computer and Monitor Replacements		15,000
Phones and Related Equipment		6,000
Software License Upgrades (Primary SQL and Exchange)		10,000
Allowance for Office Artwork and Framing		15,000
Allowance for Computers - 4 new staff		16,000
Additional Furniture Purchases		30,000
Total Capital Expenditures	**$**	**167,000**

Allocation of Expenses Across Funds

The final step in the budgeting process is to equitably allocate the budgeted expenses across the Funds. The UTIMCO Services Budget has traditionally been allocated on the basis of a combination of relative asset value of the Funds and total staff time dedicated to the management of each Fund. Budgeted expenses for 2006-2007 were allocated as follows: Permanent University Fund 46%, Long Term Fund 28%, Permanent Health Fund 6%, and Intermediate Term Fund 20%. These allocations are very similar to prior fiscal year allocations.

Direct Funds expenses are charged to each fund on the basis of costs actually incurred. Only those Direct costs associated solely with the PUF, PHF, LTF, and ITF are charged against those Funds.

UTIMCO Budget
Annual Fee and Allocation Schedule
For the fiscal year ending August 31, 2007

	The Permanent University Fund (PUF)	The Permanent Health Fund (PHF)	The University of Texas System Long Term Fund (LTF)	General Endowment Fund (GEF)	The University of Texas System Intermediate Term Fund (ITF)	Short Term Fund (STF)	Separately Invested Endowments and Charitable Trust Accounts	Total
UTIMCO Management Fee (1) (includes all operating expenses associated with the general management of the Funds)	**6,161,540**	**795,912**	**3,675,751**		**2,638,867**			**13,272,068**
Direct Expenses of the Fund								
External Management Fees	9,293,270	0	0	4,873,976	2,679,852	N/A (2)		16,847,098
External Management Fees - Performance Based	11,371,179	0	0	5,938,141	3,276,529			20,585,849
Other Direct Costs	2,953,528	18,863	160,249	1,845,533	1,008,149			5,986,321
Total Direct Expenses of the Fund	23,617,976	18,863	160,249	12,657,650	6,964,530		0	43,419,269
TOTAL	**29,779,516**	**814,775**	**3,836,000**	**12,657,650**	**9,603,397**	N/A (2)	**0**	**56,691,337**
Market Value 2/28/06 ($ millions)	**9,798.6**	**966.0**	**4,262.4**	**5,228.4** (3)	**2,920.0**	**1084.8**	**326.9**	**19,358.7**
Percentage of Market Value								
UTIMCO Services	0.063%	0.082%	0.086%	0.000%	0.090%	0.000%	0.000%	0.069%
Direct Expenses of the Fund	0.241%	0.002%	0.004%	0.242%	0.239%	0.000%	0.000%	0.224%
TOTAL	**0.304%**	**0.084%**	**0.090%**	**0.242%**	**0.329%**	**0.000%**	**0.000%**	**0.293%**

(1) Allocation Ratio: PUF-46%, PHF-6%,LTF-28%, ITF-20%
(2) Income is net of fees
(3) Pooled Fund for the collective investment of the PHF and LTF
(amounts may not foot due to rounding adjustments)

FY 2007

UTIMCO BUDGET REVIEW

The University of Texas System
Office of Finance

Prepared by:
Cathy Swain – Director of Investment Oversight
William Huang – Senior Financial Analyst

July 26, 2006

July 26, 2006

FY 2007
UTIMCO BUDGET REVIEW

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FY 2007 UTIMCO BUDGET REVIEW

I. EXECUTIVE SUMMARY

NOTE: A material change to the budget that the BOR previewed at the July 13, 2006, joint board meeting was approved by the UTIMCO Board and shared with Investment Oversight staff on July 25, 2006. This review reflects the change that increased budgeted bonuses by $569,000 (39.9% higher than presented on July 13, 2006; 61% higher than projected actual bonuses in FY06).

The UTIMCO budget consists of UTIMCO Services and Direct Costs to Funds. ("Funds" refer to the PUF, GEF and ITF). Table 1 below summarizes FY06 budget and projected actual expenses, and the proposed FY07 budget. Refer to Exhibit A for detailed FY06 and FY07 data and Exhibit C for five-year trends for FY03-FY07.

Table 1
UTIMCO FY06 Projected Actual and FY07 Budget Overview

	FY06			FY07			
	$ Budget	Projected $ Actual *	% Change vs FY06 Budget	$ Budget	$ Change vs FY06 Projected	% Change vs FY06 Projected	% Change vs FY06 Budget
UTIMCO Services	11,434,302	10,510,004	-8.1%	13,272,069	2,762,065	26.3%	16.1%
Direct Costs to Funds	37,111,691	43,356,325	16.8%	43,419,269	62,943	0.1%	17.0%
Total Budget	48,545,993	53,866,329	11.0%	56,691,338	2,825,009	5.2%	16.8%

** Projections based on actual UTIMCO Services and Direct Costs to Funds expenses through May 31, 2006.*

<u>FY06 Projected Actual versus Budget</u>: UTIMCO estimates that actual FY06 expenses will be approximately $53.9 million or $5.3 million (11%) over the total budget of $48.5 million.

- **UTIMCO Services** corporate expenses are projected to be under budget by $924k (8%), mainly due to unfilled positions and reduced bonus expectations, offset by legal and professional fees that exceed budget by about $160k.
- **Direct Costs to Funds** overall are projected to be over budget by $6.2 million (17%).
  - External management and performance fees are projected to exceed the budget by more than $7.4 million (24%).
  - Direct legal costs are projected to be 38% over budget (170% over budget in FY05).
  - Custodial, risk measurement, analytical and performance measurement costs, on the other hand, are projected at almost $1.1 million under budget (27%).

<u>FY07 Proposed Budget</u>: The proposed total UTIMCO budget for FY07 is $56.7 million, a 5% increase from FY06 projected actual expenses overall and a 17% increase from FY06 budget.

- **UTIMCO Services FY07** budget is an increase of 26% over FY06 projected actual expenses, primarily due to increases in compensation, staffing costs, and lease expenses.
- **Direct Costs to Funds** in total are budgeted consistent with actual costs forecast for FY06.
- **Total Compensation** is budgeted to increase more than 31% from FY06 projected actual, with Bonus Compensation budgeted to increase almost 61%.
- **Direct legal costs** continue to escalate, budgeted to increase 29% over FY06 projected actual.

<u>Centralized Management of Operating Funds</u>: The new ITF launched centralized management of operating funds on February 1, 2006, two months later than the budgeted December 1 start date, and was fully invested within policy asset allocation ranges within one month. Economies of scale should be possible with approved asset allocation targets achieved. Refer to Exhibit B for a detailed analysis of actual incremental costs for staff salaries and direct costs to funds.

- For the seven months of FY06, incremental costs are projected at $4.2 million, 43% lower than the budgeted amount of $7.4 million. On an annualized basis, incremental costs would have been approximately $7.3 million.
- FY07 budgeted incremental costs of $7.4 million are estimated to be approximately 0.17% of centralized operating funds (ITF and STF), not including incremental employee benefits or bonus compensation related to additional staffing.

Lease expenses are lower in FY06 on a cash basis compared to prior fiscal years as a result of the 10 months of deferred rent credit provided by the landlord for the Frost lease during FY06. From FY07 forward, however, lease expenses will be significantly higher than in previous years.

Shift to Private Investments: The ongoing shift to complex private investments throughout the portfolios is evidenced by escalating legal costs and third party management and performance fees. Private investments throughout the portfolios require more due diligence, documentation, and monitoring. (Refer to discussion of "Base and Performance Management Fees" on page 8.) External management and performance fees will be further analyzed in a separate update of total costs.

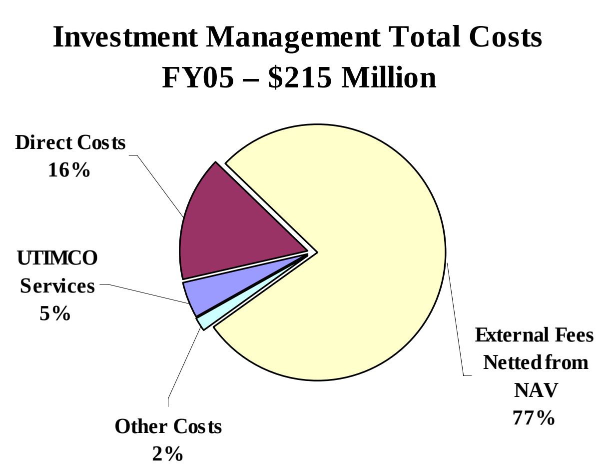
Risk Management: Data from private investments for analysis in the risk model, particularly hedge funds, is slower to materialize than anticipated. The FY07 budget contemplates increased expenses for expanded contractual resources which should result in more complete risk measurement data.

