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FOR
FINANCE AND PLANNING COMMITTEE

Committee Meeting: 8/22/2007

Board Meeting: 8/23/2007
Austin, Texas

Robert B. Rowling, Chairman
John W. Barnhill, Jr.
H. Scott Caven, Jr.
Cyndi Taylor Krier
Colleen McHugh

		Committee Meeting	Board Meeting	Page
9.	**U. T. System: Approval of aggregate amount of $102,957,000 of equipment financing for Fiscal Year 2008 and resolution regarding parity debt**	*2:55 p.m.* **Action** *Mr. Aldridge*	**Action**	**101**
10.	**U. T. System Board of Regents: Adoption of Eighteenth Supplemental Resolution authorizing Revenue Financing System Bonds in an amount not to exceed $675,000,000; adoption of a standard provisions resolution; authorization to complete all related transactions; and resolution regarding parity debt**	*2:58 p.m.* **Action** *Mr. Aldridge*	**Action**	**104**
11.	**U. T. System Board of Regents: Report on Treasury Working Group**	*3:01 p.m.* **Report** *Dr. Kelley*	Not on Agenda	**106**
12.	**U. T. System Board of Regents: Approval of amendments to the Allocation Policy for Non-Endowment Funds**	*3:08 p.m.* **Action** *Dr. Kelley*	**Action**	**108**
13.	**U. T. System Board of Regents: Investment Reports for the fiscal quarter ended May 31, 2007, and The University of Texas Investment Management Company (UTIMCO) Performance Summary Report**	*3:12 p.m.* **Report** *Mr. Zimmerman*	**Report**	**111**
14.	**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)**	*3:17 p.m.* **Action** *Mr. Zimmerman*	**Action**	**118**
Adjourn		*3:25 p.m.*		

1. <u>U. T. System: Discussion and appropriate action related to approval of *Docket No. 131*</u>

<u>RECOMMENDATION</u>

It is recommended that *Docket No. 131*, beginning on Page Docket - 1, be approved.

It is also recommended that the Board confirm that authority to execute contracts, documents, or instruments approved therein has been delegated to appropriate officials of the respective institution involved.

Supplemental Materials: Green pages following the Docket tab at the back of Volume 2 of the Agenda Book.

2. <u>U. T. System: Key Financial Indicators Report and Monthly Financial Report</u>

Dr. Scott C. Kelley, Executive Vice Chancellor for Business Affairs, will discuss the Key Financial Indicators Report, as set forth on Pages 63 - 71, and the June Monthly Financial Report. The reports represent the consolidated and individual operating results of the U. T. System institutions.

<u>REPORT</u>

The Key Financial Indicators Report compares the System-wide quarterly results of operations, key revenues and expenses, reserves, and key financial ratios in a graphical presentation from Fiscal Year 2003 through May 2007. Ratios requiring balance sheet data are provided for Fiscal Year 2002 through Fiscal Year 2006.

The Monthly Financial Report is provided as support for the Key Financial Indicators. The Report includes the detailed numbers behind the System-wide graphs as well as detail for each individual institution as of June 2007.

Supplemental Materials: June Monthly Financial Report on Pages 37 - 62 of Volume 2.

THE UNIVERSITY OF TEXAS SYSTEM

QUARTERLY KEY FINANCIAL INDICATORS REPORT

3RD QUARTER FY 2007

KEY

Actual 2002 through 2006 amounts
(SOURCE: Annual Financial Reports Fiscal Years 2002, 2003, 2004, 2005 and 2006)

2007 Budget amounts
(SOURCE: Operating Budget Summary 2007)

Projected 2007 amounts
(trend based on the average change of the previous four years of data)

Monthly Financial Report Year to Date amounts for May 2006 and May 2007

Annual State Net Revenue Collections for 2002, 2003, 2004, 2005 and 2006
(SOURCE: Texas Revenue History by Source 1978-2006, State Comptroller's Office)

Year to Date State Net Revenue Collections for May 2006 and May 2007
(SOURCE: State Comptroller's Office)

Estimated State Revenue Collections for 2007
(SOURCE: Revenue Estimate for the 79th Legislature 3rd Called Session, April 2006, State Comptroller's Office)

2002, 2003, 2004, 2005 & 2006 Annual Average of FTEs, and Average of 1st, 2nd, & 3rd Quarter 2007 FTEs
(SOURCE: State Auditor's Office Quarterly FTE Report)

Year to Date margin for June 2007
(SOURCE: Monthly Financial Report for June 2007)

Projected 2007
(SOURCE: Monthly Financial Report Year- End Projections collected June 2007)

Year to Date margin for June 2006
(SOURCE: Monthly Financial Report for June 2007)

Target Normalized Rates

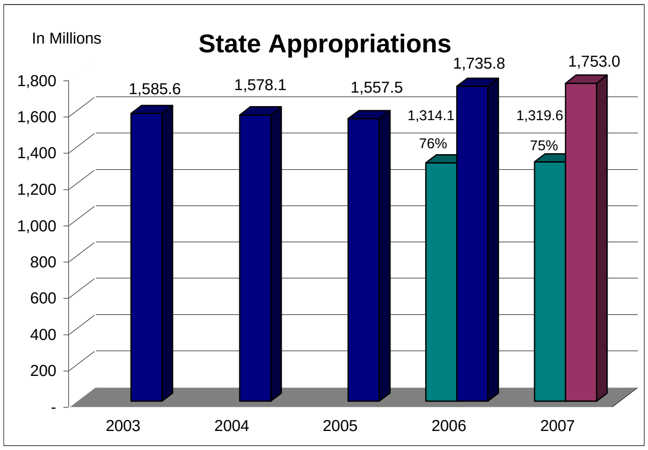
Aaa/Aa1 Median
(SOURCE: Moody's)

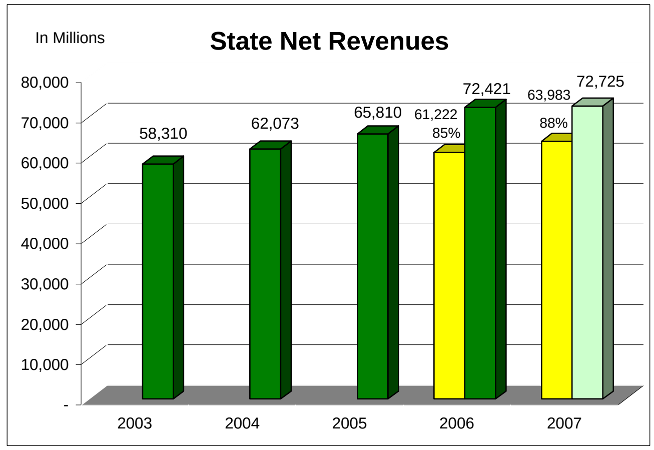
A2 Median
(SOURCE: Moody's)

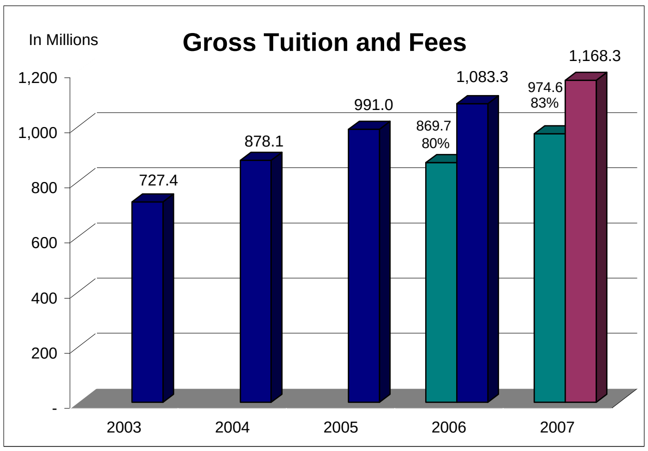
Fair Facilities Condition Index (5% - 10%)

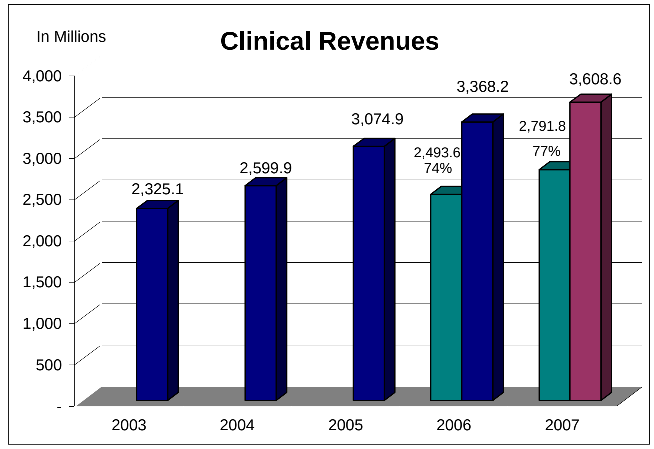
Good Facilities Condition Index (Exceeds 10%)

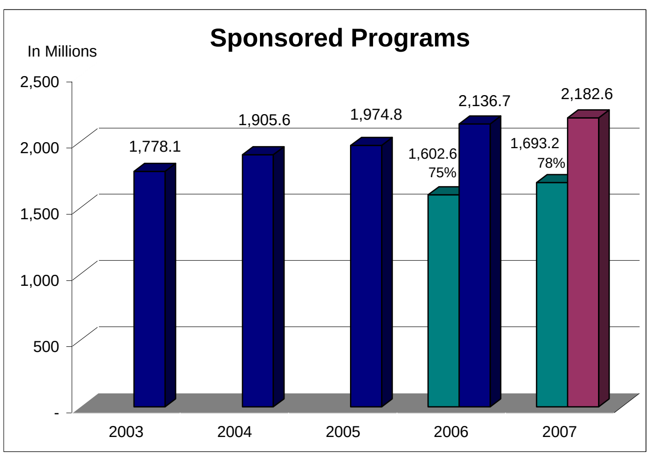
KEY INDICATORS OF REVENUES
ACTUAL 2003 THROUGH 2006
PROJECTED 2007
YEAR TO DATE 2006 AND 2007 FROM MAY MONTHLY FINANCIAL REPORT