UTIMCO Proposed Fee Schedule: UTIMCO Services expenses are allocated to U. T. System Funds based on detailed "bottom up" analysis of staff time and specific costs; direct costs to funds are paid directly by each fund as much as possible. The proposed formula for FY07 allocates 20% of budgeted UTIMCO Services expenses to the ITF; the compensation program, on the other hand, weights the ITF 15% for entity performance targets. At 0.09% of total assets as of February 28, 2006, UTIMCO Services expenses allocated to the ITF are the highest of the funds. For the full year FY06, 15% of UTIMCO Services expenses were allocated to the ITF.

Distribution: Last fall $4 million in surplus UTIMCO corporate reserves were distributed back to the U. T. System Funds. A review of the most recent UTIMCO balance sheet available as of this writing (February 28, 2006) indicates that an additional distribution this year is not necessary.

II. Investment Management Total Costs

UTIMCO budgeted costs that are examined in this report include UTIMCO Services costs for corporate operations and Direct Costs of Funds, or fees and expenses paid directly by the funds for third party services. The chart illustrates that the $44 million in UTIMCO budgeted costs in FY05 represented only 21% of the $215 million in actual total costs (1.25% of average total assets under management).

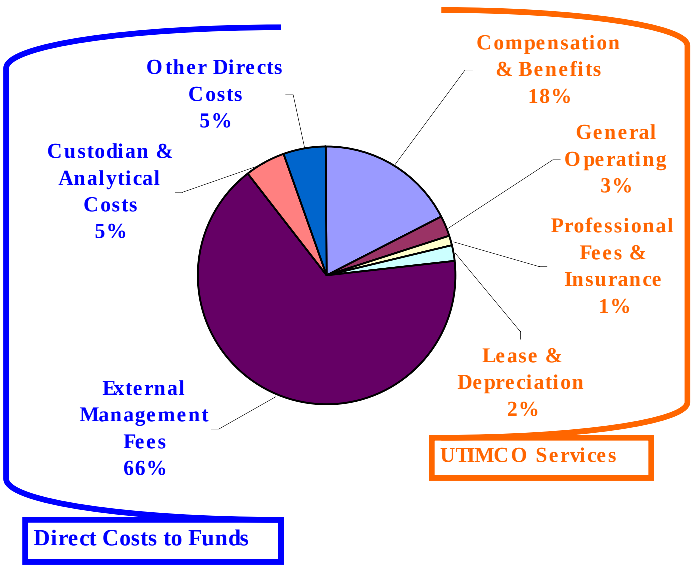


Investment management total costs are updated separately in an addendum to this report. Partnership, hedge fund, mutual fund, and other private investment fund fees and expenses are netted from reported investment results (net asset values). Since these expenses are not paid directly by U. T. System Funds, they are not budgeted. These expenses in FY05 were 77% of the investment management total costs. Other expenses budgeted by the U. T. System (2% of total costs) are fees for education and endowment compliance (LTF only), investment oversight, and internal audit.

III. FY 2007 Budget Trends Overview

UTIMCO proposes a total budget for FY07 of $56.7 million. The chart titled "FY 2007 UTIMCO Budget Components" shows the breakdown of the total budget. The UTIMCO Services operating budget accounts for 23% of the total, with personnel costs the largest component.

FY 2007 UTIMCO Budget Components
$56.691 million



Direct Costs to Funds include external management fees paid directly, custodial, consulting, legal, analytical, and other direct costs. External management fees paid directly, including related performance fees, dominate the total budget (66%). UTIMCO retains external managers for 82% of the $20 billion in assets managed including operating funds, up from approximately 75% in June 2005, partly due to the shift to external management of the REIT portfolio.

Table 2 shows the trend of Direct Costs to Funds and UTIMCO Services costs as a percent of total funds under management, including operating funds, since FY02. Active management of the centralized operating funds is resulting in slightly higher relative costs as a percent of total assets beginning in FY06.

Table 2
UTIMCO Budgeted Investment Management Cost Trends ($ Millions)

	Actual				Projected	Budget
	FY02	FY03	FY04	FY05	FY06	FY07
Average Total Assets Under Management (AUM) *	13,716	14,034	15,470	17,245	20,185	21,187
% Change in AUM	-8%	2%	10%	11%	17%	5%
UTIMCO Services	5.0	7.6	8.8	10.2	10.5	13.3
UTIMCO Services % of AUM	0.04%	0.05%	0.06%	0.06%	0.05%	0.06%
Direct Costs to Funds	20.1	16.0	25.5	33.8	43.4	43.4
Direct Costs to Funds % of AUM	0.15%	0.11%	0.16%	0.20%	0.21%	0.20%
Total Budgeted Costs	**25.1**	**23.7**	**34.3**	**44.0**	**53.9**	**56.7**
Total Budgeted Costs % of AUM	**0.18%**	**0.17%**	**0.22%**	**0.26%**	**0.27%**	**0.27%**

** Total average funds managed were calculated for FY 2003-2005 using beginning and ending FY totals as of August 31 and dividing by two. The averages for FY06 and FY07 are based on UTIMCO estimates.*

IV. UTIMCO Services

FY06 UTIMCO Services are projected to be under budget by $760k excluding depreciation, and $924k (8%) overall. Highlights are:

- Three unfilled budgeted positions saved approximately $656k, and some positions (including the Manager for Centralized Operating Funds) were filled at below budgeted salaries.
- Projected performance bonuses expect to save an additional $118k because one eligible position remains unfilled and performance FY06 year-to-date (YTD) has not achieved budget expectations.
- General operating, lease expense and insurance costs are consistent with budgeted amounts.
- Lease expenses are lower on a cash basis compared to prior fiscal years as a result of the 10 months of deferred rent credit provided by the landlord for the Frost lease during FY06.
- Professional fees (mainly legal) should exceed the budgeted amount by $160k.
- Depreciation is below budget by about $165k due to a change in prior year treatment of anticipated deferred rent in budgeting for depreciation. Projected actual depreciation for FY06 is in line with budgeted capital expenditures.
- FY07 UTIMCO Services budget is more than 26% higher than projected FY06 actual expenses.

Staffing and Personnel Costs: Nearly 75% of the FY07 UTIMCO Services budget (18% of the total budget) is directly related to personnel including employee benefits. Trends in staffing and total compensation are shown in Table 3. Compensation since FY03 has significantly outpaced both growth in managed assets and the increase in number of employees:

- UTIMCO staff has grown 51% from 37 in FY03 to a budgeted 56 in FY07, while funds managed also increased 51%;
- Bonus compensation has increased 145% based on the FY07 proposed budget;
- Total compensation has more than doubled in the aggregate;
- Average total compensation per employee has increased 34% to more than $150k budgeted in FY07; and
- Funds managed per employee is projected in FY07 to decline to the lowest level since FY03.

Table 3
UTIMCO Compensation and Headcount – FY03-FY07

	FY03 Actual	FY04 Actual	FY05 Actual	FY06 Projected	FY07 Budget *	Growth Rate Since FY03
Employees	37	38	42	49	56	51%
AUM ($ millions)	14,034	15,470	17,245	20,185	21,187	51%
AUM per Employee	379,299	407,113	410,590	411,934	378,348	0%
Salaries and Wages	3,102,883	3,773,961	4,203,100	4,807,446	5,815,449	87%
Bonus Compensation	1,089,333	1,858,653	2,094,447	1,661,284	2,670,927	145%
Total Compensation	4,192,216	5,632,614	6,297,547	6,468,730	8,486,376	102%
Total Compensation per Employee	113,303	148,227	149,942	132,015	151,542	34%
Bonus as % of Salaries and Wages	35%	49%	50%	35%	46%	
Bonus as % of Total Compensation	26%	33%	33%	26%	31%	

** For FY07 bonus compensation, UTIMCO assumes 50% of the maximum incentive award opportunity will be earned under UTIMCO's compensation program, of which 70% is budgeted to be paid in the fiscal year. The remaining 30% of bonuses earned in FY07 would be deferred, budgeted, and paid over the next three fiscal years.*

Salaries and Wages are projected to be approximately $656k (12%) under budget in FY06 because of delays in hiring and filling some positions at below budgeted salaries. Last year the budget was based on staffing of 52 employees; actual staffing is projected to be 49 employees by fiscal year end 2006. Refer to Exhibit D for a list of the unfilled budgeted and proposed new positions for FY06 and FY07. Three budgeted, unfilled positions have been open since FY05; one position (the portfolio manager for REITS) is deleted from the FY07 budget.

The FY07 budget for total compensation represents 64% of the total UTIMCO Services budget and proposes to increase $2.0 million (31%) to $8.5 million from a projected $6.5 million in FY06. Salaries proposed in the FY07 budget include increased salaries for three unfilled positions, four proposed new positions (approximately 20% of the increase), and an average 4.6% base salary increase for existing employees.

Actual bonuses paid for FY05 were on average 50% of salaries and wages, including positions not filled. In FY06 UTIMCO budgeted for 35% of the incentive award opportunity to be paid under the compensation program and 50% of discretionary bonuses for employees outside of the program. Based on performance YTD, bonus compensation for FY06 (including deferred bonuses earned in prior years and related investment income) is forecast to be $118k under budget and on average 35% of salaries and wages.

For FY07 UTIMCO assumes 50% of the maximum incentive award opportunity will be earned by eligible key employees (on average 46% of total salaries and wages), of which 70% is budgeted and would be paid in the fiscal year. The remaining 30% of bonuses earned in FY07 would be deferred, budgeted, and paid over the next three fiscal years. The FY07 budget also includes $592k of deferred bonuses earned by employees in prior years, related investment income, and nearly $112k budgeted for a discretionary bonus pool up to 15% of salaries for employees not eligible to participate in the formal incentive plan.

Employee Benefits budgeted for FY07 cost roughly 18% of proposed base compensation, which is slightly lower than U. T. System Administration averages because of UTIMCO's higher average salary levels. Employee Benefit costs are expected to be under budget in FY06 by $107k (11%) due to unfilled existing positions. UTIMCO pays a portion of the cost of employee group health, dental, life, short term disability, and long term disability insurance, and contributes on behalf of participating employees to a 403(b) retirement savings plan. UTIMCO's portion of Employee Benefits costs is budgeted to increase 23% to $1.0 million in FY07, reflecting higher costs for existing staff and new employees. We have recommended that UTIMCO should evaluate whether cost savings may be gained from participating in self-insured benefit plans like the U. T. System's.

General Operating Expenses are on target with the budgeted amount for FY06 of $1.6 million. The FY07 budget proposes a slight increase, primarily due to increased on-line data and contract services and travel, offset by reduced recruiting and relocation expenses.

Lease Expense: UTIMCO's move to 70% larger space in the Frost Bank Tower, with 14 months of deferred rent starting in October 2005, reduced total lease expenses on a cash basis in FY06 to 49% below FY05. The majority of the $308k projected actual lease expense in FY06 was for final months of occupancy in the Chase building. At budgeted staffing of 56 employees in FY07, the space allows an average of approximately 500 square feet per employee; however, the increase in leased space is intended to accommodate staffing growth over the 11-year term of the lease.

The Frost Bank lease is less expensive on a per square foot basis but more expensive on a dollar basis than the previous Chase building lease due to the increase in leased space, higher parking expense, and higher operating expenses passed through. Table 4 below illustrates that cost savings in FY06 will be offset by increased lease costs in FY07 and beyond. Lease expenses of $810k budgeted for FY07 (allowing for the final two months of deferred rent) are 163% higher than actual FY06 expenses and 35% higher than FY05 (54% higher on a full year basis).

Lease expense presented here on a cash basis excludes the accrual of amortization of $1.8 million in deferred rent expense which will be amortized ratably over the life of the 132 month lease. Deferred rent expense includes allowances for leasehold improvements and free rent that are expensed over the life of the lease so that lease expense on an accrual basis will be the same each month.

Table 4
Lease Expense Analysis

	Chase		**Frost Bank Tower**				
Actual / Projected	**FY05**	**FY06**	**FY07**	**FY08**	**FY09**	**FY10**	**FY11**
Parking Expense	62,362	71,500	90,600	93,318	96,118	99,001	101,971
Misc. Lease Expense*	4,432	3,775	4,500	4,500	4,500	4,500	4,500
Property Lease	362,010	150,838	425,409	493,274	493,274	493,274	493,274
Lease Operating Expense	171,789	81,874	289,230	345,431	355,794	366,468	377,462
Total	600,593	307,987	809,739	936,523	949,686	963,243	977,207

** Storage. Note also that parking and lease operating expenses are assumed to increase 3% annually, starting in FY08.*

Capital Expenditures associated with the office move to the Frost Bank Tower were approximately $2.7 million through FY06, of which $1.6 million was refunded by the landlord as an allowance for leasehold improvements. Total capital expenditures budgeted for office relocation, including information technology (IT) upgrades and a portion of leasehold improvements expenditures that were incurred during the end of FY05, are projected to be approximately 14% under budget. Capital expenditures of $1.4 million associated with the office move (excluding moving costs) and IT planned upgrades, and related increases in depreciation of approximately $236k are explained in Table 5.

Table 5
Capital Expenditures and Depreciation

	Budget FY06	**Projected FY06**	**Variance**	**Budget FY07**
Leasehold Improvements (net)	786,452	637,811	-19%	0
Furniture	485,000	499,461	3%	30,000
IT Upgrades	366,000	267,506	-27%	137,000
Total Capital	1,637,452	1,404,778	-14%	167,000
Change in Depreciation/amortization	264,900	235,771	-11%	39,333
Total Depreciation/amortization	535,900	371,387	-31%	410,720

Projected depreciation expense for leasehold improvements and the purchase of new furniture and equipment associated with the office move in FY06 is anticipated to be about 31% below budget because of a change in prior year treatment of anticipated deferred rent in budgeting for depreciation. The FY07 budget adjusts for this change with $411k budgeted for depreciation, reflecting an increase of $39k above projected FY06 to account for $167k in proposed capital expenditures, summarized in Table 6. Total new furniture costs of nearly $530k average of nearly $9,500 per employee, and new staff computers are budgeted at $4k each.

Table 6
Capital Budget FY07

Computer server replacements and related software licenses	75,000
Software license upgrades (primary SQL and exchange)	10,000
Staff computer and monitor replacements	15,000
Computers for four new staff	16,000
Phones and related equipment	6,000
Allowance for office artwork and framing	15,000
Furniture	30,000
Total Capital Budget	**$ 167,000**

Professional Fees are expected to be $385k in FY06, 71% higher than the budgeted amount of $225k. Compensation Consultant fees are projected at $65k from a budgeted $25k; and Accounting Fees increased from a budgeted $25k to nearly $48k. Legal expenses are projected to be over budget by $80k in FY06, and budgeted to decrease 24% in FY07 to $195k. (See discussion of "Legal Expenses" below.) Total Professional Fees are budgeted to decrease 30% to a $270k in FY07.

V. Direct Costs to Funds

Direct Costs to Funds for FY06, including centralized management of operating funds, are projected to be $43.4 million or 17% over a budgeted $37.1 million. The FY07 budget will increase only slightly (0.1%) from projected FY06 actual expenses.

Base and Performance Management Fees paid to external managers under agency agreements represent approximately 86% of Direct Costs to Funds and continue to increase in both dollar terms and as a percentage of assets. In FY06, these fees are expected to be approximately $38.2 million or 24% over a budgeted total of $30.8 million. REIT assets were shifted to third party management upon the departure last year of UTIMCO's REIT portfolio manager. As a result, an estimated $2.4 million in unanticipated base management fees were incurred for PUF and GEF REIT holdings. The FY07 budget includes approximately $4.6 million (not including performance fees) for external management of REIT assets for all three funds.

Incremental external management fees for centralized operating funds were budgeted at an estimated $5.7 million and are currently projected to be only $3.4 million, which means fees for the PUF and GEF are over budget by nearly 40%. During the budget review last summer, UTIMCO projected that FY05 direct external management costs would be $3.1 million (13%) over budget; actual costs turned out to be $5.6 million (24%) over budget.

The 2% budgeted decrease in FY07 from the FY06 projected actual external management fees may not be realistic, given the increase in actively managed assets with the ITF fully invested for a full year in FY07 vs. seven months in FY06. Direct external management costs overall could level off, however, if assets continue to shift to private investments whose fees and expenses are netted from asset values, not budgeted or paid directly.

Custodial and performance measurement costs have increased significantly since FY05 because of daily valuations by the custodian and increasing assets. Due in part to more competitive fees as a consequence of the RFP process, Mellon custodial fees in FY06 are projected to be $1.8 million, well under a budgeted $2.4 million. The FY07 budget anticipates a further decrease of nearly 29% to $1.3 million. Performance measurement expenses in FY06, projected to be 15% below budget at $526k, are budgeted in FY07 to increase slightly to a proposed $531k.

Timely independent verification of performance and asset allocation information and close monitoring of internal derivative positions are critical to support UTIMCO's active management style. Internal derivatives positions of approximately $5.575 billion gross-weighted (28% of all U. T. System total assets as of April 30, 2006) require detailed reporting of underlying collateral and net asset values to mark-to-market positions for accurate performance reporting and risk measurement. To maintain minimal cash portfolio targets, accurate and timely trade (vs. settlement date) accounting is also necessary to accurately clear and match all current trading activities.