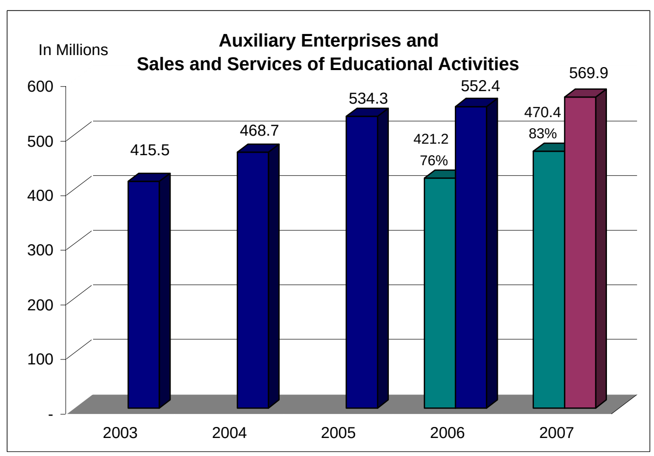


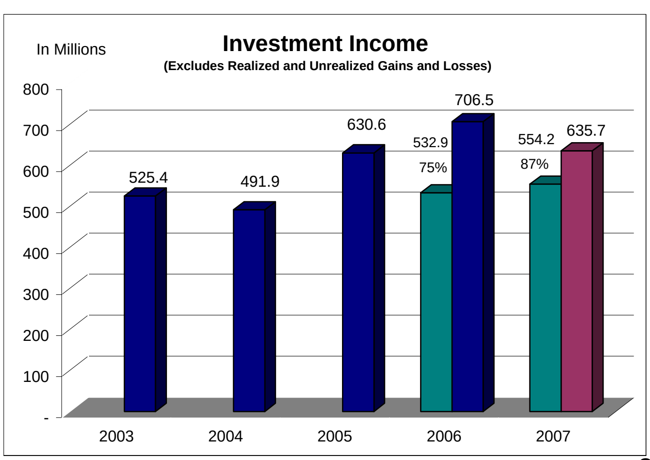


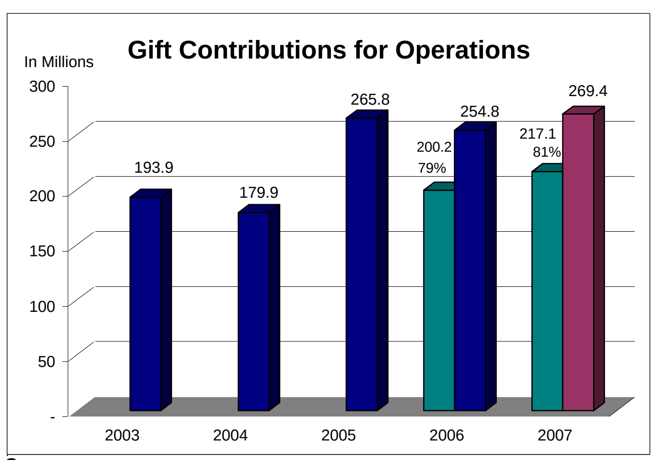




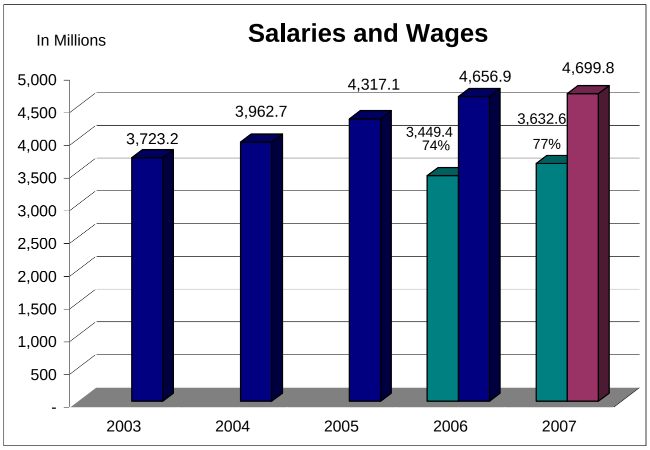


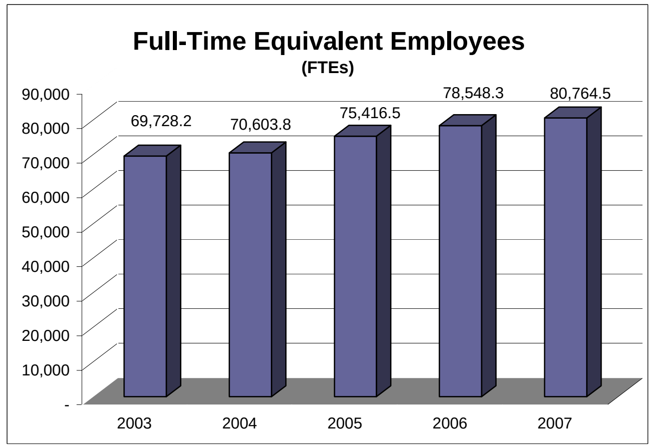


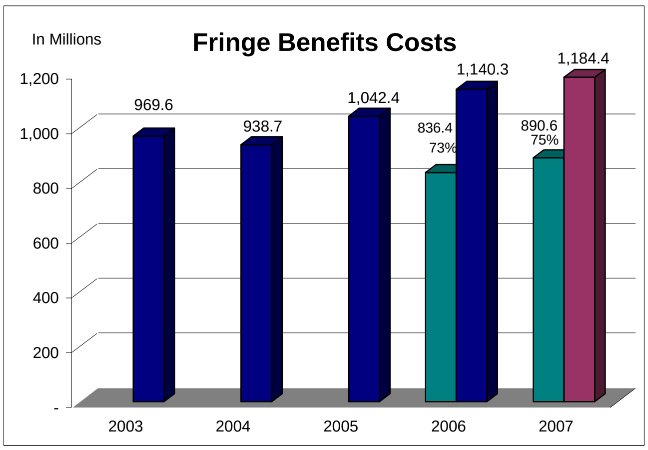


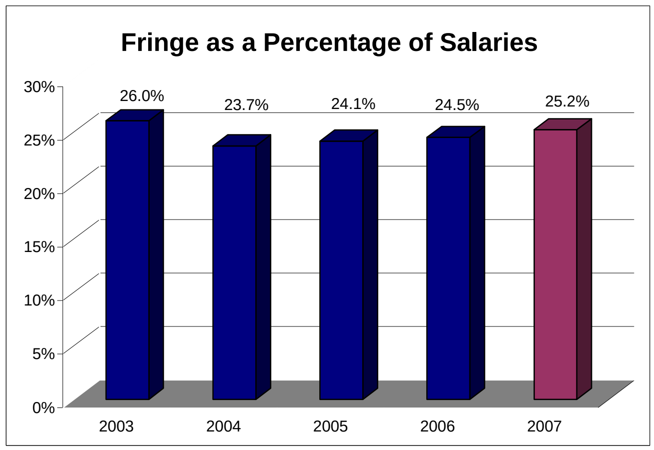


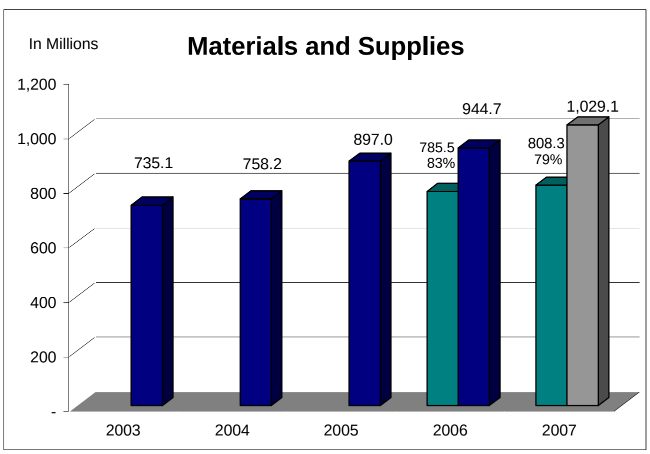
KEY INDICATORS OF EXPENSES
ACTUAL 2003 THROUGH 2006
PROJECTED 2007
YEAR TO DATE 2006 AND 2007 FROM MAY MONTHLY FINANCIAL REPORT

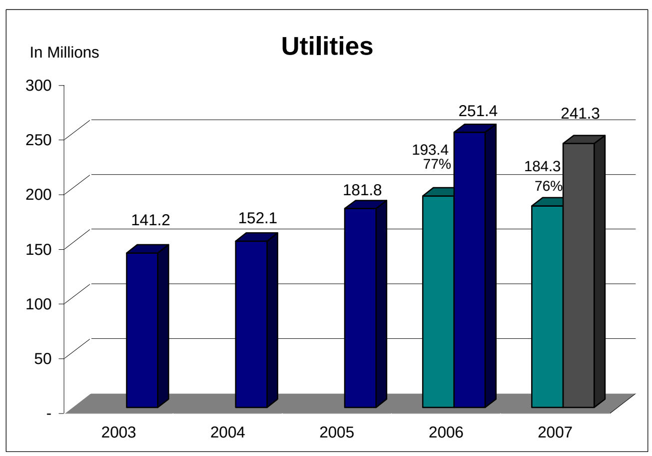


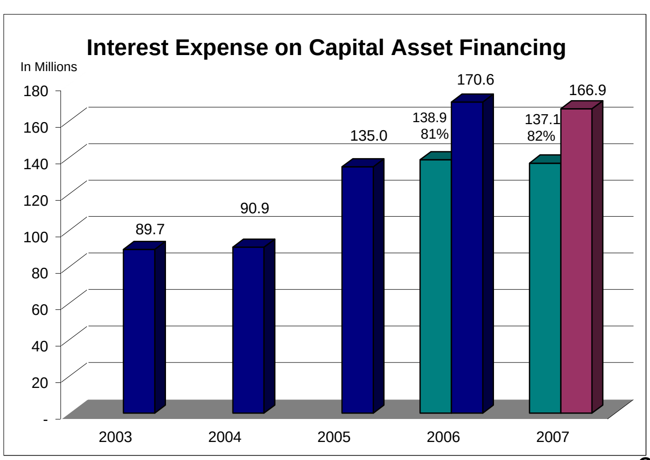


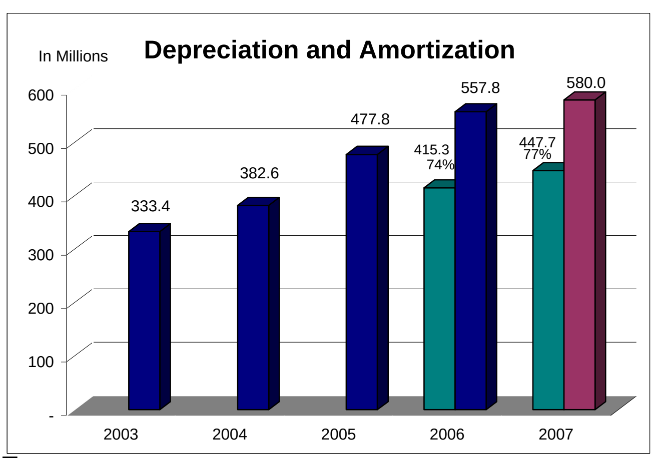




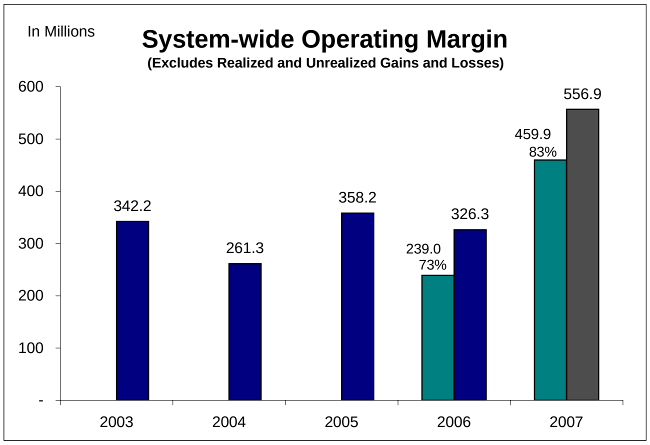


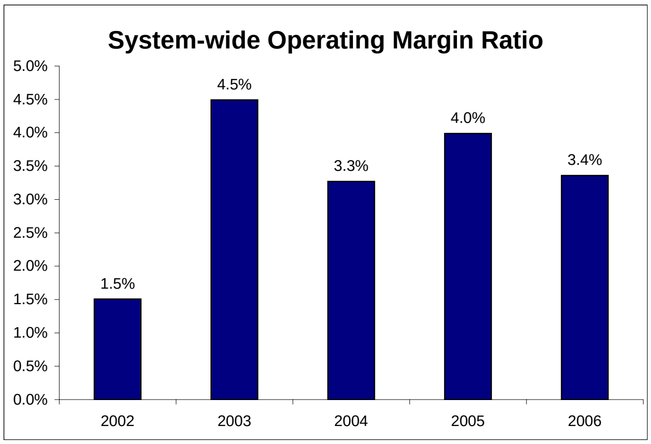


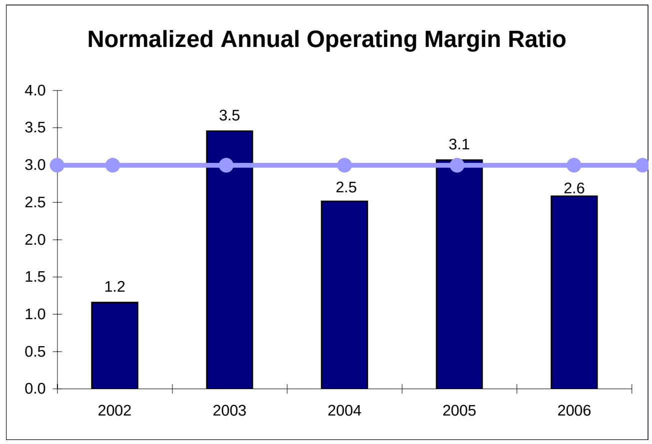


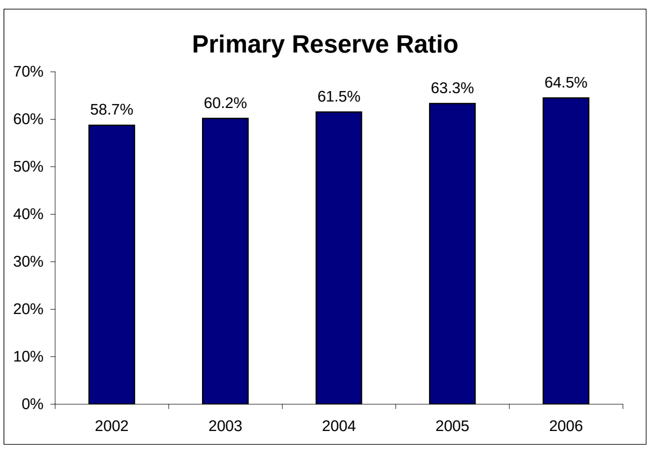


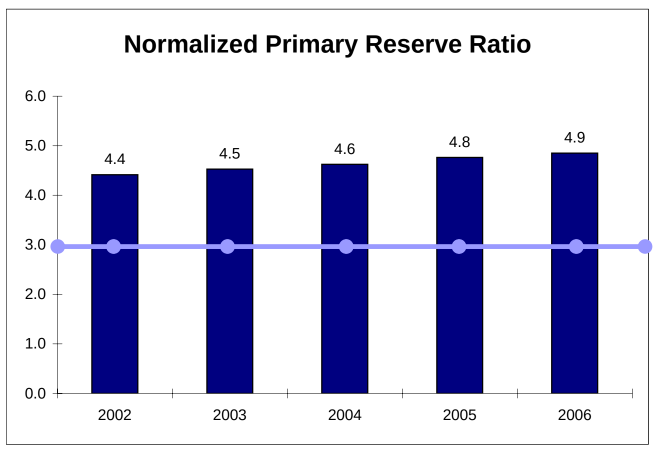
KEY INDICATORS OF RESERVES
ACTUAL 2003 THROUGH 2006
PROJECTED 2007
YEAR TO DATE 2006 AND 2007 FROM MAY MONTHLY FINANCIAL REPORT

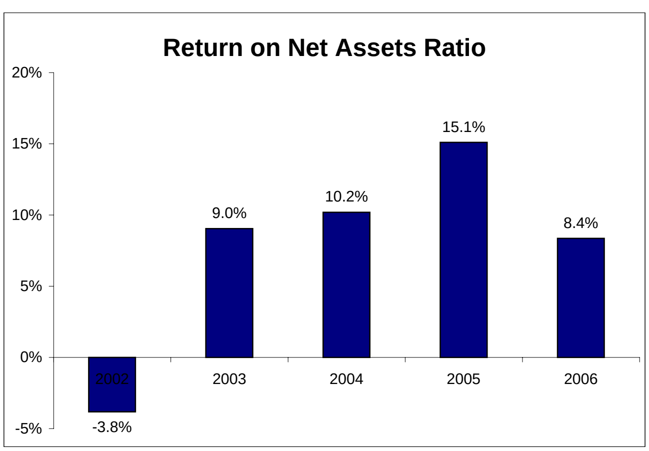


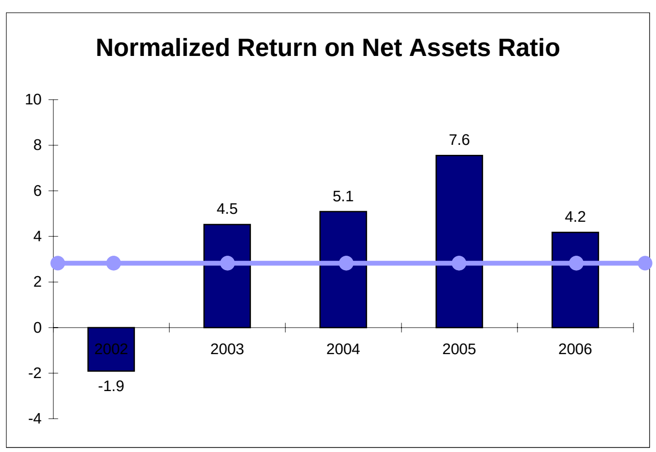




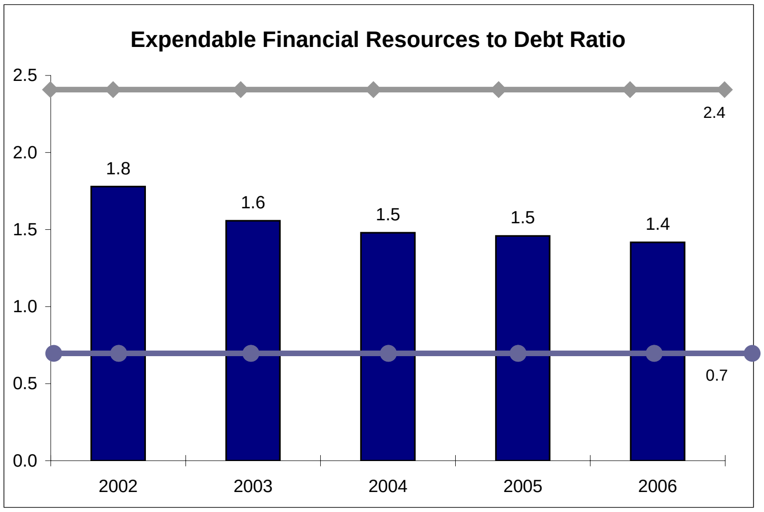


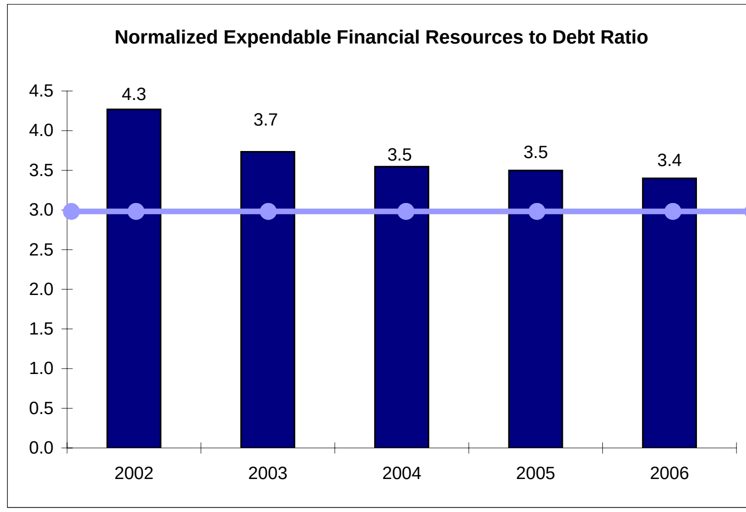


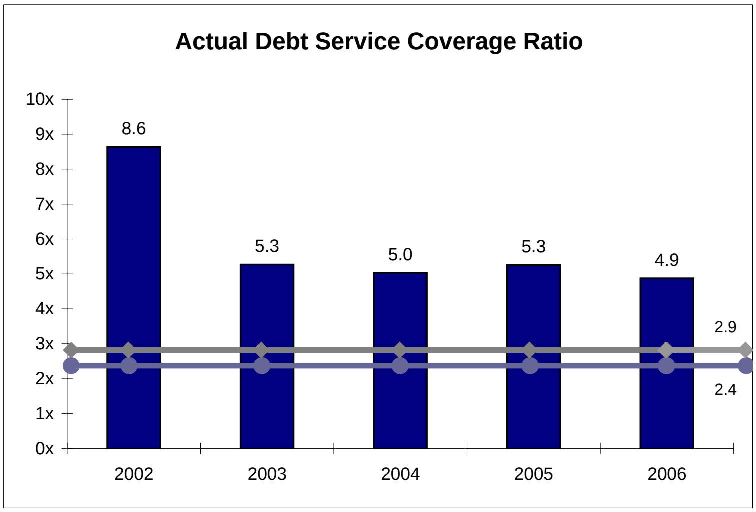


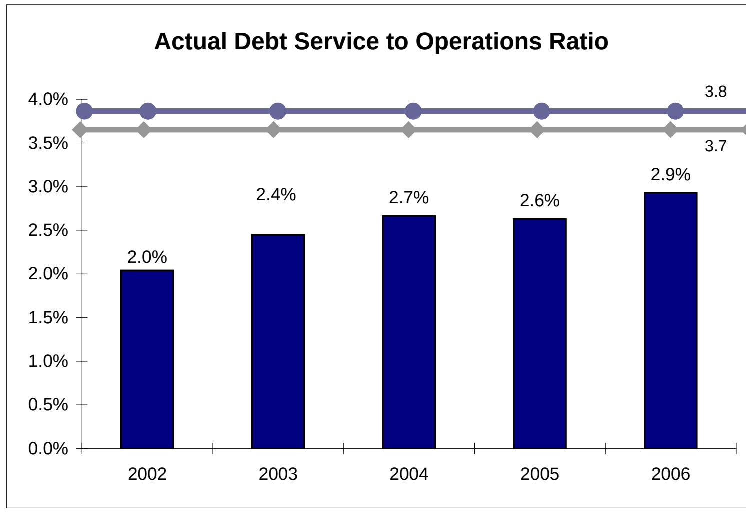


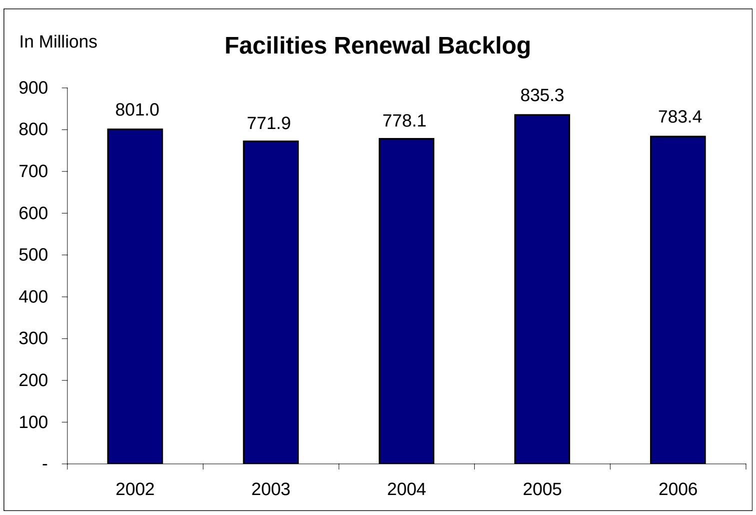
KEY INDICATORS OF CAPITAL NEEDS AND CAPACITY
2002 THROUGH 2006

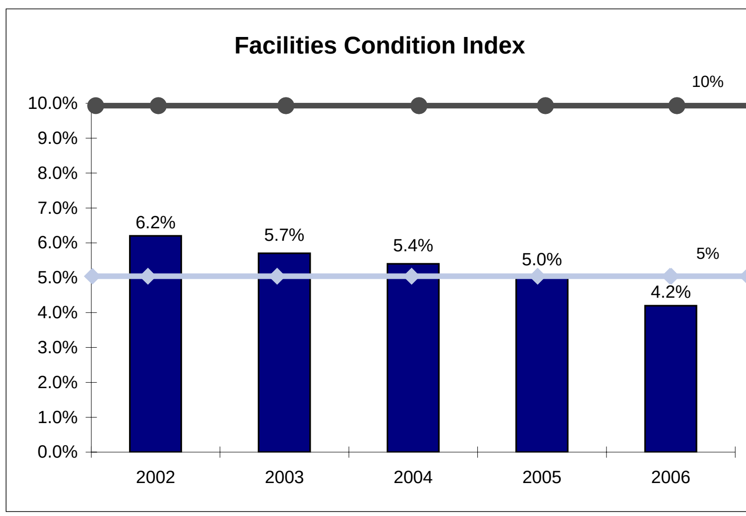




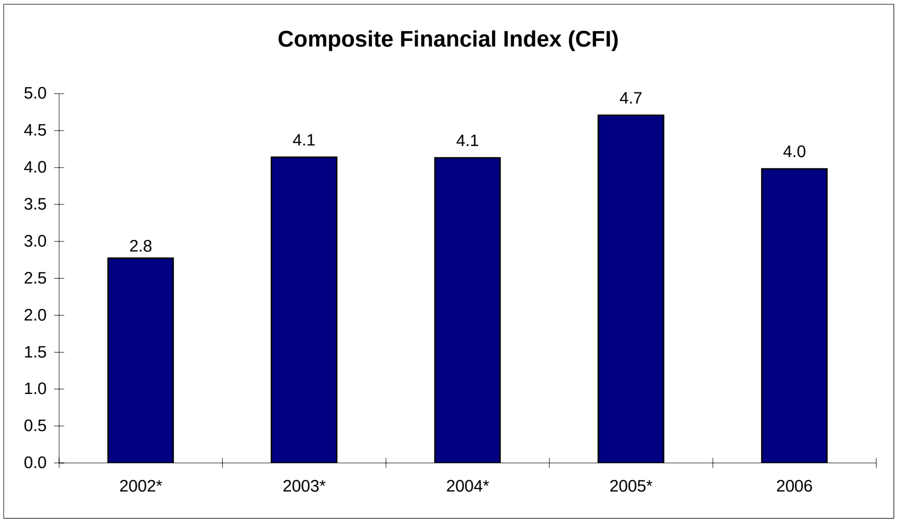




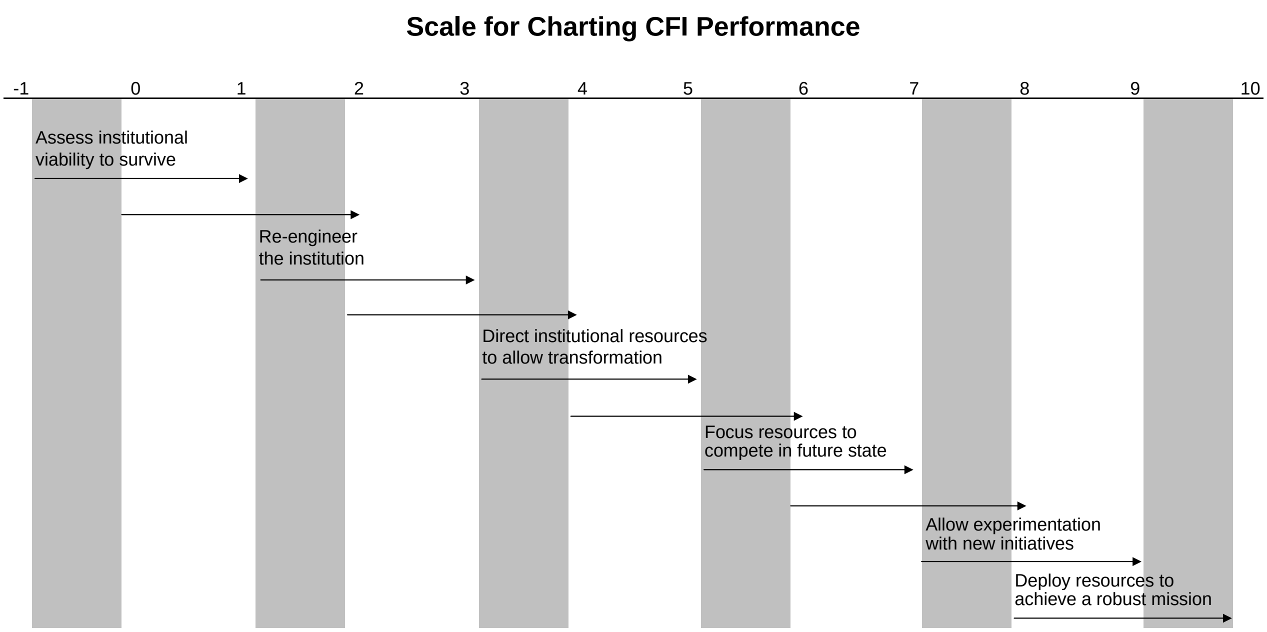




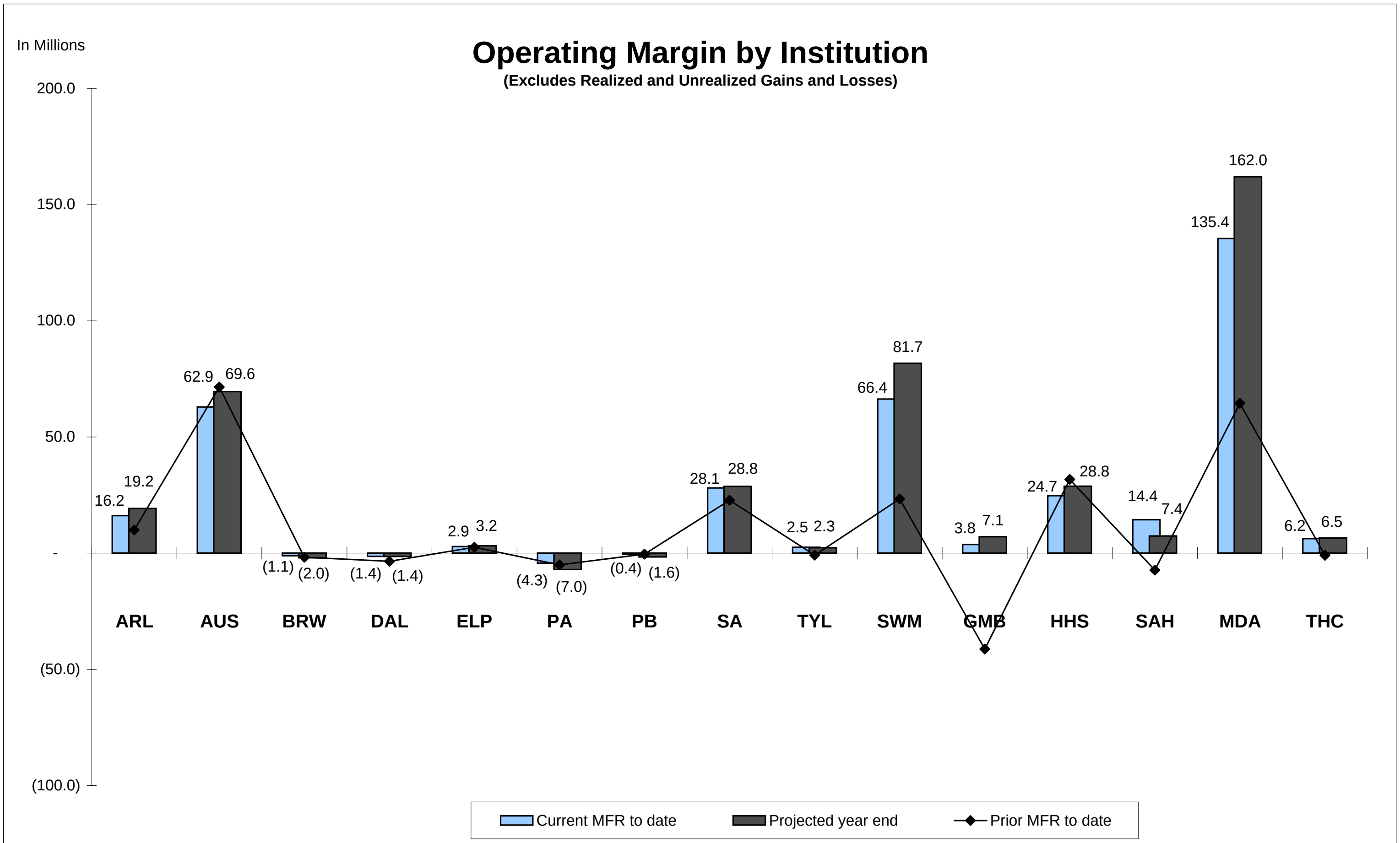
KEY INDICATORS OF FINANCIAL HEALTH
2002 THROUGH 2006