Risk Management System expenses charged to the funds in FY06 are expected to be more than 55% ($444k) under budget. U. T. System oversight staff are concerned that FY06 projected expenditures are significantly lower than budgeted amounts because availability of data on holdings of external hedge funds and other private investments has been delayed and still is not complete.

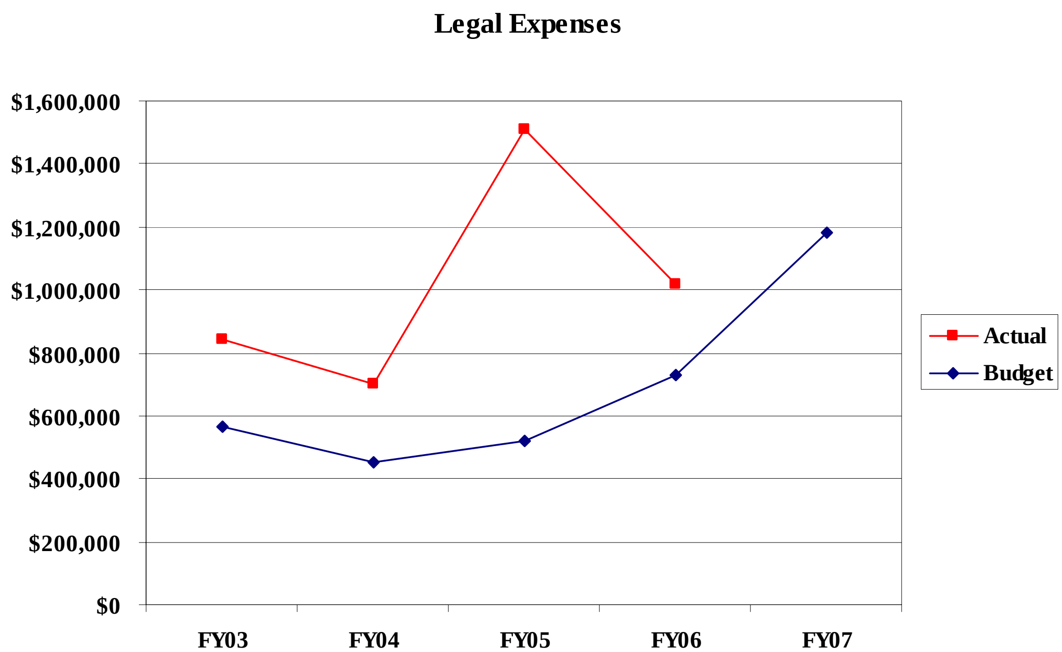
This area of analysis is critically important, especially given internal derivatives exposure and the lack of transparency with hedge fund positions. In the absence of actual position data, UTIMCO's risk model uses "proxies" to simulate the hedge fund and private capital components of the portfolio risk profile. The recent demise of the S&P Hedge Fund Index highlights concerns about relying on these benchmarks for risk assessment.

UTIMCO signed a 12-month contract for $250k with IFS (International Fund Systems) effective October 1, 2005, and reported recently in Board materials that the contract is being renewed for an annual fee of $400k for the risk management system. Additionally, IFS receives and analyzes individual investment positions from some hedge fund managers and reports the risk factor exposures to UTIMCO. IFS charges a fee of $15k per hedge fund annually for managers who agree to disclose holdings to IFS ($7,500 for hedge funds already reporting to IFS). Some managers do report holdings to IFS, but fees for analysis of individual hedge fund holdings have been delayed while IFS completes the system configuration.

For FY07, risk system costs are budgeted to be $400k for the traditional portfolio and an additional $450k for 31 hedge funds (14 existing, 17 new) for a total of $850k. The total FY07 budget for direct costs of the risk management system is nearly 6% higher than the FY06 budgeted level, and 137% above projected actual FY06 expenses.

Controls Assessment expenses in FY06 were budgeted for full Sarbanes-Oxley controls assessment certifications for the UTIMCO corporation and U. T. System Funds, but full implementation occurred only for the corporation and PUF. As a result, related expenses are currently estimated at $122k this fiscal year, about 11% under budget. The FY07 budget expects these costs to increase slightly to $124k to fund U. T. System Audit Office and Ernst & Young fees for scheduled controls assessment certifications for the corporation, PUF, GEF, LTF, and PHF. Certification for the ITF is expected to occur in FY08.

<u>Legal fees</u>: Total legal fees for management of U. T. System Funds, including UTIMCO corporate services and direct legal expenses charged to the funds, have escalated since FY2004 as shown in the chart below.



The trend to higher legal fees is expected to continue with the shift to complex private investment funds throughout the portfolios. The spike in 2005 was attributed to disclosure issues related to private capital investments and analysis of centralization options. Legal fees paid directly by U. T. System Funds in FY06 are projected to be approximately 38% over budget at $764k. This increase is related to new private capital investments, other private investment funds, and hedge funds, many of which are domiciled outside the U.S. and require more due diligence and documentation. The FY07 budget proposes a further increase of almost 29% to $985k.

Exhibit A

UTIMCO Operating Expenses/Budgets FY06-FY07

	8/31/2006			Change from 2006 Budget		8/31/2007	Change from 2006 Projected		Change from 2006 Budget
	Budget	**YTD***	**Projected**	**$**	**%**	**Budget**	**$**	**%**	**%**
UTIMCO Services									
Salaries and Wages + Vacation	5,463,555	3,571,374	4,807,446	(656,109)	-12.0%	5,815,449	1,008,003	21.0%	6.4%
Bonus Compensation + Interest	1,778,784	1,347,394	1,661,284	(117,500)	-6.6%	2,670,927	1,009,643	60.8%	50.2%
Total Compensation	7,242,339	4,918,768	6,468,730	(773,609)	-10.7%	8,486,376	2,017,646	31.2%	17.2%
Total Payroll taxes	345,516	226,809	302,412	(43,104)	-12.5%	379,877	77,465	25.6%	9.9%
403(b) Contributions	415,102	283,254	377,672	(37,430)	-9.0%	426,313	48,641	12.9%	2.7%
Group Health, Dental, AD&D, Life, LTD	531,079	346,991	462,654	(68,425)	-12.9%	610,877	148,223	32.0%	15.0%
Employee Benefit Services	6,000	3,216	4,950	(1,050)	-17.5%	4,715	(235)	-4.7%	-21.4%
Employee Benefits	952,181	633,461	845,276	(106,905)	-11.2%	1,041,905	196,629	23.3%	9.4%
On-Line Data & Contract Services	779,086	597,833	787,428	8,342	1.1%	881,212	93,784	11.9%	13.1%
Recruiting and Relocation Expenses	171,000	186,250	225,000	54,000	31.6%	49,500	(175,500)	-78.0%	-71.1%
Travel	300,488	188,531	265,000	(35,488)	-11.8%	349,320	84,320	31.8%	16.3%
Phone Equipment and Charges	42,750	28,112	40,483	(2,267)	-5.3%	32,250	(8,233)	-20.3%	-24.6%
Computer & Office Supplies	78,325	68,135	85,405	7,080	9.0%	85,325	(80)	-0.1%	8.9%
Employee Education	51,410	15,108	27,450	(23,960)	-46.6%	51,175	23,725	86.4%	-0.5%
Repairs/Maintenance	62,850	44,965	59,950	(2,900)	-4.6%	82,950	23,000	38.4%	32.0%
BOD Meetings	37,500	41,419	42,500	5,000	13.3%	37,500	(5,000)	-11.8%	0.0%
Other Operating Expenses	41,045	24,474	35,821	(5,224)	-12.7%	41,995	6,174	17.2%	2.3%
Total General Operating	1,564,454	1,194,827	1,569,037	4,583	0.3%	1,611,227	42,190	2.7%	3.0%
Total Lease Expense	307,212	283,255	307,987	775	0.3%	809,739	808,964	162.9%	163.6%
Invest., Hiring & Board Consultants	0	12,500	17,500	17,500	N/A	17,500	0	0.0%	N/A
Legal Expenses	175,000	164,231	255,000	80,000	45.7%	195,000	(60,000)	-23.5%	11.4%
Compensation Consultant	25,000	35,750	65,000	40,000	160.0%	12,500	(52,500)	-80.8%	-50.0%
Accounting fees	25,000	43,681	47,500	22,500	90.0%	45,000	(2,500)	-5.3%	80.0%
Total Professional Fees	225,000	256,162	385,000	160,000	71.1%	270,000	(115,000)	-29.9%	20.0%
Property/Liability Package	15,700	11,685	15,700	0	0.0%	15,750	50	0.3%	0.3%
Umbrella Policy	6,000	4,312	5,950	(50)	-0.8%	5,950	0	0.0%	-0.8%
Workers Compensation	11,600	7,134	11,250	(350)	-3.0%	12,250	1,000	8.9%	5.6%
Business Auto	800	472	775	(25)	-3.1%	775	0	0.0%	-3.1%
Commercial Bonding Policy	44,000	28,019	45,000	1,000	2.3%	45,000	0	0.0%	2.3%
Prof., D&O & Emp. Practices Liability	183,600	136,050	181,500	(2,100)	-1.1%	182,500	1,000	0.6%	-0.6%
Total Insurance	261,700	187,672	260,175	(1,525)	-0.6%	262,225	2,050	0.8%	0.2%
Depreciation of Equipment	535,900	252,163	371,387	(164,513)	-30.7%	410,720	39,333	10.6%	-23.4%
Total UTIMCO Services	11,434,302	7,953,117	10,510,004	(924,298)	-8.1%	13,272,069	2,762,065	26.3%	16.1%
Direct Costs to Funds									
External Management Fees	20,421,000	11,072,574	14,998,239	(5,422,761)	-26.6%	16,847,098	1,848,859	12.3%	-17.5%
External Mgt. Fees-Performance Fees	10,391,371	18,519,402	23,241,813	12,850,442	123.7%	20,585,849	(2,655,964)	-11.4%	98.1%
External Management Fees	30,812,370	29,591,976	38,240,052	7,427,681	24.1%	37,432,947	(807,104)	-2.1%	21.5%
Custodian Fees and Other Direct Costs	2,356,175	1,286,717	1,762,217	(593,958)	-25.2%	1,260,072	(502,145)	-28.5%	-46.5%
Performance Measurement	621,169	368,638	526,138	(95,031)	-15.3%	530,599	4,462	0.8%	-14.6%
Analytical Tools	289,570	253,723	336,095	46,525	16.1%	386,700	50,605	15.1%	33.5%
Risk Measurement	803,121	152,000	358,667	(444,454)	-55.3%	850,000	491,333	137.0%	5.8%
Custodian and Analytical Costs	4,070,034	2,061,077	2,983,116	(1,086,918)	-26.7%	3,027,371	44,256	1.5%	-25.6%
Consultant Fees	1,100,000	619,666	808,666	(291,334)	-26.5%	1,356,000	547,334	67.7%	23.3%
Auditing	213,920	140,000	212,000	(1,920)	-0.9%	205,000	(7,000)	-3.3%	-4.2%
Controls Assessment (Sarbanes Oxley)	136,500	97,110	122,110	(14,390)	-10.5%	124,000	1,890	1.5%	-9.2%
Printing	150,666	0	163,790	13,124	8.7%	182,250	18,460	11.3%	21.0%
Bank Fees	6,000	14,606	18,006	12,006	200.1%	18,500	494	2.7%	208.3%
Rating Agency Fees	0	10,646	10,646	10,646	N/A	0	(10,646)	-100.0%	N/A
Legal Fees	555,000	594,173	764,483	209,483	37.7%	985,000	220,517	28.8%	77.5%
Background Searches & Other	67,200	24,956	33,456	(33,744)	-50.2%	88,200	54,744	163.6%	31.3%
Other Directs Total	2,229,286	1,501,158	2,133,158	(96,128)	-4.3%	2,958,950	825,792	38.7%	32.7%
Total Direct Costs to Funds	37,111,691	33,154,210	43,356,325	6,244,635	16.8%	43,419,269	62,943	0.1%	17.0%
Total Costs	48,545,993	41,107,327	53,866,329	5,320,337	11.0%	56,691,338	2,825,009	5.2%	16.8%

** Actual UTIMCO Services and Direct Costs to Funds expenses as of 05/31/2006*

Exhibit B

Centralized Operating Fund Expenses

	FY06				Annual v. Budget		FY07	Budget v. FY06 Annual	
	Budget	FY06 YTD (1)	Projected	Annualized (2)	$	%	Budget	$	%
Centralized Fund Positions:									
Client Services Manager (3)									
Manager Core Fund Investments									
Risk Management Associate									
Core Fund Analyst									
Operating Funds Sr Accountant									
Operations Associate									
UTIMCO Services Salaries (4)	470,833	121,792	215,792	494,929	24,096	5.1%	453,333	(41,596)	-19.3%
Direct Costs to Funds:									
External Manager Fees	5,708,281	1,875,025	3,402,843	5,833,446	125,165	2.2%	5,956,381	122,935	3.6%
Custodian Fees	647,057	124,478	217,478	372,820	(274,237)	-42.4%	332,416	(40,403)	-18.6%
Performance Measurement	117,419	48,000	84,000	144,000	26,581	22.6%	156,650	12,650	15.1%
Analytical Tools	0	33,675	61,133	104,799	104,799	N/A	58,005	(46,794)	-76.5%
Risk Measurement	157,121	0	68,889	118,095	(39,025)	-24.8%	127,500	9,405	13.7%
Cambridge Fees	200,000	33,332	58,331	99,996	(100,004)	-50.0%	203,400	103,404	177.3%
Auditing	52,731	0	7,000	12,000	(40,731)	-77.2%	41,498	29,498	421.4%
Printing	5,250	0	0	0	(5,250)	-100.0%	5,000	5,000	N/A
Legal Fees	15,000	37,450	62,950	107,914	92,914	619.4%	72,750	(35,164)	-55.9%
Background Searches & Other	21,000	4,709	5,984	10,258	(10,742)	-51.2%	10,930	672	11.2%
Direct Costs to Funds	6,923,859	2,156,669	3,968,607	6,803,327	(120,532)	-1.7%	6,964,530	161,203	4.1%
Total Operating Fund Expenses	**$7,394,692**	**$3,326,803**	**$4,184,399**	**$7,298,256**	**($96,436)**	**-1.3%**	**$7,417,863**	**$119,607**	**2.9%**
Net Asset Value ($ millions) (5)	3,700.0	4,317.4	4,317.4	4,317.4			4,462.4		
UTIMCO Services (% of NAV)	0.013%	0.003%	0.005%	0.011%			0.010%		
Direct Costs (% of NAV)	0.187%	0.050%	0.092%	0.158%			0.156%		
Total Expenses (% of NAV)	**0.200%**	**0.053%**	**0.097%**	**0.169%**			**0.166%**		

(1) FY06 YTD actuals through May 31, 2006.
(2) FY06 annualized expenses are the estimated full year expenses based on the 7 month FY06 projected expenses and includes unfilled positions.
(3) Position is currently unfilled.
(4) The difference between FY06 budget and projected amounts are the result of the start date of the ITF and for each individual. When centralization was pushed back to February 2006 from December 2005, these positions were not filled until later in the fiscal year.
(5) The net asset value for centralized operating funds includes both the STF and ITF. FY06 projected/annualized and FY07 budget values are based on UTIMCO estimates.