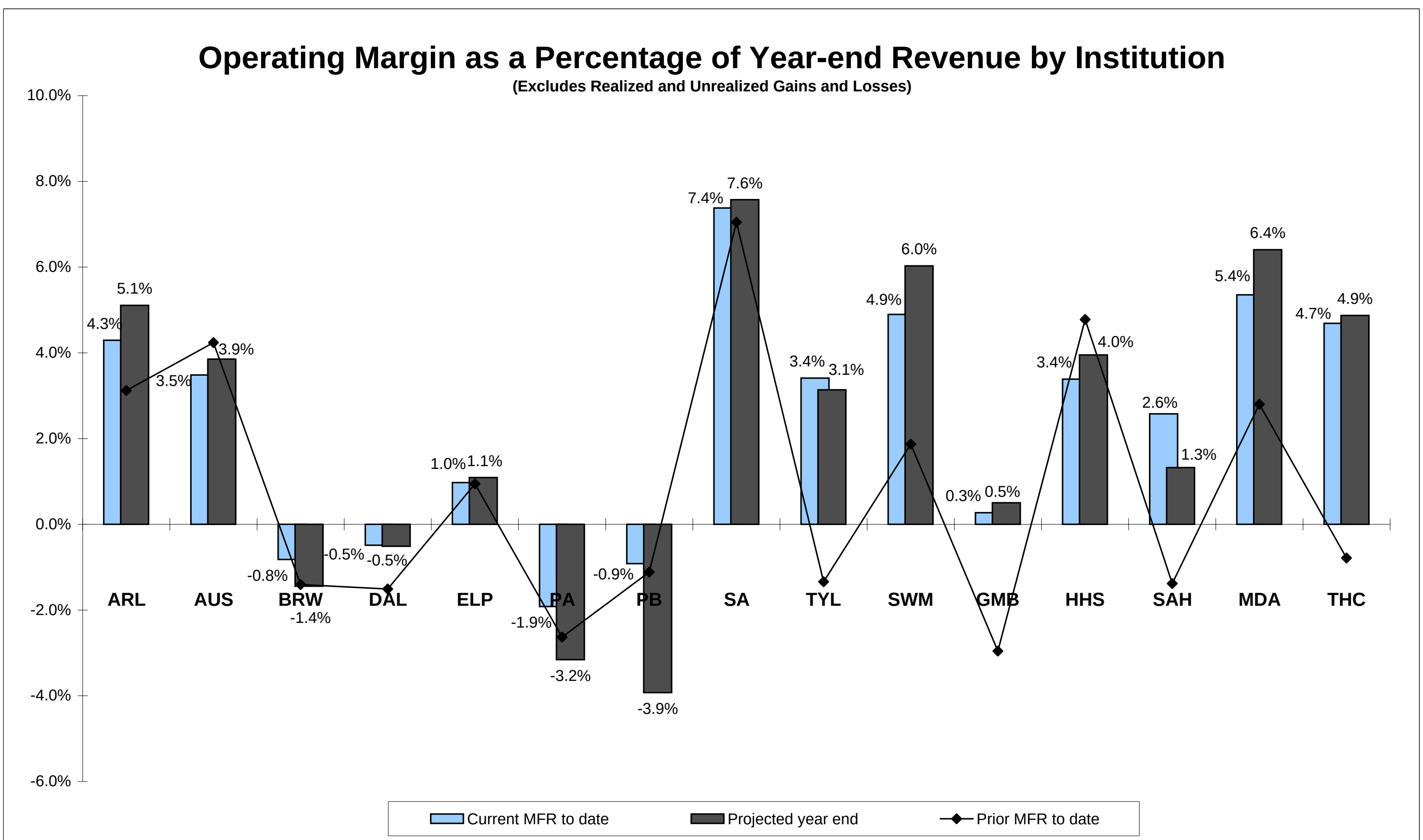


*Restated to reflect appreciation on endowments as restricted expendable net assets as a result of the 2006 external audit.
Permanent University Fund Appreciation Restatements are not included above.



KEY INDICATORS OF RESERVES
YEAR TO DATE 2006 AND 2007 FROM JUNE MONTHLY FINANCIAL REPORT
PROJECTED 2007 YEAR-END MARGIN





3. U. T. System: Approval of transfer of funds between Legislative Appropriation items during the biennium beginning September 1, 2007

RECOMMENDATION

The Chancellor, with the concurrence of the Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Business Affairs, the Executive Vice Chancellor for Health Affairs, and presidents of the U. T. System institutions, recommends that the U. T. System Board of Regents adopt the resolution that follows to provide for the most effective utilization of General Revenue Appropriations during the biennium beginning September 1, 2007.

RESOLUTION

Pursuant to the appropriate transfer provisions of the General Appropriations Act of the 80th Legislature, it is hereby resolved that the State Comptroller be requested to make necessary transfers within the Legislative Appropriations (and/or Informational Items of Appropriation) from the General Revenue Fund as authorized by the Chief Financial Officer of each entity as follows:

The University of Texas at Arlington
The University of Texas at Austin
The University of Texas at Brownsville
The University of Texas at Dallas
The University of Texas at El Paso
The University of Texas - Pan American
The University of Texas of the Permian Basin
The University of Texas at San Antonio
The University of Texas at Tyler
The University of Texas Southwestern Medical Center at Dallas
The University of Texas Medical Branch at Galveston
The University of Texas Health Science Center at Houston
The University of Texas Health Science Center at San Antonio
The University of Texas M. D. Anderson Cancer Center
The University of Texas Health Center at Tyler
The University of Texas System Administration

BACKGROUND INFORMATION

This resolution is a standard action by the U. T. System Board of Regents at the beginning of each biennium and is pursuant to provisions of the General Appropriations Act, Article III, Section 4, enacted by the 80th Texas Legislature.

4. U. T. System: Approval to exceed the full-time equivalent limitation on employees paid from appropriated funds

RECOMMENDATION

The Chancellor concurs in the recommendation of the 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 affected U. T. System institutions that the U. T. System Board of Regents approve allowing those institutions, as set forth in the table on Page 74, to exceed the number of full-time equivalent (FTE) employees paid from appropriated funds for Fiscal Year 2008 that are authorized in Article III of the General Appropriations Act. Also, as required by Article IX, Section 6.10 of the General Appropriations Act, it is recommended that the U. T. System Board of Regents submit a request to the Governor's Office and the Legislative Budget Board to grant approval for these institutions to exceed the authorized number of FTE employees paid from appropriated funds.

Supplemental Materials: Detailed justification information on Pages 63 - 65 of Volume 2.

BACKGROUND INFORMATION

The General Appropriations Act places a limit on the number of FTE employees paid from appropriated funds that an institution may employ without written approval of the Governor and the Legislative Budget Board. To exceed the FTE limitation, a request must be submitted by the governing board and must include the date on which the board approved the request, a statement justifying the need to exceed the limitation, the source of funds to be used to pay the salaries, and an explanation as to why the functions of the proposed additional FTEs cannot be performed within current staffing levels.

U. T. Austin, U. T. Dallas, U. T. Pan American, U. T. Permian Basin, U. T. Medical Branch - Galveston, U. T. Health Science Center - Houston, U. T. Health Science Center - San Antonio, and U. T. Health Center - Tyler will be under the FTE cap and are not requesting to exceed the FTE limitation.

The University of Texas System
Request to Exceed Full-time Equivalent Limitation on Employees Paid From Appropriated Funds
For Period Septemer 1, 2007 through August 31, 2008

Request to Exceed Cap - by NACUBO Function

	Faculty	Staff	Total
Instruction	513.16	239.17	752.33
Academic Support	-	9.80	9.80
Research	80.52	172.72	253.24
Public Service	1.70	3.66	5.36
Hospitals and Clinics	33.35	731.23	764.58
Institutional Support	-	135.46	135.46
Student Support	-	29.67	29.67
Operations and Maintenance of Plant	-	351.59	351.59
Scholarships and Fellowships	-	1.25	1.25
Total	628.73	1,674.55	2,303.28

Request to Exceed Cap - by Institution

		Request to Exceed Cap			
	FY 2008 Cap	Faculty	Staff	Total	
U. T. Arlington	2,247.90	10.00	-	10.00	
U. T. Austin	6,619.10	-	-	-	*
U. T. Brownsville	554.00	128.17	153.05	281.22	
U. T. Dallas	1,322.60	-	-	-	*
U. T. El Paso	1,797.90	17.50	12.50	30.00	
U. T. Pan American	1,896.10	-	-	-	*
U. T. Permian Basin	306.40	-	-	-	*
U. T. San Antonio	2,041.00	36.20	1.30	37.50	
U. T. Tyler	481.80	18.61	17.30	35.91	
Total Academic Institutions	17,266.80	210.48	184.15	394.63	
U. T. Southwestern Medical Center	1,240.10	373.40	401.70	775.10	
U. T. Medical Branch - Galveston	5,534.70	-	-	-	*
U. T. Health Science Center - Houston	1,869.60	-	-	-	*
U. T. Health Science Center - San Antonio	2,516.70	-	-	-	*
U. T. M. D. Anderson Cancer Center	11,947.20	44.85	1,078.70	1,123.55	
U. T. Health Center - Tyler	740.70	-	-	-	*
Total Health Institutions	23,849.00	418.25	1,480.40	1,898.65	
U. T. System Administration	249.00	-	10.00	10.00	
U. T. System Total	41,364.80	628.73	1,674.55	2,303.28	

* U. T. Austin, U. T. Dallas, U. T. Pan American, U. T. Permian Basin, U. T. Medical Branch - Galveston, U. T. Health Science Center - Houston, U. T. Health Science Center - San Antonio, and U. T. Health Center - Tyler will not exceed their cap.

NACUBO - National Association of College and University Business Officers

5. U. T. System: Approval of Optional Retirement Program employer contribution rates for Fiscal Year 2008

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Business Affairs, the Executive Vice Chancellor for Health Affairs, and the Vice Chancellor for Administration that the U. T. System Board of Regents approve the Optional Retirement Program (ORP) employer contribution rates for Fiscal Year 2008 as follows:

a. 8.5% for all institutions and U. T. System Administration with respect to employees who participated in the ORP prior to September 1, 1995; and

b. for all other employees, an employer contribution rate as recommended by each institution and set forth on Page 77.

Supplemental Materials: Institution ORP Rate Surveys on Pages 66 - 81 of Volume 2.

BACKGROUND INFORMATION

Prior to September 1, 1995, the ORP employer contribution rate was 8.5% for all ORP participants. An enactment by the 74th Texas Legislature reduced ORP employer contributions to participants from 8.5% to 6.0%, effective September 1, 1995. However, U. T. System was permitted to "grandfather" those employees participating in the ORP during the 1994-95 biennium. This resulted in a two-tiered ORP employer contribution rate for U. T. System employees: those who participated in ORP during the 1994-95 biennium continued to receive 8.5%, while those who did not participate during the 1994-95 biennium received 6.0%.

The 78th Texas Legislature enacted *Texas Government Code*, Section 830.2015, which expanded the definition of a grandfathered employee from one who had participated during the 1994-95 biennium to one who had participated in ORP prior to September 1, 1995. The legislation also granted permissive authority for institutions of higher education to set the ORP employer contribution rate for grandfathered and nongrandfathered participants at any percentage level between the amount appropriated by the State and 8.5%. In the General Appropriations Act, the 80th Legislature has increased the appropriated rate from 6.0% to 6.58% for the 2008-09 biennium. It is not required that the rate be the same for grandfathered employees nor that the rate be the same for all U. T. System institutions.

Given the diversity of the U. T. System institutions and the differential budget impact for each institution, each institutional president was asked to propose its ORP employer contribution rates for grandfathered and nongrandfathered participants as noted in the chart on Page 77.

- For Fiscal Year 2008, with respect to grandfathered employees hired prior to September 1, 1995, all U. T. System institutions elected to continue the current 8.5% employer contribution rate.

- For nongrandfathered participants hired after September 1, 1995, five institutions (U. T. Arlington, U. T. Austin, U. T. Dallas, U. T. Pan American, and U. T. Southwestern Medical Center - Dallas) have proposed to increase the ORP employer contribution rate from the rate established by the Board for Fiscal Year 2007.

- Of the five, U. T. Arlington recommends an increase in the contribution rate from 6.5% to 7.0% while the remaining four propose an increase in the contribution rate from 7.0% to 7.5%.

- Six institutions (U. T. Permian Basin, U. T. San Antonio, U. T. Tyler, U. T. Medical Branch - Galveston, U. T. M. D. Anderson Cancer Center, and U. T. Health Center - Tyler) and U. T. System Administration will continue the contribution rate of 8.5% as approved by the Board for Fiscal Year 2007.

- The remaining institutions (U. T. Brownsville, U. T. El Paso, U. T. Health Science Center - Houston, and U. T. Health Science Center - San Antonio) will adopt the rate of 6.58% as established by the legislature.

The governing board of an institution of higher education has the authority to set the ORP employer contribution rates in accordance with rules issued by the Texas Higher Education Coordinating Board. Under those rules, the governing board is to determine the employer contribution rates once per year, to be effective for the entire year. All institutions plan to implement the employer contribution rates effective September 1, 2007, with the exception of U. T. Austin. Because of the number of employees this will impact and the required analysis of each individual's tax deferrals to ensure compliance with the *Internal Revenue Code*, U. T. Austin proposes implementation of the new employer contribution rate change beginning with paychecks issued on or after January 1, 2008.

Approval of this Agenda Item will authorize all U. T. System institutions with the exception of U. T. Austin to implement the ORP employer contribution rates on September 1, 2007, and authorize U. T. Austin to implement beginning with paychecks issued on or after January 1, 2008.

The University of Texas System
FY 2008 Optional Retirement Program Contribution Rates

Grandfathered Employees	2007 Approved Rate	2008 Proposed Rate	2008 Participants	2008 Total Cost	Cost Above 6.58%
U. T. Arlington	8.50%	8.50%	437	3,381,723	763,805
U. T. Austin*	8.50%	8.50%	1,361	16,243,713	3,669,168
U. T. Brownsville	8.50%	8.50%	136	779,551	176,087
U. T. Dallas	8.50%	8.50%	201	1,806,730	408,320
U. T. El Paso	8.50%	8.50%	248	1,606,745	362,935
U. T. Pan American	8.50%	8.50%	165	1,029,832	232,621
U. T. Permian Basin	8.50%	8.50%	33	220,991	49,918
U. T. San Antonio	8.50%	8.50%	290	2,111,436	476,936
U. T. Tyler	8.50%	8.50%	94	590,498	133,383
U. T. Southwestern Medical Center - Dallas	8.50%	8.50%	498	7,596,696	1,715,959
U. T. Medical Branch - Galveston	8.50%	8.50%	1,126	8,400,462	1,897,516
U. T. Health Science Center - Houston	8.50%	8.50%	472	5,930,470	1,339,589
U. T. Health Science Center - San Antonio	8.50%	8.50%	481	5,343,391	1,206,978
U. T. M. D. Anderson Cancer Center	8.50%	8.50%	511	9,590,842	2,166,401
U. T. Health Center - Tyler	8.50%	8.50%	44	448,479	101,303
U. T. System Administration	8.50%	8.50%	34	381,630	86,203
TOTAL			6,131	$ 65,463,189	$ 14,787,122

Nongrandfathered Employees	2007 Approved Rate	2008 Proposed Rate	2008 Participants	2008 Total Cost	Cost Above 6.58%
U. T. Arlington	6.50%	7.00%	345	1,784,077	150,000
U. T. Austin*	7.00%	7.50%	1,390	8,784,550	1,077,572
U. T. Brownsville	6.00%	6.58%	154	576,566	-
U. T. Dallas	7.00%	7.50%	315	2,531,030	311,315
U. T. El Paso	6.00%	6.58%	405	1,708,487	-
U. T. Pan American	7.00%	7.50%	243	1,162,091	142,549
U. T. Permian Basin	8.50%	8.50%	73	358,324	80,939
U. T. San Antonio	8.50%	8.50%	412	2,264,209	511,445
U. T. Tyler	8.50%	8.50%	159	886,448	200,233
U. T. Southwestern Medical Center - Dallas	7.00%	7.50%	1,275	10,483,118	1,285,929
U. T. Medical Branch - Galveston	8.50%	8.50%	617	7,726,608	1,745,304
U. T. Health Science Center - Houston	6.00%	6.58%	650	5,894,180	-
U. T. Health Science Center - San Antonio	6.00%	6.58%	650	5,195,761	-
U. T. M. D. Anderson Cancer Center	8.50%	8.50%	949	14,065,343	3,177,113
U. T. Health Center - Tyler	8.50%	8.50%	44	992,931	197,277
U. T. System Administration	8.50%	8.50%	40	478,637	108,114
TOTAL			7,721	$ 64,892,360	$ 8,987,790

*U. T. Austin will implement on 1/1/2008.

6. U. T. System: Discussion regarding estimated costs associated with the U. T. System-wide common chart of accounts initiative

PURPOSE

Executive Vice Chancellor Kelley will discuss the U. T. System-wide common chart of accounts initiative, including engaging Alvarez & Marsal, a global professional services firm, to assist in developing a common chart of accounts to facilitate improved consolidated System-wide financial reporting.

There are two phases proposed for this initiative: the Planning Phase and the Delivery Phase. Due to the estimated costs of the Delivery Phase, it is important to focus on the initiative in its entirety when discussing this recommendation.

This recommendation relates to the Planning Phase and is made with the intent that the actions proposed be designed and implemented by a U. T. System-wide working group consisting of staff from the U. T. System Office of the Controller and accounting and information technology management professionals from several U. T. System institutions assigned by the Executive Vice Chancellor for Business Affairs. The working group would be supplemented by the outside consultant to assist with identifying implementation strategies and specifications.

The Executive Vice Chancellor for Business Affairs will report to the Finance and Planning Committee of the Board after the Planning Phase to seek approval of a specific plan for implementation.

Dr. Kelley will discuss the proposed scope of the Planning Phase and a roadmap for the Planning and Delivery Phases.

Supplemental Materials: Project Roadmap and Chart of Project Cost on Pages 82 - 83 of Volume 2.

BACKGROUND INFORMATION

The Management Letter related to the 2005 U. T. System-wide Consolidated Financial Statements audit contained an observation that the process of creating consolidated financial statements by physically combining the data from the institutions into a complex spreadsheet is prone to errors, does not provide an audit trail, and makes generating interim financials for management purposes more burdensome. To address this observation, the Executive Vice Chancellor for Business Affairs formed a Common Chart of Accounts Ad Hoc Committee with representatives from U. T. System Administration, U. T. Austin, U. T. Southwestern Medical Center - Dallas, and U. T. M. D. Anderson Cancer Center. The Committee was charged with developing an action plan for developing a common chart of accounts for consolidated reporting purposes.

Alvarez & Marsal, a professional services firm, was selected through a competitive bid process to provide consulting services for U. T. M. D. Anderson Cancer Center for a similar project involving an accounting key design. A representative from U. T. System Administration and a member of the Ad Hoc Committee attended the presentations of the finalists in that process. After discussing the credentials of Alvarez & Marsal and an overview of their strategy and approach for the U. T. System initiative, the Common Chart of Accounts Ad Hoc Committee met with representatives of the firm to outline and further define the objectives of the project.

The Planning Phase will include a review and analysis of the reporting process resulting in a gap assessment and documentation of functional and technical requirements. A project work plan will be developed for fully implementing the initiative. A model chart of accounts and data model will be developed for use in vendor selection and evaluation criteria for a financial reporting software provider. The final step in the Planning Phase will be a project plan with an overall cost estimate for the Delivery Phase. This would include software licensing and maintenance, hardware, and consulting fees for project management and business process design. The consulting fees would include full testing and deployment of the system, change management, and training the users. Alvarez & Marsal's estimate at this time for the Delivery Phase, without the benefit and knowledge gained from having performed the Planning Phase, ranges from $2.045 to $3.305 million with a median of $2.675 million.

The main objective of harmonizing the charts of accounts is to speed the consolidation, closing, and reporting cycles by reducing the amount of manual work required for their completion. Other benefits include greater transparency and limiting the chance of fraud and errors that are the inevitable by-product of any manual system. The direct expense of having to maintain dissimilar charts of accounts is the extra time required to roll up and consolidate the periodic results. Indirect costs include lags in getting critical business information to management, limited transparency, lack of accountability, and distorted measurements of operating results.

The Ad Hoc Committee believes that developing a common chart of accounts will facilitate improved reporting and controls. Further, it will ultimately boost efficiency by providing faster, streamlined report processing in a consistent manner, resulting in more informed decision-making. The common chart of accounts will also provide a basis for institutions to use when changing or developing their accounting systems.

The cost of the Planning Phase is estimated at $549,380. The project will ultimately have an estimated cost of approximately $3.5+ million. This is a best-guess estimate at this stage and is without the benefit and knowledge the consultants will gain from having performed the Planning Phase.

Due to the extensive amount of time the project will require from the accounting staffs throughout the U. T. System, it will be necessary to time the project around the deadlines associated with the annual financial report. The project will be completed in Fiscal Year 2009 with reporting capabilities to begin in Fiscal Year 2010.

7. U. T. System Board of Regents: Adoption of a Resolution authorizing the issuance, sale, and delivery of Permanent University Fund Bonds not to exceed $300,000,000, adoption of Liquidity Resolution, and authorization to complete all related transactions

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Business Affairs that the U. T. System Board of Regents

a. adopt a Resolution, substantially in the form previously approved by the U. T. System Board of Regents, authorizing the issuance, sale, and delivery of Board of Regents of The University of Texas System Permanent University Fund Bonds in one or more installments in an aggregate principal amount not to exceed $300,000,000 to be used to refund certain outstanding Permanent University Fund Bonds, to refund all or a portion of the then outstanding Permanent University Fund Flexible Rate Notes, Series A, to provide new money to fund construction and acquisition costs and to pay the costs of issuance;

b. adopt a Liquidity Resolution, substantially in the form previously approved by the U. T. System Board of Regents, covenanting to provide internal liquidity support for certain Permanent University Fund Bonds issued by the U. T. System and authorizing amendments to the Security Purchase Agreement with The University of Texas Investment Management Company (UTIMCO), relating to the U. T. System's variable rate note and bond programs; and

c. authorize appropriate officers and employees of U. T. System as set forth in the resolutions to take any and all actions necessary to carry out the intentions of the U. T. System Board of Regents within the limitations and procedures specified therein; to make certain covenants and agreements in connection therewith; and to resolve other matters incident and related to the issuance, sale, security, and delivery of such bonds.

BACKGROUND INFORMATION

Adoption of the Resolution would authorize the advance or current refunding of a portion of certain outstanding Permanent University Fund (PUF) Bonds provided that an advance refunding exceeds a minimum 3% present value debt service savings threshold. An advance refunding involves issuing bonds to refund outstanding bonds more than 90 days in advance of the call date whereas a current refunding involves issuing bonds to refund outstanding bonds within 90 days of the call date. Refunding bonds are issued at lower interest rates thereby producing debt service savings. Adoption of this Resolution will provide the flexibility to select the particular bonds to be refunded depending on market conditions at the time of pricing.

As provided in the Resolution, the potential bonds to be refunded include the outstanding PUF Bonds, Series 1997, Series 2002A, Series 2004A&B, Series 2005A&B, and Series 2006A-C.

The Resolution would also authorize the current refunding of all or a portion of the PUF Flexible Rate Notes, Series A. The PUF Flexible Rate Note program is used to provide interim financing for PUF projects approved by the Board. Adoption of the Resolution will permit the interim financing provided through the Notes to be replaced with long-term financing. The Resolution also authorizes the issuance of bonds to provide new money to fund the capital costs of eligible projects.

Proceeds from the Bonds related to refunding outstanding debt will be used to purchase U.S. government or other eligible securities to be placed in one or more escrow accounts. Proceeds from the escrowed securities will be used to redeem the refunded bonds and the refunded Flexible Rate Notes.

On November 10, 2005, the U. T. System Board of Regents adopted a resolution covenanting to use lawfully available funds to purchase certain PUF notes and RFS variable rate debt obligations in the event these obligations could not be remarketed. Adoption of the proposed Liquidity Resolution would expand liquidity provided from lawfully available funds of the U. T. System Board of Regents to include variable rate PUF Bonds.

The proposed resolutions have been reviewed by outside bond counsel and the U. T. System Office of General Counsel.

> Note: The proposed resolutions are available online at http://www.utsystem.edu/bor/AgendaBook/Aug07/8-22&23-07Meetingpage.htm.

8. U. T. System Board of Regents: Amendment to the Regents' *Rules and Regulations*, Series 70202, concerning the Interest Rate Swap Policy, and adoption of resolutions authorizing certain bond enhancement agreements for Revenue Financing System debt and Permanent University Fund debt

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Business Affairs and the Vice Chancellor and General Counsel that the Regents' *Rules and Regulations*, Series 70202, concerning the Interest Rate Swap Policy, be amended as reflected in congressional style on Pages 84 - 90.

The Chancellor also concurs in the recommendation of the Executive Vice Chancellor for Business Affairs that the U. T. System Board of Regents adopt resolutions substantially in the form set out on Pages 91 - 100 (the Resolutions) authorizing appropriate officers of the U. T. System to enter into bond enhancement agreements related to its Revenue Financing System (RFS) and Permanent University Fund (PUF) debt programs in accordance with the amended U. T. System Interest Rate Swap Policy and to take any and all actions necessary to carry out the intentions of the U. T. System Board of Regents.

BACKGROUND INFORMATION

Regents' *Rules and Regulations*, Series 70202, concerning the Interest Rate Swap Policy, was approved by the U. T. System Board of Regents on February 13, 2003.

Prior to the passage of Senate Bill 968 by the 80th Legislature, the U. T. System Board of Regents executed interest rate swap agreements related to its RFS debt under general authority provided to various state and local issuers under *Texas Government Code*, Chapter 1371. Additionally, while the U. T. System Board of Regents has had specific legislative authority to execute swaps since 1985, it did not have specific authority to make payments under interest rate swap agreements related to PUF debt from Available University Fund (AUF) monies. During the 80th Legislative Session, various U. T. System staff worked with members of the Legislature on Senate Bill 968, which modernizes the statutory authority governing interest rate swaps and provides increased flexibility to issuers to better manage risk related to their debt programs.

Included in Senate Bill 968 is the addition of *Texas Education Code* Section 65.461, which provides specific authority to the U. T. System Board of Regents to enter into "bond enhancement agreements," which includes interest rate swaps and related agreements, in connection with administration of the U. T. System's RFS and PUF debt programs.

The proposed swap policy amendments are needed to update the policy to reference the new statutory authority provided to the U. T. System Board of Regents under *Texas Education Code* Section 65.461 to execute bond enhancement agreements related to both RFS and PUF debt, to accommodate changes made to *Texas Government Code*, Chapter 1371 by Senate Bill 968, and to make other nonsubstantive changes.

The International Swaps and Derivatives Association, Inc. (ISDA) Master Agreement is a standardized legal agreement for derivative transactions between swap counterparties that contains standardized definitions, terms, and representations governing such transactions. The U. T. System has ISDA Master Agreements in place with six swap counterparties related to RFS debt. The form of the ISDA Master Agreement has been previously approved by the U. T. System Board of Regents and each of these ISDA Master Agreements has been approved by the Texas Attorney General.

Approval of this item would (i) authorize the execution of additional ISDA Master Agreements related to PUF debt in substantially the same form as those previously approved by the U. T. System Board of Regents in connection with RFS debt, and (ii) authorize the execution of confirmations and other agreements to enter into bond enhancement agreement transactions related to RFS and PUF debt in accordance with the U. T. System Interest Rate Swap Policy. The determination to utilize bond enhancement agreements will be made based on market conditions at the time of pricing. The Chairman of the Board of Regents and the Chairman of the Finance and Planning Committee will be informed in advance of any proposed transactions to be undertaken pursuant to the resolutions.