Exhibit C

UTIMCO Operating Expenses/Budgets FY03-FY07

	8/31/2003	8/31/2004	8/31/2005	8/31/2006		Change from 2006 Budget	8/31/2007	Change from 2006 Projected	Change from 2006 Budget
	Actual	Actual	Actual	Budget	Projected	%	Budget	%	%
UTIMCO Services									
Salaries and Wages + Vacation	3,102,883	3,773,961	4,203,100	5,463,555	4,807,446	-12.0%	5,815,449	21.0%	6.4%
Bonus Compensation + Interest	1,089,333	1,858,653	2,094,447	1,778,784	1,661,284	-6.6%	2,670,927	60.8%	50.2%
Total Compensation	4,192,216	5,632,614	6,297,547	7,242,339	6,468,730	-10.7%	8,486,376	31.2%	17.2%
Total Payroll taxes	195,076	206,777	313,637	345,516	302,412	-12.5%	379,877	25.6%	9.9%
403(b) Contributions	219,898	280,400	304,359	415,102	377,672	-9.0%	426,313	12.9%	2.7%
Group Health, Dental, AD&D, Life, LTD	201,090	259,932	315,457	531,079	462,654	-12.9%	610,877	32.0%	15.0%
Employee Benefit Services	4,490	4,984	3,949	6,000	4,950	-17.5%	4,715	-4.7%	-21.4%
Employee Benefits	425,478	545,316	623,765	952,181	845,276	-11.2%	1,041,905	23.3%	9.4%
On-Line Data & Contract Services	417,995	598,504	677,346	779,086	787,428	1.1%	881,212	11.9%	13.1%
Recruiting and Relocation Expenses	359,917	2,513	35,600	171,000	225,000	31.6%	49,500	-78.0%	-71.1%
Travel	109,138	138,855	170,069	300,488	265,000	-11.8%	349,320	31.8%	16.3%
Phone Equipment and Charges	41,990	45,660	39,340	42,750	40,483	-5.3%	32,250	-20.3%	-24.6%
Computer & Office Supplies	73,887	58,934	68,431	78,325	85,405	9.0%	85,325	-0.1%	8.9%
Employee Education	14,424	20,244	21,814	51,410	27,450	-46.6%	51,175	86.4%	-0.5%
Repairs/Maintenance	39,453	45,576	56,434	62,850	59,950	-4.6%	82,950	38.4%	32.0%
BOD Meetings	29,811	17,541	27,552	37,500	42,500	13.3%	37,500	-11.8%	0.0%
Other Operating Expenses	25,554	57,082	48,357	41,045	35,821	-12.7%	41,995	17.2%	2.3%
Total General Operating	1,112,169	984,909	1,144,943	1,564,454	1,569,037	0.3%	1,611,227	2.7%	3.0%
Total Lease Expense	606,013	599,047	600,593	307,212	307,987	0.3%	809,739	162.9%	163.6%
Invest., Hiring & Board Consultants	2,000	0	17,500	0	17,500	N/A	17,500	0.0%	N/A
Legal Expenses	500,823	183,102	579,720	175,000	255,000	45.7%	195,000	-23.5%	11.4%
Compensation Consultant	45,200	108,397	33,650	25,000	65,000	160.0%	12,500	-80.8%	-50.0%
Accounting fees	6,870	12,910	30,135	25,000	47,500	90.0%	45,000	-5.3%	80.0%
Total Professional Fees	554,893	304,409	661,005	225,000	385,000	71.1%	270,000	-29.9%	20.0%
Property/Liability Package	15,009	16,657	28,797	15,700	15,700	0.0%	15,750	0.3%	0.3%
Umbrella Policy	6,756	7,521	6,720	6,000	5,950	-0.8%	5,950	0.0%	-0.8%
Workers Compensation	14,109	18,227	17,419	11,600	11,250	-3.0%	12,250	8.9%	5.6%
Business Auto	175	186	469	800	775	-3.1%	775	0.0%	-3.1%
Commercial Bonding Policy	39,138	42,879	28,849	44,000	45,000	2.3%	45,000	0.0%	2.3%
Prof., D&O & Emp. Practices Liability	158,881	173,208	171,959	183,600	181,500	-1.1%	182,500	0.6%	-0.6%
Total Insurance	234,068	258,678	254,213	261,700	260,175	-0.6%	262,225	0.8%	0.2%
Depreciation of Equipment	286,176	261,894	272,836	535,900	371,387	-30.7%	410,720	10.6%	-23.4%
Total UTIMCO Services	7,606,089	8,793,644	10,168,539	11,434,302	10,510,004	-8.1%	13,272,069	26.3%	16.1%
Direct Costs to Funds									
External Management Fees	10,699,801	12,715,126	14,217,736	20,421,000	14,998,239	-26.6%	16,847,098	12.3%	-17.5%
External Mgt. Fees-Performance Fees	4,467,459	9,165,879	14,898,389	10,391,371	23,241,813	123.7%	20,585,849	-11.4%	98.1%
External Management Fees	12,314,265	21,881,005	29,116,125	30,812,370	38,240,052	24.1%	37,432,947	-2.1%	21.5%
Custodian Fees and Other Direct Costs	1,351,899	1,043,993	1,506,759	2,356,175	1,762,217	-25.2%	1,260,072	-28.5%	-46.5%
Performance Measurement	261,625	463,238	487,976	621,169	526,138	-15.3%	530,599	0.8%	-14.6%
Analytical Tools		218,172	284,050	289,570	336,095	16.1%	386,700	15.1%	33.5%
Risk Measurement	335,172	120,000	267,500	803,121	358,667	-55.3%	850,000	137.0%	5.8%
Custodian and Analytical Costs	1,948,696	1,845,403	2,546,285	4,070,034	2,983,116	-26.7%	3,027,371	1.5%	-25.6%
Consultant Fees	1,477,800	900,000	900,000	1,100,000	808,666	-26.5%	1,356,000	67.7%	23.3%
Auditing	168,202	205,000	158,309	213,920	212,000	-0.9%	205,000	-3.3%	-4.2%
Controls Assessment (Sarbanes Oxley)			0	136,500	122,110	-10.5%	124,000	1.5%	-9.2%
Printing	99,583	111,431	132,196	150,666	163,790	8.7%	182,250	11.3%	21.0%
Bank Fees	7,605	12,036	5,332	6,000	18,006	200.1%	18,500	2.7%	208.3%
Rating Agency Fees	21,508	22,008	21,992	0	10,646	N/A	0	-100.0%	N/A
Legal Fees	343,849	517,868	932,525	555,000	764,483	37.7%	985,000	28.8%	77.5%
Background Searches & Other	1,540	11,490	23,481	67,200	33,456	-50.2%	88,200	163.6%	31.3%
Other Directs Total	2,120,087	1,779,833	2,173,835	2,229,286	2,133,158	-4.3%	2,958,950	38.7%	32.7%
Total Direct Costs to Funds	16,048,173	25,506,242	33,836,245	37,111,691	43,356,325	16.8%	43,419,269	0.1%	17.0%
Total Costs	23,654,262	34,299,886	44,004,784	48,545,993	53,866,329	11.0%	56,691,338	5.2%	16.8%

Exhibit D
Staffing Analysis

Budgeted but unfilled positions as of June 30, 2005 *** Positions filled during FY06**	**Salary**
Managing Director (Inflation Hedging)	
Client Services Manager	
Senior Associate (Non Marketable Alternatives) *	
Analyst (Public Markets) *	
Analyst (Inflation Hedging)	
Total	**555,000**

Proposed Positions Approved for FY06 Budget *** Positions filled during FY06**	**Salary**
Manager of Core Fund Investments (Public Markets) *	
Associate (Risk Management) *	
Analyst of Core Fund Investments (Marketable Alternatives) *	
Sr. Accountant (Accounting & Operations) *	
Associate (Accounting & Operations) *	
Total	**345,833**

Budgeted but Unfilled Positions as of June 28, 2006 **3 unfilled positions**	**Salary**
Managing Director (Inflation Hedging)	
Client Services Manager	
Analyst (Inflation Hedging)	
Total	**405,000**

New Proposed Positions for FY07 Budget **4 proposed positions**	**Salary**
Sr. Analyst (Public Markets)	
Analyst (Public Markets)	
Compliance Officer (Accounting & Operations)	
Admin. Assistant (Accounting & Operations)	
Total	**260,000**

ADDENDUM to FY2007 UTIMCO Budget Review
Total Investment Management Costs and UTIMCO Value Added

I. EXECUTIVE SUMMARY

NOTE: A material change to the budget that the BOR previewed at the July 13th joint board meeting was approved by the UTIMCO Board and shared with Investment Oversight staff on July 25, 2006. This review reflects the change that increased budgeted bonuses by $561,000 (39.9% higher than presented on July 13th; 61% higher than projected actual bonuses in FY06).

This report summarizes the analysis of the cost effectiveness of UTIMCO's investment management of the U. T. System assets, comparing value added and total costs for fiscal years 2002-2005 and providing a forecast for FY2006 and FY2007, based on data provided by UTIMCO. Highlights are:

1. **UTIMCO performance added nearly $1.3 billion in value for the PUF and the GEF during the five fiscal years** ending August 31, 2005, net of all investment management costs. While value added for FY06 is not finalized**,** zero value added is estimated based on actual performance through June 30, 2006. This could change, with two months remaining in the fiscal year and lags in some managers' reporting.
2. **Centralized management of operating funds** expands opportunities to add value and should result in higher costs. Costs decreased slightly in FY06, however, despite substantial UTIMCO and external resources dedicated to the startup of the ITF. YTD results for the ITF show positive value added relative to its policy portfolio.
3. **Total costs have increased significantly over the past five years**, both in dollar terms and as a percent of assets managed:
   a. From nearly $91 million in FY02 to $213 million projected in FY06. More than $289 million is budgeted/estimated for FY07.
   b. From 0.66% of average annual assets under management in FY02 to a high of 1.25% in FY05; 1.05% projected based on YTD FY06; estimated 1.36% in FY07.
4. **Projected total cost increases** of 36% in FY07 are attributed mainly to higher base and performance fees netted from asset values by third party managers, reflecting the shifting investment strategy to more expensive "alternative" asset classes, active management style, and performance-based fees.
5. **Cumulative total investment management costs of approximately $798 million** during the past five fiscal years (estimated for FY06 based on actual costs through May 31, 2006 and assuming zero valued added YTD) were recovered by a factor of 1.6 X.