> Note: The form of the PUF ISDA agreement has not been included as part of the agenda materials, but is available upon request.

1. Title

Interest Rate Swap Policy

2. Rule and Regulation

Sec. 1 Authority. *Texas Education Code*, Chapter 55, including Section 55.13, *Texas Education Code,* Chapter 65, including Section 65.461, and *Texas Government Code*, Chapter 1371, including Section 1371.056, authorize the Board of Regents (Board) of The University of Texas System (U. T. System) to enter into interest rate management agreements ~~swap transactions~~ and ~~related~~ bond enhancement agreements (collectively “swaps”). ~~Pursuant to this authority, the Board of Regents approved the Eighth Supplemental Resolution to the Master Resolution, authorizing the System to enter into Master Swap Agreements with certain counterparties, in 1999.~~

Sec. 2 Purpose. This policy will govern the use of ~~by the U. T. System of interest rate~~ swaps ~~transactions~~ in connection with the U. T. System’s management of its debt programs, including the Permanent University Fund and Revenue Financing System debt programs ~~for the purpose of either reducing the cost of existing or planned Revenue Financing System debt, or to hedge the interest rate of existing or planned Revenue Financing System debt~~. By using swaps in a prudent manner, the U. T. System can increase the U. T. System’s financial flexibility, provide opportunities for interest rate savings, allow the U. T. System to actively manage asset and liability interest rate risk, take advantage of market opportunities to ~~reduce costs~~ lower the overall cost of debt, ~~and reduce~~ balance interest rate risk, or hedge other exposures. The use of swaps must be tied directly to U. T. System debt instruments. The U. T. System shall not enter into ~~swap transactions~~ swaps for speculative purposes.

Sec. 3 Legality/Approval. Prior to entering into a swap~~To enter into a Master Swap Agreement (which governs each swap transaction)~~, the U. T. System must receive~~: 1)~~ approval from the Board of Regents (which may include a delegation of authority to an Authorized Representative to enter into one or more swaps) and any required~~; 2)~~ approvals ~~by~~ from the Texas Attorney General~~, 3) approval from~~ and the Texas Bond Review Board. ~~, and 4)~~ The U. T. System will also secure an opinion acceptable to the Authorized Representative from ~~bond~~ legal counsel that the ~~agreement relating to the~~ swap ~~transaction~~ is a legal, valid, and binding obligation of the U. T. System and that entering into the swap ~~transaction~~ complies with applicable State and federal laws.

Sec. 4 Form of Agreements. Each interest rate swap ~~new Master Swap Agreement~~ shall contain terms and conditions as set forth in the International Swaps and Derivatives Association, Inc. (ISDA) Master Agreement, as amended, and such other terms and conditions including schedules, credit support annexes and confirmations as deemed necessary by an Authorized Representative.

Sec. 5 Methods of Procuring Swaps. Swaps can be procured via competitive bids or on a negotiated basis ~~.~~with counterparties or its credit support providers having credit ratings of 'A' or 'A2' or better from Standard & Poor's or Moody's, respectively.

5.1 Competitive. The competitive bid should include a minimum of three firms. ~~with counterparty credit ratings of 'A' or 'A2' or better from Standard & Poor's or Moody's, respectively.~~ An Authorized Representative may allow a firm or firms not submitting the bid that produces the lowest cost to match the lowest bid and be awarded ~~up to~~ a ~~40%~~ specified percentage of the notional amount of the swap ~~transaction~~.

5.2 Negotiated. An Authorized Representative may procure swaps by negotiated methods in the following situations:

(a) A determination is made by an Authorized R~~r~~epresentative that due to the complexity of a particular swap ~~transaction~~, a negotiated bid would result in the most favorable pricing;~~.~~

(b) An Authorized Representative makes a determination that, in light of the facts and circumstances, doing so will promote the U. T. System's interests by encouraging and rewarding innovation; or~~.~~

(c) A determination is made by an Authorized Representative that a competitive bid would likely create market pricing effects that would be detrimental to the interests of the U. T. System.

Sec. 6 Counterparty Risk. Counterparty risk is the risk of a failure by one of the U. T. System's swap counterparties to perform as required under a swap. To mitigate this risk, the U. T. System will 1) diversify its exposure among highly rated swap counterparties satisfying the rating criteria set forth in Section 5 above; 2) require collateralization as set forth below; and 3) include an optional termination event if the counterparty (or its credit support provider, if applicable) is downgraded below a second (lower) threshold.

~~Management of Swap Transaction Risk. Certain risks are created when the U. T. System enters into any swap transaction. In order to manage the associated risks, guidelines and parameters for each risk category are as follows:~~

6.1 Value Owed by Counterparty. To limit and diversify the U. T. System's counterparty risk and to monitor credit exposure to each counterparty, the U. T. System may not enter into a swap ~~transaction~~ with an otherwise qualified counterparty unless the cumulative mark-to-market value owed by the counterparty (and its ~~unconditional guarantor~~ credit support provider, if applicable) to the U. T. System shall be less than or equal to ~~$30 million~~ the applicable threshold amount set forth in Section 6.3 below.

6.2 Calculation of Value Owed. The ~~$30 million limitation~~ value owed shall be the sum of all mark-to-market values between the subject counterparty and the U. T. System regardless of the type of swap ~~transaction~~, net of collateral posted by the counterparty. Collateral will consist of cash, U.S. Treasury securities, and Federal Agency securities guaranteed unconditionally by the full faith and credit of the U.S. Government. Collateral shall be deposited with a third party trustee acceptable to U. T. System or as mutually agreed upon between U. T. System and each counterparty.

6.3 ~~Limits~~ Threshold Amounts Based on Credit Rating. Specific threshold amounts ~~limits~~ by counterparty are based on the cumulative mark-to-market value of the swap(s) and the credit rating of the counterparty or its credit support provider. The ~~limits~~ threshold amounts are as follows:

(a) AAA / Aaa________$30 million
(b) AA+ / Aa1________$25 million
(c) AA / Aa2_________$20 million
(d) AA- / Aa3_________$15 million
(e) A+ / A1__________$10 million
(f) A / A2___________$ 5 million

6.4 Downgraded Rating. If ~~counterparty's~~ the credit rating of a counterparty or its credit support provider is downgraded such that the cumulative mark-to-market value of all swaps between such counterparty and the U. T. System exceeds the maximum permitted by this policy, the counterparty must ~~terminate a portion of the swap,~~ post collateral~~,~~ or provide other credit enhancement that is satisfactory to the U. T. System and ensures compliance with this policy.

Sec. 7 Termination Risk. The U. T. System shall consider the merits of including a provision that permits it to optionally terminate a swap ~~agreement~~ at any time over the term of the swap ~~agreement~~ (elective termination right). In general, exercising the right to optionally terminate ~~an agreement~~ a swap should produce a benefit to the U. T. System, either through receipt of a payment from a termination, or if a termination payment is made by the U. T. System, a conversion to a more beneficial debt instrument or credit relationship. If no other remedies are available, it is possible that a termination payment by the U. T. System may be required in the event of termination of a swap ~~agreement~~ due to a counterparty default or following a decrease in credit rating.

Sec. 8 Amortization Risk. The amortization schedules of the debt and associated swap ~~transaction~~ should be closely matched for the duration of the swap. Mismatched amortization schedules can result in a less than satisfactory hedge and create unnecessary risk. In no circumstance may (i) the notional amount of a swap exceed the principal amount of the related debt at any time, or (ii) the term of a swap ~~transaction~~ extend beyond the final maturity date of the ~~affected~~ related debt instrument, or in the case of a refunding transaction, beyond the final maturity date of the refunding bonds.

Sec. 9 Basis ~~Index~~ Risk. Basis risk arises as a result of movement in the underlying variable rate indices that may not be in tandem, creating a cost differential that could result in a net cash outflow from the U. T. System. Basis risk can also result from the use of floating, but different, indices. To mitigate basis risk, any index used as part of a swap ~~an interest rate swap agreement~~ shall be a recognized market index, including but not limited to the Securities Industry and Financial Markets Association (SIFMA)~~Bond Market Association~~ Municipal Swap Index ~~(BMA)~~ or the London Interbank Offered Rate (LIBOR).

Sec. 10 Tax Risk. Tax risk is the risk that tax laws will change, resulting in a change in the marginal tax rates on swaps and their underlying assets. Tax risk is also present in all tax-exempt debt issuances. The Office of Finance should continually monitor and evaluate tax risk ~~will need to understand and document tax risk for a contemplated swap transaction as part of the approval process~~.

Sec. 11 Interest Rate Risk. Additional interest rate risk can be created by entering into certain types of swaps. Interest rate risk is risk that costs associated with variable rate exposure increase as a result of changes in market interest rates. The Office of Finance will incorporate the impact of each swap on the overall debt portfolio.

Sec. 12 Annual Reporting. The Annual Financial Report prepared by the U. T. System and presented to the Board of Regents will discuss the status of all ~~interest rate~~ swaps. The report shall include a list of all swaps with notional value and interest rates, a list of counterparties (and credit support providers, if applicable) and their respective credit ratings, and other key terms.

3. Definitions

~~Counterparty Long-Term Debt Rating – lowest prevailing rating from Standard & Poor's / Moody's maximum cumulative mark-to-market value of swaps owed to System by counterparty (net of collateral posted).~~

Authorized Representative – includes the Executive Vice Chancellor for Business Affairs, the Vice Chancellor and General Counsel, the Associate Vice Chancellor for Finance, and the Director of Finance.

~~BMA Index – the Bond Market Association Municipal Swap Index, the principal benchmark for the floating rate payments for tax-exempt issuers. The index is a national rate based on a market basket of high-grade, seven-day, tax-exempt variable rate bond issues.~~

Counterparty – a participant in a swap ~~or other derivatives agreement~~ who exchanges payments based on interest rates or other criteria with another counterparty.

Counterparty Long-Term Debt Rating – lowest prevailing rating from Standard & Poor's / Moody's.

Hedge – a transaction entered into to reduce exposure to market fluctuations.

Interest Rate Swap – a swap ~~transaction~~ in which two parties agree to exchange future net cash flows based on predetermined interest rates or indices calculated on an agreed notional amount. ~~The~~ An interest rate swap is not a debt instrument and there is no exchange of principal.

ISDA Master Agreement – the International Swaps and Derivatives Association, Inc. (ISDA), is the global trade association for the derivatives industry. The ISDA Master Agreement is the basic governing document that serves as a framework for all interest rate swaps and certain other types of swaps ~~interest rate swap, swap enhancement, and derivative transactions~~ between two counterparties. It is a standard form used throughout the industry. It is typically negotiated once, prior to the first swap transaction, and remains in force for all subsequent swap transactions.

London Interbank Offered Rate (LIBOR) – the rate of interest at which banks borrow funds from other banks in the London interbank market. It is a commonly used benchmark for swaps~~interest rate transactions ranging from one month to one year~~.

Mark-to-Market – calculation of the value of a financial instrument (like an interest rate swap) based on the current market rates or prices of the underlying indices.

~~Master Resolution – the Amended and Restated Master Resolution Establishing The University of Texas System Revenue Financing System, adopted on February 14, 1991, amended on October 8, 1993 and August 14, 1997, and each supplemental resolution thereto authorizing parity debt.~~

Maximum cumulative mark-to-market – value of swaps owed to the U. T. System by counterparty (net of collateral posted).

Notional Amount – the size of the ~~interest rate~~ swap and the dollar amount used to calculate interest payments.

SIFMA Index - (formerly known as the Bond Market Association (BMA) Municipal Swap index). The principal benchmark for floating rate payments for tax-exempt issuers. The index is a national rate based on a market basket of high-grade, seven-day, tax-exempt variable rate bond issues.

A RESOLUTION AUTHORIZING THE EXECUTION AND DELIVERY OF BOND ENHANCEMENT AGREEMENTS RELATING TO REVENUE FINANCING SYSTEM DEBT AND AUTHORIZING AND APPROVING OTHER INSTRUMENTS AND PROCEDURES RELATING TO SAID AGREEMENTS

WHEREAS, the Board of Regents (the "Board") of The University of Texas System (the "System") is the governing body of the System, an institution of higher education under the *Texas Education Code* and an agency of the State of Texas; and

WHEREAS, on February 14, 1991, the Board adopted the First Amended and Restated Master Resolution Establishing The University of Texas System Revenue Financing System and amended such resolution on October 8, 1993, and August 14, 1997 (referred to herein as the "Master Resolution"); and

WHEREAS, unless otherwise defined herein, terms used herein shall have the meaning given in the Master Resolution; and

WHEREAS, the Master Resolution establishes the Revenue Financing System comprised of the institutions now or hereafter constituting components of the System that are designated "Members" of the Financing System by action of the Board and pledges the Pledged Revenues attributable to each Member of the Financing System to the payment of Parity Debt to be outstanding under the Master Resolution; and

WHEREAS, the Board has adopted the Supplemental Resolutions to the Master Resolution authorizing the issuance of Parity Debt thereunder as special, limited obligations of the Board payable solely from and secured by a lien on and pledge of Pledged Revenues pledged for the equal and proportionate benefit and security of all owners of Parity Debt; and

WHEREAS, the Board has previously entered into certain Executed Master Agreements (as defined herein) with certain counterparties setting forth the terms and conditions applicable to each Confirmation (as defined herein) executed thereunder; and

WHEREAS, the Board hereby desires to severally authorize each Authorized Representative (as defined in the System's Interest Rate Swap Policy) to enter into Bond Enhancement Agreements (as defined herein) from time to time, all as provided in this Resolution.