Data presented in this report is from the following sources:

1. Value added by UTIMCO was estimated by Cambridge Associates, measuring UTIMCO performance relative to BOR approved policy portfolio benchmarks for the System funds from FY01 through FY05. Bruce Meyers' memo dated December 7, 2005 summarizing this analysis is available upon request.
2. Cost data provided by UTIMCO represents actual reported expenses through FY05; FY06 forecasts full fiscal year expenses based on nine months of actual reported expenses (through May 31, 2006); and FY07 UTIMCO Services and Direct Costs to Funds are the budget as approved by the UTIMCO Board on July 25, 2006.
3. Estimates for FY07 of external management fees and performance fees netted from asset values are provided by UTIMCO staff. Other Fees and Expenses for FY07 are budgeted by the U. T. System.

II. Value Added: FY02 - FY06

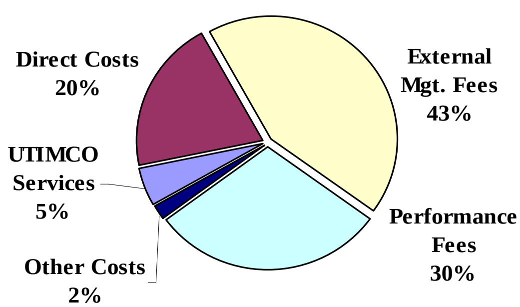
Table 1 below shows UTIMCO's value added for the PUF and the GEF in dollar terms and as a multiple of both total costs and performance fees paid to third party managers. More than half of the total value of approximately $1.3 billion was added in FY03. Value added estimates for FY06 will not be final until this fall, but performance YTD indicates value added may be zero, excluding the ITF. Performance fees at 40% of total costs cumulatively during the five year period were recovered by a factor of 4.0 X; however, there does not appear to be a smooth correlation between value added and performance fees or total costs. (See discussion of "Performance Fees" below.)

Table 1
UTIMCO Value Added versus Performance Fees and Total Costs FY02-FY06

	$Millions			Times Value Added	
Fiscal Year	**Value Added**	**Total Costs**	**Performance Fees**	**Total Costs**	**Performance Fees**
Projected FY06	0	213	86	0.0 X	0.0 X
FY05	458	215	105	2.1 X	4.3 X
FY04	206	157	66	1.3 X	3.1 X
FY03	701	123	48	5.7 X	14.5 X
FY02	(66)	91	16	(0.7) X	(4.2) X
Five-Year Cumulative	***1,299***	***798***	***322***	***1.6 X***	***4.0 X***

III. Total Investment Cost Trends: FY02 - FY06

The chart below illustrates that budgeted costs including UTIMCO services, direct costs to funds, and other U. T. System fees and expenses represent about 27% of projected total costs in FY06. UTIMCO Services costs support internal UTIMCO staff management of about 18% of the total assets ($3.6 billion); selection and monitoring of external managers for 82% of the assets ($16.4 billion); and client reporting and administration for all System funds.



UTIMCO does not budget for fees and expenses that are netted against asset values for investments in mutual funds, partnerships, and hedge funds managed by third parties. This practice is typical for institutional investors because performance and related costs are impossible to predict. These expenses comprise nearly three-quarters of total investment management costs. Table 2 provides details and Table 3 summarizes cost trends in the following categories:

- UTIMCO Services - direct expenses incurred by UTIMCO operations.
- Direct Costs to Funds - external management and performance fees, custody, legal, audit, consulting, risk management system, and other expenses paid directly by the funds.
- External asset management fees (excluding performance fees) netted from reported asset values for investments in third party mutual funds, partnerships, and hedge funds.
- Performance fees netted from asset values by third party managers for performance exceeding benchmarks tailored to their individual investment objectives and asset mixes.
- Other Fees and Expenses paid to U. T. System Administration and Institutions – education fee, endowment compliance fee, investment oversight, and audit expenses.

Tables 2 and 3 present actual cost data for four fiscal years ending August 31, 2005; projected costs for FY06 based on nine months of actual costs reported through May 31, 2006; and budgeted/estimated FY07 costs. Average total assets under management (AUM) include operating funds for all years; FY06 and FY07 AUMs are based on UTIMCO estimates. Centralized operating fund expenses are reflected during FY06 and FY07; expenses and asset values associated with PUF West Texas Lands are not included. Private capital partnership expenses that are netted from asset values include management fees and other partnership expenses, but performance fees and carried interests are not reported here.

Table 2
U. T. System Total Investment Cost Summary

($ millions)	FY02	FY03	FY04	FY05	Proj. FY06	*Five-Year Cum.*	Budget/ Estimate FY07
AVERAGE TOTAL ASSETS UNDER MANAGEMENT (AUM)	**13,716**	**14,034**	**15,470**	**17,245**	**20,185**		**21,187**
UTIMCO BUDGETED EXPENSES:							
UTIMCO Services Expenses	4.97	7.61	8.79	10.17	10.51	***42***	13.27
UTIMCO Services % of AUM	0.04%	0.05%	0.06%	0.06%	0.05%	***0***	0.06%
Direct Costs to Funds	20.10	16.05	25.51	33.84	43.36	***139***	43.42
Direct Costs to Funds % of AUM	0.15%	0.11%	0.16%	0.20%	0.21%		0.20%
Total UTIMCO Budgeted Expenses Paid Directly	25.07	23.65	34.30	44.00	53.87	***148***	56.69
Total UTIMCO Budgeted Expenses Paid Directly % of AUM	**0.18%**	**0.17%**	**0.22%**	**0.26%**	**0.27%**		**0.27%**
EXTERNAL MANAGEMENT FEES NETTED FROM ASSET VALUES:							
Non-Marketable Alternative Assets - Private Capital	36.00	32.10	36.50	38.60	44.20	***187***	54.60
Marketable Alternative Assets - Hedge Funds	11.80	16.40	20.30	30.50	21.50	***101***	57.70
Public Markets Assets	-	-	-	2.90	15.60	***19***	23.40
Mutual Fund Assets - Management Fees	2.80	4.20	5.70	4.50	10.20	***27***	9.00
Total External Mgmt. Fees Netted from Asset Values	50.60	52.70	62.50	76.50	91.50	***334***	144.70
Total External Mgmt. Fees Netted from Asset Values % of AUM	**0.37%**	**0.38%**	**0.40%**	**0.44%**	**0.45%**		**0.68%**
Total Direct Expenses & Netted External Mgmt. Fees w/o Perf.	**75.67**	**76.35**	**96.80**	**120.50**	**145.37**	***515***	**201.39**
Total Direct Expenses & Netted External Mgmt. Fees w/o Perf. % of AUM	**0.55%**	**0.54%**	**0.63%**	**0.70%**	**0.72%**		**0.95%**
PERFORMANCE FEES NETTED FROM ASSET VALUES:							
Marketable Alternative Assets - Performance Fees	12.00	44.00	56.90	90.50	52.00	***255***	62.70
Public Markets Assets - Performance Fees	-	-	-	-	11.00	***11***	19.90
Total Performance Fees Netted from Asset Values	12.00	44.00	56.90	90.50	63.00	***266***	82.60
Total Performance Fees Netted from Asset Values % of AUM	**0.09%**	**0.31%**	**0.37%**	**0.52%**	**0.31%**		**0.39%**
TOTAL UTIMCO COSTS INCLUDING PERFORMANCE FEES	**87.7**	**120.4**	**153.7**	**211.0**	**208.4**	***781***	**284.0**
Total UTIMCO Costs including Performance Fees % of AUM	**0.64%**	**0.86%**	**0.99%**	**1.22%**	**1.03%**		**1.34%**
U. T. SYSTEM FEES AND EXPENSES:							
Education Fee (LTF Only)	0.55	0.54	0.67	0.76	0.86	***3***	0.93
Endowment Compliance Fee (LTF only; paid to U. T. Institutions)	2.38	2.44	2.38	2.53	2.72	***12***	3.14
Investment Oversight Fee -- U. T. System Finance	-	-	-	0.50	0.80	***1***	1.01
U. T. System Internal Audit Fee	-	-	-	0.03	0.03	***0***	0.03
Total U. T. System Fees and Expenses	**2.93**	**2.98**	**3.05**	**3.82**	**4.40**	***17***	**5.11**
Total U. T. System Fees and Expenses % of AUM	**0.02%**	**0.02%**	**0.02%**	**0.02%**	**0.02%**		**0.02%**
TOTAL INVESTMENT MANAGEMENT COSTS	**90.6**	**123.3**	**156.7**	**214.8**	**212.8**	***798***	**289.1**
TOTAL INVESTMENT MANAGEMENT COSTS % OF AUM	**0.66%**	**0.88%**	**1.01%**	**1.25%**	**1.05%**		**1.36%**

"**Total Direct Expenses & Netted External Mgmt. Fees w/o Perf.**" in Table 2 above are comparable to the Cambridge Associates "UTIMCO Cost Study," completed May 5, 2005. The study compared UTIMCO expense data for twelve months ending June 30, 2004, to a privately surveyed peer group of large public and private endowments. Performance Fees for hedge funds, partnerships, and mutual funds were excluded in the study because comparable peer data was not available. Cost increases in FY05 and projected in FY06 placed UTIMCO above the FY04 median for the study's peer universe and for private endowments surveyed, but still below the FY04 median for large public endowments.