NOW THEREFORE BE IT RESOLVED, that

SECTION 1. Pursuant to the International Swaps and Derivatives Association, Inc. ("ISDA") Master Agreement dated as of December 6, 2005, between the Board and Bank of America, N.A., the ISDA Master Agreement dated as of December 6, 2005, between the Board and Goldman Sachs Mitsui Marine Derivative Products, L.P., the ISDA Master Agreement dated as of May 2, 2006, between the Board and JPMorgan Chase Bank, National Association, the ISDA Master Agreement dated as of December 6, 2005 and Amended and Restated as of

April 21, 2006, between the Board and Lehman Brothers Commercial Bank, the ISDA Master Agreement dated as of May 1, 2006, between the Board and Merrill Lynch Capital Services, Inc., and the ISDA Master Agreement dated as of December 6, 2005, between the Board and Morgan Stanley Capital Services Inc. (collectively, the "Executed Master Agreements") and any New Master Agreements (as defined below, and collectively with the Executed Master Agreements, the "Master Agreements") authorized by Section 4 of this Resolution, each Authorized Representative is hereby severally authorized to act on behalf of the Board in accepting and executing confirmations under one or more of the Master Agreements (each, a "Confirmation", and collectively with the applicable Master Agreement, a "Bond Enhancement Agreement") when, in his or her judgment, the execution of such Confirmation is consistent with this Resolution, the System's Interest Rate Swap Policy and either (i) the transaction is expected to reduce the net interest to be paid by the Board with respect to any then outstanding Parity Debt or Parity Debt anticipated to be issued in the future over the term of the Bond Enhancement Agreement or (ii) the transaction is in the best interests of the Board given the market conditions at the time.

SECTION 2. The Board hereby determines that any such Bond Enhancement Agreement entered into by an Authorized Representative pursuant to this Resolution is necessary or appropriate to place the Board's obligations with respect to its outstanding Parity Debt or Parity Debt anticipated to be issued in the future on the interest rate, currency, cash flow or other basis set forth in such Bond Enhancement Agreement as approved and executed on behalf of the Board by an Authorized Representative. Each Bond Enhancement Agreement constitutes a "Credit Agreement" as defined in the Master Resolution and a "bond enhancement agreement" under Section 65.461 of the *Texas Education Code* ("Section 65.461"). Pursuant to Section 65.461, a Bond Enhancement Agreement authorized and executed by an Authorized Representative under this Resolution shall not be considered a "credit agreement" under Chapter 1371 of the *Texas Government Code*, as amended ("Chapter 1371"), unless specifically designated as such by the Authorized Representative. In the event an Authorized Representative elects to treat a Bond Enhancement Agreement authorized by this Resolution as a "credit agreement" under Chapter 1371 and this Resolution has not previously been submitted to the Attorney General by an Authorized Representative, such Authorized Representative may submit this Resolution to the Attorney General for review and approval in accordance with the requirements of Chapter 1371 as the proceedings authorizing Bond Enhancement Agreements entered into by the Board pursuant to this Resolution.

SECTION 3. The costs of any Bond Enhancement Agreement and the amounts payable thereunder shall be payable out of Pledged Revenues and each Bond Enhancement Agreement shall constitute Parity Debt under the Master Resolution, except to the extent that a Bond Enhancement Agreement provides that an obligation of the Board thereunder shall be payable from and secured by a lien on Pledged Revenues subordinate to the lien securing the payment of the Parity Debt. The maximum term of each Bond Enhancement Agreement authorized by this Resolution shall not exceed the maturity date of the then outstanding related Parity Debt or the related Parity Debt anticipated to be issued in the future, as applicable. The notional amount of any Bond Enhancement Agreement authorized by this Resolution shall not at any time exceed the aggregate principal amount of the then outstanding related Parity Debt and related Parity Debt anticipated to be issued in the future, as applicable. No Confirmation entered into pursuant to this Resolution shall contain early termination provisions at the option of the counterparty except upon the occurrence of an event of default or an additional termination event, as prescribed in the applicable Master Agreement. No Bond Enhancement Agreement authorized by this Resolution shall be payable at a rate greater than the maximum rate allowed by law. An Authorized Representative may obtain credit enhancement for any Bond Enhancement Agreement if such Authorized Representative, as evidenced by a certificate delivered to the General Counsel to the Board, has determined that after taking into account the cost of such credit enhancement, such credit enhancement will reduce the amount payable by the Board pursuant to such Bond Enhancement Agreement; provided that the annual cost of credit enhancement on any Bond Enhancement Agreement entered into pursuant to this Resolution may not exceed 0.25% of the notional amount of such Bond Enhancement Agreement. No Bond Enhancement Agreement may be executed and delivered under this Resolution after August 31, 2008.

SECTION 4. Each Authorized Representative is hereby authorized to enter into ISDA Master Agreements (the "New Master Agreements") with counterparties satisfying the ratings requirements of the System's Interest Rate Swap Policy. Such New Master Agreements shall be in substantially the same form as the Executed Master Agreements, with such changes as, in the judgment of an Authorized Representative, with the advice and counsel of the Office of General Counsel and Bond Counsel, are necessary or desirable (i) to carry out the intent of the Board as expressed in this Resolution, (ii) to receive approval of this Resolution by the Attorney General of the State of Texas, if pursuant Section 2 of this Resolution, an Authorized Representative elects to designate any Bond Enhancement Agreement entered into by the Board pursuant to this Resolution as a "credit agreement" under Chapter 1371, (iii) to accommodate the credit structure or requirements of a particular counterparty or (iv) to incorporate comments received or anticipated to be received from any credit rating agency relating to a New Master Agreement. Each Authorized Representative is authorized to enter into such New Master Agreements and to enter into Confirmations thereunder in accordance with this Resolution and in furtherance of and to carry out the intent hereof.

SECTION 5. Each Authorized Representative is hereby further severally authorized to enter into amendments to the Master Agreements to allow Confirmations thereunder to be issued and entered into with respect to any then outstanding Parity Debt or Parity Debt anticipated to be issued in the future and to make such other amendments as in the judgment of such Authorized Representative, with the advice and counsel of the Office of General Counsel and Bond Counsel, are necessary or desirable to allow the Board to achieve the benefits of the Bond Enhancement Agreements in accordance with and subject to the System's Interest Rate Swap Policy and this Resolution.

SECTION 6. In addition to the authority otherwise granted in this Resolution, each Authorized Representative is hereby severally granted continuing authority to enter into the following specific transactions pursuant to a Confirmation upon satisfaction of the following respective conditions:

(A) Floating-to-fixed rate interest rate swap transactions under which the Board would pay an amount based upon a fixed rate of interest and the counterparty would pay an amount based upon a variable rate of interest with respect to Parity Debt then outstanding bearing interest at a variable rate and Parity Debt anticipated to be issued in the future that will bear interest at a variable rate, as applicable. Prior to entering into such transaction, an Authorized Representative must deliver to the General Counsel to the Board a certificate to the effect that (i) the synthetic fixed rate to the Board pursuant to the swap transaction is lower than the rate available to the Board for comparable fixed rate debt at the time of the swap transaction, and (ii) if the variable rate being paid or expected to be paid by the Board on the applicable Parity Debt is computed on a basis different from the calculation of the variable rate to be received under the swap transaction over the stated term of such swap transaction, the basis risk of the transaction is expected to be minimal based upon historical relationships between such bases.

(B) Fixed-to-floating rate interest rate swap transactions under which the Board would pay an amount based on a variable rate of interest and the counterparty would pay an amount based on a fixed rate of interest, with respect to Parity Debt then outstanding bearing interest at a fixed rate and Parity Debt anticipated to be issued in the future that will bear interest at a fixed rate, as applicable. Prior to entering into such transaction the Authorized Representative must deliver to the General Counsel to the Board a certificate to the effect that converting such portion of fixed rate Parity Debt to a variable rate pursuant to the fixed-to-floating interest rate swap transaction would be beneficial to the System by (i) lowering the anticipated net interest cost on the Parity Debt to be swapped against or (ii) assisting in the System's asset/liability management by matching a portion of its variable rate assets with variable rate Parity Debt.

(C) Basis swap transactions under which the Board would pay a variable rate of interest computed on one basis, such as the Securities Industry and Financial Markets Association Municipal Swap Index, and the counterparty would pay a variable rate of interest computed on a different basis, such as the London Interbank Offered Rate ("LIBOR"), with respect to a designated maturity or principal amount of outstanding Parity Debt and Parity Debt anticipated to be issued in the future, as applicable. Prior to entering into such transaction, an Authorized Representative must deliver to the General Counsel to the Board a certificate to the effect that by entering into the basis swap transaction the Board is expected to be able to (i) achieve spread income or upfront cash payments, (ii) preserve call option and advance refunding capability on its Parity Debt, (iii) lower net interest cost by effecting a percent of LIBOR synthetic refunding without issuing additional bonds or acquiring credit enhancement, (iv) lower net interest cost on Parity Debt by layering tax risk on top of a traditional fixed rate financing, (v) preserve liquidity capacity, or (vi) avoid the mark to market volatility of a fixed-to-floating or floating-to-fixed swap in changing interest rate environments.

(D) Interest rate locks, caps, floors, and collars for the purpose of limiting the exposure of the Board to adverse changes in interest rates in connection with outstanding Parity Debt or additional Parity Debt anticipated to be issued in the future. Prior to entering into such a transaction, an Authorized Representative must deliver to the General Counsel to the Board a certificate to the effect that such transaction is expected to limit or eliminate such exposure.

SECTION 7. To the extent that the Board receives payments pursuant to a Bond Enhancement Agreement authorized by this Resolution, such payments shall be applied to pay: (i) debt service on Parity Debt; (ii) the costs to be financed by the Parity Debt or anticipated issuance of Parity Debt related to the Bond Enhancement Agreement; provided that, if applicable, such costs shall have been approved for construction by the Board and that the applicable projects have received the required approval or review of the Texas Higher Education Coordinating Board to the extent and as required by the provisions of Section 61.058 of the *Texas Education Code*; or (iii) to the extent that costs set forth in (i) and (ii) have been satisfied, any lawful expenses of the System.

SECTION 8. To the extent that a Bond Enhancement Agreement is entered into under this Resolution with respect to the Board's obligations under an anticipated future issuance of Parity Debt, an Authorized Representative must also deliver to the General Counsel to the Board a certificate with respect to such anticipated Parity Debt stating: (i) the anticipated issuance date of such Parity Debt or a range of anticipated dates of up to six months for such issuance, provided that such date or range of dates may not be more than seventy-two (72) months after the date of the applicable Confirmation; (ii) whether such Parity Debt will bear interest at a fixed or variable rate; (iii) if such Parity Debt will bear interest at a fixed rate, what fixed interest rate or range of interest rates with respect to such Parity Debt is anticipated; (iv) if such Parity Debt will bear interest at a variable rate, what basis is anticipated to be used to compute such variable rate; (v) the assumed maturity schedule and amortization for such Parity Debt, including the assumed interest cost; (vi) the anticipated purposes for which the proceeds of such Parity Debt will be used; and (vii) for Parity Debt anticipated to be issued for new money projects, a list or description of such projects anticipated to be financed.

SECTION 9. Each Authorized Representative and all officers or officials of the Board are severally authorized to execute and deliver such other agreements and documents as are contemplated by this Resolution and the Master Agreements or are otherwise necessary in connection with entering into Confirmations and Bond Enhancement Agreements as described in this Resolution, as any such officer or official shall deem appropriate, including without limitation, officer's certificates, legal opinions, and credit support documents.

SECTION 10. All officers or officials of the Board and its agents and counsel are authorized to take all such further actions, to execute and deliver such further instruments and documents in the name and on behalf of the Board to pay all such expenses as in his or her judgment shall be necessary or advisable in order fully to carry out the purposes of this Resolution.

A RESOLUTION AUTHORIZING THE EXECUTION AND DELIVERY OF BOND ENHANCEMENT AGREEMENTS RELATING TO PERMANENT UNIVERSITY FUND DEBT AND AUTHORIZING AND APPROVING OTHER INSTRUMENTS AND PROCEDURES RELATING TO SAID AGREEMENTS

August 23, 2007

WHEREAS, the Board of Regents (the "Board") of The University of Texas System (the "System") is the governing body of the System, an institution of higher education under the *Texas Education Code* and an agency of the State of Texas (the "State"); and

WHEREAS, the Permanent University Fund is a constitutional fund and public endowment created in the Texas Constitution of 1876, as created, established, implemented and administered pursuant to Sections 10, 11, 11a, 11b, 15 and 18 of Article VII of the Constitution of the State, as amended, and by other applicable present and future constitutional and statutory provisions, and further implemented by the provisions of Chapter 66, *Texas Education Code*, as amended, (the "Permanent University Fund"); and

WHEREAS, the Available University Fund is defined by the Constitution of the State and consists of distributions made to it from the total return on all investment assets of the Permanent University Fund, including the net income attributable to the surface of Permanent University Fund land, as determined by the Board pursuant to Section 18 of Article VII of the Constitution of the State (the "Available University Fund"); and

WHEREAS, Section 18 of Article VII of the Constitution of the State, as may hereafter be amended (the "Constitutional Provision"), authorizes the Board to issue bonds and notes ("PUF Debt") not to exceed a total amount of 20% of the cost value of investments and other assets of the Permanent University Fund, exclusive of real estate, at the time of issuance thereof and to pledge all or any part of its two-thirds interest in the Available University Fund (the "Interest of the System") to secure the payment of the principal of and interest on PUF Debt, for the purpose of acquiring land, constructing and equipping buildings or other permanent improvements, major repair and rehabilitation of buildings and other permanent improvements, acquiring capital equipment and library books and library materials, and refunding bonds or notes issued under the Constitutional Provision or prior law, at or for the System Administration and institutions of the System as listed in the Constitutional Provision; and

WHEREAS, the Constitutional Provision also provides that out of the Interest of the System in the Available University Fund there shall be appropriated an annual sum sufficient to pay the principal and interest due on PUF Debt, and the remainder of the Interest of the System in the Available University Fund (the "Residual AUF") shall be appropriated for the support and maintenance of The University of Texas at Austin and the System Administration; and

WHEREAS, the Board has been presented with the form of an International Swaps and Derivatives Association, Inc. Master Agreement (including the Schedule and Credit Support Annex thereto) attached hereto as Exhibit A; and

WHEREAS, the Board hereby desires to severally authorize each Authorized Representative (as defined in the U.T. System Interest Rate Swap Policy) to enter into Bond Enhancement Agreements (as defined herein) from time to time, all as provided in this Resolution.