Endowment compliance fees (the largest component of U. T. System fees and expenses) are for the Long Term Fund only, not the PUF, and are paid directly to the institutions, not to U. T. System Administration. Texas A&M shares fees and expenses indirectly, with reduced net asset value of their 1/3 share of the PUF.

Table 3
U. T. System Total Investment Cost Trend Summary

($ millions)	FY02	FY03	FY04	FY05	Proj. FY06	*Five-Year Cum.*	Budget/ Estimate FY07
UTIMCO Services	5.0	7.6	8.8	10.2	10.5	***42***	13.3
Direct Costs to Funds	20.1	16.0	25.5	33.8	43.4	***139***	43.4
External Fees Netted from Asset Values	50.6	52.7	62.5	76.5	91.5	***334***	144.7
Performance Fees Netted from Investment Returns	12.0	44.0	56.9	90.5	63.0	***266***	82.6
Miscellaneous Other Fees and Expenses:	2.9	3.0	3.0	3.8	4.4	***17***	5.1
TOTAL INVESTMENT MANAGEMENT COSTS	**90.6**	**123.3**	**156.7**	**214.8**	**212.8**	***798***	**289.1**
TOTAL % OF AVERAGE ASSETS MANAGED	**0.66%**	**0.88%**	**1.01%**	**1.25%**	**1.05%**		**1.36%**

IV. Performance Fees

Performance fees paid to third party managers have increased dramatically from $16 million in FY02 (0.12% of average assets managed - AUM) to a high of $105 million in FY05 (0.61% of AUM), and a projected total of approximately $86 million in FY06 (0.43% of AUM). Performance fees paid in years when value added is less than or equal to zero overall results when performance by some managers exceed their individual benchmarks but the portfolios overall under-perform policy portfolio composite benchmarks. Derivative positions and other internal management activities also influence portfolio asset exposures and overall portfolio performance, for better or for worse.

Table 4 shows performance fees paid directly to managers under external agency contracts and those netted from asset values for marketable alternatives (hedge funds) and public markets investment funds (mutual funds, limited partnerships, other). Performance fees netted from asset values by non-marketable alternatives managers (private capital limited partnerships) are not reported separately from management fees; and public markets assets investment in funds with performance fees netted from asset values only report these separately during FY06.

Table 4
UTIMCO Performance Fee Summary FY02-FY07

($ millions)	FY02	FY03	FY04	FY05	Proj. FY06	*Five-Year Cum.*	Budget/ Estimate FY07
Direct Costs (External Agency Agreements)	3.9	4.5	9.2	14.9	23.2	***56***	20.6
Public Market Assets (Netted from Asset Values)	-	-	-	-	11.0	***11***	19.9
Marketable Alternatives -- Hedge Funds (Netted from Asset Values)	12.0	44.0	56.9	90.5	52.0	***255***	62.7
TOTAL PERFORMANCE FEES	**15.9**	**48.5**	**66.1**	**105.4**	**86.2**	***322***	**103.2**
TOTAL % OF AVERAGE ASSETS MANAGED	**0.12%**	**0.35%**	**0.43%**	**0.61%**	**0.43%**		**0.49%**
Value Added	**(66.0)**	**701.0**	**206.0**	**458.0**	**-**	***1,299***	
X Total Performance Fees	**(4.2)**	**14.5**	**3.1**	**4.3**	**-**	***4***	**-**

Pages 124-128 are intentionally left blank

16. U. T. Medical Branch - Galveston: Discussion of implementation of Performance Improvement Plan

REPORT

President Stobo will address the Board on issues related to implementation of the findings and recommendations of an external performance improvement review conducted by Navigant Consultants at U. T. Medical Branch – Galveston.

17. U. T. System Board of Regents: Report on the Archer Center, Washington, D.C.

REPORT

Vice Chancellor for Federal Relations William Shute will report on the Archer Center following a PowerPoint presentation set forth on Pages 1 - 11 in the Supplemental Materials (Volume 2) of the Agenda Book.

BACKGROUND INFORMATION

Upon his retirement from Congress in 2000, Congressman Bill Archer, of the 7th District of Texas, worked with the U. T. System to establish an intensive semester-based program of academics and internship for U. T. System students. The Archer Center Fellowship Program began as a collaboration between U. T. Austin and the U. T. System Office of Federal Relations located in Washington, D.C., with the stated purpose of introducing the best and brightest undergraduate students from Texas to the federal process. The Archer Center slogan states, "Where Texas Meets the World."

The program began with 12 students during Spring 2001 and since has been host to 162 upper-division undergraduate students. The original class was populated with only U. T. Austin students, but has expanded to each of the nine academic campuses. U. T. Brownsville selected its first Archer Fellow this past spring.

Prospective Fellows apply on their home campus and are submitted to a rigorous application and interview process. Once selected, each Fellow works with the Program Director to find an internship in Washington that matches his or her degree matriculation, work experience, and career goals. But unlike most Washington intern programs, Archer Fellows do not work in a Congressional office by default. Over the course of the past five years, the program has helped place students in the White House, at the World Bank, at embassies, in polling firms, at Cable News Network (CNN), in the public affairs shop of the Smithsonian, and in federal agencies, as well as Capitol Hill. Archer alumni have gone on to numerous post-graduate programs of the first caliber (at institutions including Oxford, Columbia, and Harvard), and many are working in prestigious positions within various governments. Currently, Archer alums are working in the White House and at federal agencies, teaching in Israel, and working as the Border Director for President Vincente Fox's Secretary of External Relations in Mexico.

The program is supported by a small endowment that has been funded by individuals, corporations, and charitable foundations. In addition, in 2005, the Archer Center was awarded two Department of Education grants with the help of the Texas Congressional Delegation.

H. RECESS FOR MEETINGS OF THE STANDING COMMITTEES AND COMMITTEE REPORTS TO THE BOARD

I. RECONVENE AS COMMITTEE OF THE WHOLE

19. U. T. System: Request to adopt resolution regarding the U. T. System Police Academy

RECOMMENDATION

The Chancellor concurs in the recommendation of the Vice Chancellor for Administration and the Director of the Office of Police that the U. T. System Board of Regents adopt the following resolution committing their continued support and endorsement of The University of Texas System Police Academy for the purpose of training law enforcement officers for the U. T. System:

RESOLUTION

Whereas, The University of Texas System Police Academy was created and established by The University of Texas System in 1968, and was licensed by the Texas Commission on Law Enforcement Officer Standards and Education in 1969;

Whereas, The University of Texas System Board of Regents recognizes the importance of training Law Enforcement Officers for The University of Texas System Institutions;

Whereas, The University of Texas System Police Academy through the Office of the Director of Police provides the training to these Law Enforcement Officers for the purpose of performing their duties in a professional, prepared, and skilled manner;

Whereas, The Texas Commission on Law Enforcement Officer Standards and Education issues a license to a training academy that meets the requirements of training Law Enforcement Officers; and

Whereas, The University of Texas System Police Academy meets all licensing requirements as set forth by the Texas Commission on Law Enforcement Officer Standards and Education.

NOW THEREFORE BE IT RESOLVED, that we, the members of The University of Texas System Board of Regents hereby continue to support and endorse the establishment of The University of Texas System Police Academy for the purpose of training Law Enforcement Officers for The University of Texas System.

BACKGROUND INFORMATION

As reported to the U. T. System Board of Regents in January 26, 1968, and October 23, 1970, the U. T. System Police Academy (formerly known as Basic Training Schools) was created and established in 1968 and received licensure from the Texas Commission on Law Enforcement Officer Standards and Education (TCLEOSE) in 1969. The need for this ministerial act follows a result of a recent audit of TCLEOSE. TCLEOSE requested the U. T. System provide a resolution from the Academy's governing board to complete the Commission's files.

An overview of the U. T. System police operations, including the Academy, was provided at the May 2004 Student, Faculty, and Staff Campus Life Committee meeting.

19. U. T. System Board of Regents: Presentation of certificate of appreciation to Director of Police Roy R. Baldridge

Chairman Huffines and Chancellor Yudof will present a certificate of appreciation to Director of Police Roy R. Baldridge for his distinguished service and outstanding contributions as a leader, administrator, and teacher at The University of Texas at Austin and The University of Texas System. Mr. Baldridge has served as Director of Police for the U. T. System for the past 10 years and has announced plans to retire effective August 31, 2006.