NOW THEREFORE BE IT RESOLVED, that

SECTION 1. Each Authorized Representative is hereby severally authorized to enter into International Swaps and Derivatives Association, Inc. Master Agreements (the "Master Agreements") with counterparties satisfying the ratings requirements of the U.T. System Interest Rate Swap Policy, and such Master Agreements shall be in substantially the same form as set forth in Exhibit A hereto, with such changes as, in the judgment of an Authorized Representative, with the advice and counsel of the U.T. Office of General Counsel and Bond Counsel, are necessary or desirable (i) to carry out the intent of the Board as expressed in this Resolution, (ii) to receive approval of this Resolution by the Attorney General of the State of Texas, if pursuant to Section 2 of this Resolution, an Authorized Representative elects to designate any Bond Enhancement Agreement entered into by the Board pursuant to this Resolution as a "credit agreement" under Chapter 1371 of the *Texas Government Code*, as amended ("Chapter 1371"), (iii) to accommodate the credit structure or requirements of a particular counterparty, or (iv) to incorporate comments received or anticipated to be received from any credit rating agency relating to a Master Agreement.

Each Authorized Representative is further severally authorized to act on behalf of the Board in accepting and executing confirmations under one or more of the Master Agreements (each, a "Confirmation," and collectively with the applicable Master Agreement, a "Bond Enhancement Agreement") when, in his or her judgment, the execution of such Confirmation is consistent with this Resolution, the U.T. System Interest Rate Swap Policy and either (i) the transaction is expected to reduce the net interest to be paid by the Board with respect to any then outstanding PUF Debt or PUF Debt anticipated to be issued in the future over the term of the Bond Enhancement Agreement or (ii) the transaction is in the best interests of the Board given the market conditions at that time.

SECTION 2. The Board hereby determines that any such Bond Enhancement Agreement entered into by an Authorized Representative pursuant to this Resolution is necessary or appropriate to place the Board's obligations with respect to its outstanding PUF Debt or PUF Debt anticipated to be issued in the future on the interest rate, currency, cash flow or other basis set forth in such Bond Enhancement Agreement as approved and executed on behalf of the Board by an Authorized Representative. Each Bond Enhancement Agreement constitutes a "bond enhancement agreement" under Section 65.461 of the *Texas Education Code* ("Section 65.461"). Pursuant to Section 65.461, a Bond Enhancement Agreement authorized and executed by an Authorized Representative under this Resolution shall not be considered a "credit agreement" under Chapter 1371, unless specifically designated as such by such Authorized Representative. In the event an Authorized Representative elects to treat a Bond Enhancement Agreement authorized by this Resolution as a "credit agreement" under Chapter 1371 and such Authorized Representative has not previously submitted this Resolution to the Attorney General, such Authorized Representative may submit this Resolution to the Attorney General for review and approval in accordance with the requirements of Chapter 1371 as the proceedings authorizing Bond Enhancement Agreements entered into by the Board pursuant to this Resolution.

SECTION 3. The costs of any Bond Enhancement Agreement and the amounts payable thereunder shall be payable from proceeds of the sale of PUF Debt to which the Bond Enhancement Agreement relates, the portion of the Residual AUF appropriated by the Board for the support and maintenance of System administration or from any other source that is legally available to make such payments. The maximum term of each Bond Enhancement Agreement authorized by this Resolution shall not exceed the maturity date of the then outstanding related PUF Debt or the related PUF Debt anticipated to be issued in the future, as applicable. The notional amount of any Bond Enhancement Agreement authorized by this Resolution shall not at any time exceed the aggregate principal amount of the then outstanding related PUF Debt or related PUF Debt anticipated to be issued in the future, as applicable. No Confirmation entered into pursuant to this Resolution shall contain early termination provisions at the option of the counterparty except upon the occurrence of an event of default or an additional termination event, as prescribed in the applicable Master Agreement. No Bond Enhancement Agreement authorized by this Resolution shall be payable at a rate greater than the maximum rate allowed by law. An Authorized Representative may obtain credit enhancement for any Bond Enhancement Agreement if such Authorized Representative, as evidenced by a certificate delivered to the General Counsel to the Board, has determined that after taking into account the cost of such credit enhancement, such credit enhancement will reduce the amount payable by the Board pursuant to such Bond Enhancement Agreement; provided that the annual cost of credit enhancement on any Bond Enhancement Agreement entered into pursuant to this Resolution may not exceed 0.25% of the notional amount of such Bond Enhancement Agreement. No Bond Enhancement Agreement may be executed and delivered under this Resolution after August 31, 2008.

SECTION 4. Each Authorized Representative is hereby further severally authorized to enter into amendments to the Master Agreements to allow Confirmations thereunder to be issued and entered into with respect to any then outstanding PUF Debt or PUF Debt anticipated to be issued in the future and to make such other amendments as in the judgment of such Authorized Representative, with the advice and counsel of the U.T. Office of General Counsel and Bond Counsel, are necessary or desirable to allow the Board to achieve the benefits of the Bond Enhancement Agreements in accordance with and subject to the U.T. System Interest Rate Swap Policy and this Resolution.

SECTION 5. In addition to the authority otherwise granted in this Resolution, each Authorized Representative is hereby severally granted continuing authority to enter into the following specific transactions pursuant to a Confirmation upon satisfaction of the following respective conditions:

(A) Floating-to-fixed rate interest rate swap transactions under which the Board would pay an amount based upon a fixed rate of interest and the counterparty would pay an amount based upon a variable rate of interest with respect to PUF Debt then outstanding bearing interest at a variable rate and any PUF Debt anticipated to be issued in the future that will bear interest at a variable rate. Prior to entering into such transaction, an Authorized Representative must deliver to the General Counsel to the Board a certificate to the effect that (i) the synthetic fixed rate to the Board pursuant to the swap transaction is lower than the rate available to the Board for comparable fixed rate debt at the time of the swap transaction, and (ii) if the variable rate being paid or expected to be paid by the Board on the applicable PUF Debt is computed on a basis different from the calculation of the variable rate to be received under the swap transaction over the stated term of such swap transaction, the basis risk of the transaction is expected to be minimal based upon historical relationships between such bases.

(B) Fixed-to-floating rate interest rate swap transactions under which the Board would pay an amount based upon a variable rate of interest and the counterparty would pay an amount based upon a fixed rate of interest, with respect to PUF Debt then outstanding bearing interest at a fixed rate or PUF Debt anticipated to be issued in the future that will bear interest at a fixed rate. Prior to entering into such transaction, an Authorized Representative must deliver to the General Counsel to the Board a certificate to the effect that converting such portion of fixed rate PUF Debt to a variable rate pursuant to the fixed-to-floating interest rate swap transaction would be beneficial to the System by (i) lowering the anticipated net interest cost on the PUF Debt to be swapped against or (ii) assisting in the System’s asset/liability management by matching a portion of its variable rate assets with variable rate PUF Debt.

(C) Basis swap transactions under which the Board would pay a variable rate of interest computed on one basis, such as the Securities Industry and Financial Markets Association Municipal Swap Index, and the counterparty would pay a variable rate of interest computed on a different basis, such as a designated maturity of the London Interbank Offered Rate ("LIBOR"), with respect to a given principal amount of PUF Debt then outstanding or PUF Debt anticipated to be issued in the future. Prior to entering into such transaction, an Authorized Representative must deliver to the General Counsel to the Board a certificate to the effect that by entering into the basis swap transaction the Board is expected to be able to (i) achieve spread income or upfront cash payments, (ii) preserve call option and advance refunding capability on its PUF Debt, (iii) lower net interest cost by effecting a percent of LIBOR synthetic refunding without issuing additional bonds or acquiring credit enhancement, (iv) lower net interest cost on PUF Debt by layering tax risk on top of a traditional fixed rate financing, (v) preserve liquidity capacity, or (vi) avoid the mark to market volatility of a fixed-to-floating or floating-to-fixed swap in changing interest rate environments.

(D) Interest rate locks, caps, floors, and collars for the purpose of limiting the exposure of the Board to adverse changes in interest rates in connection with outstanding PUF Debt or additional PUF Debt anticipated to be issued in the future. Prior to entering into such transaction, an Authorized Representative must deliver to the General Counsel to the Board a certificate to the effect that such transaction is expected to limit or eliminate such exposure. Any such transaction may be evidenced by the execution of a Confirmation or other agreement or instrument deemed necessary by an Authorized Representative.

SECTION 6. To the extent that the Board receives payments pursuant to a Bond Enhancement Agreement authorized by this Resolution, such payments shall be applied to pay: (i) the costs to be financed by the PUF Debt or anticipated issuance of PUF Debt related to the Bond Enhancement Agreement; provided that, if applicable, such costs shall have been approved for construction by the Board and that the applicable projects have received the required approval or review of the Texas Higher Education Coordinating Board to the extent and as required by the provisions of Section 61.058 of the *Texas Education Code*; or (ii) to the extent that costs set forth in (i) have been satisfied, any lawful expenses of the System.

SECTION 7. To the extent that a Bond Enhancement Agreement is entered into under this Resolution with respect to the Board's obligations under an anticipated future issuance of PUF Debt, an Authorized Representative must also deliver to the General Counsel to the Board a certificate with respect to such anticipated PUF Debt stating: (i) the anticipated issuance date of such PUF Debt or a range of anticipated dates of up to six months for such issuance, provided that such date or range of dates may not be more than seventy-two (72) months after the date of the applicable Confirmation or other applicable agreement; (ii) whether such PUF Debt will bear interest at a fixed or variable rate; (iii) if such PUF Debt will bear interest at a fixed rate, what fixed interest rate or range of interest rates with respect to such PUF Debt is anticipated; (iv) if such PUF Debt will bear interest at a variable rate, what basis is anticipated to be used to compute such variable rate; (v) the assumed maturity schedule and amortization for such PUF Debt, including the assumed interest cost; (vi) the anticipated purposes for which the proceeds of such PUF Debt will be used; and (vii) for PUF Debt anticipated to be issued for new money projects, a list or description of such projects anticipated to be financed.

SECTION 8. Each Authorized Representative and all officers or officials of the Board are severally authorized to execute and deliver such other agreements and documents as are contemplated by this Resolution and the Master Agreements or are otherwise necessary in connection with entering into Confirmations and Bond Enhancement Agreements as described in this Resolution, as any such officer or official shall deem appropriate, including without limitation, officer's certificates, legal opinions, and credit support documents.

SECTION 9. All officers or officials of the Board and its agents and counsel are authorized to take all such further actions, to execute and deliver such further instruments and documents in the name and on behalf of the Board to pay all such expenses as in his or her judgment shall be necessary or advisable in order fully to carry out the purposes of this Resolution.

EXHIBIT A

FORM OF MASTER AGREEMENT

Note: The form of the PUF ISDA agreement not been included as part of the agenda materials, but is available upon request.

9. U. T. System: Approval of aggregate amount of $102,957,000 of equipment financing for Fiscal Year 2008 and resolution regarding parity debt

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Business Affairs that the U. T. System Board of Regents

a. approve an aggregate amount of $102,957,000 of Revenue Financing System Equipment Financing as allocated to those U. T. System institutions set out on Page 103; and

b. 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 cost of equipment including costs incurred 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;

- the institutions and U. T. System Administration, which are "Members" as such term is used in the Master Resolution, possess the financial capacity to satisfy their direct obligation 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 aggregate amount of $102,957,000 for the purchase of equipment; and

- this resolution satisfies the official intent requirements set forth in Section 1.150-2 of the *Code of Federal Regulations* that evidences the Board's intention to reimburse project expenditures with bond proceeds.

BACKGROUND INFORMATION

On April 14, 1994, the U. T. System Board of Regents approved the use of Revenue Financing System debt for equipment purchases in accordance with the Guidelines Governing Administration of the Revenue Financing System. The guidelines specify that the equipment to be financed must have a useful life of at least three years. The debt is amortized twice a year with full amortization not to exceed 10 years.

This Agenda Item requests approval of an aggregate amount of $102,957,000 for equipment financing for Fiscal Year 2008.

The U. T. System Board of Regents approved $108,000,000 of equipment financing in Fiscal Year 2007, of which $52,314,000 has been issued through June 1, 2007.

Further details on the equipment to be financed and debt coverage ratios for individual institutions can be found on Page 103.

APPROVAL OF U. T. SYSTEM EQUIPMENT FINANCING
FY 2008

Institution	$ Amount of Request	Description of Expected Equipment Purchases	DSC*
U. T. Austin	$1,500,000	Classroom equipment, research equipment, and information technology hardware	4.4x
U. T. Dallas	4,000,000	General purpose equipment and equipment, software, and services for the Pilot Shared Services project	3.5x
U. T. El Paso	1,632,000	Technology infrastructure, facilities maintenance equipment, vehicle replacement, parking control software and equipment, elevator purchase and installation, and conference services management system	2.3x
U. T. San Antonio	2,425,000	Scientific equipment, lab equipment, and vehicle purchases	3.1x
U. T. Southwestern Medical Center - Dallas	45,000,000	Information resources equipment, clinical and hospital equipment, and non-clinical equipment	2.3x
U. T. Medical Branch - Galveston	14,000,000	Clinical and information technology equipment	1.9x
U. T. Health Science Center - San Antonio	4,000,000	Cyclotron, research, clinical & information technology equipment	1.4x
U. T. M. D. Anderson Cancer Center	25,000,000	Medical equipment, research equipment, and diagnostic equipment	4.5x
U.T. Health Center - Tyler	5,000,000	New telephone system, clinical equipment, and diagnostic equipment	3.2x
U. T. System Administration	400,000	Information technology equipment	N/A

Total	$102,957,000

* Debt Service Coverage ("DSC") based on actual results for FY06.

U. T. System Office of Finance, July 23, 2007

10. U. T. System Board of Regents: Adoption of Eighteenth Supplemental Resolution authorizing Revenue Financing System Bonds in an amount not to exceed $675,000,000; adoption of a standard provisions resolution; authorization to complete all related transactions; and resolution regarding parity debt

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Business Affairs that the U. T. System Board of Regents

a. adopt the Eighteenth Supplemental Resolution to the Master Resolution, containing terms in substantially the form approved by the Board of Regents on November 13, 2003, authorizing the issuance, sale, and delivery of Board of Regents of The University of Texas System Revenue Financing System Bonds in one or more installments in an aggregate principal amount not to exceed $675,000,000 for the purpose of refunding a portion of the outstanding Revenue Financing System Commercial Paper Notes, Series A; to provide new money to fund construction and acquisition costs of projects in the Capital Improvement Program; to current or advance refund certain outstanding Revenue Financing System Bonds to produce present value debt service savings; and to pay the costs of issuance and any original issue discount;

b. adopt a standard provisions resolution approving certain standard provisions and procedures applicable to bonds issued pursuant to the supplemental resolutions to the Master Resolution authorizing the issuance, sale, and delivery of Board of Regents of The University of Texas System Revenue Financing System Bonds; and

c. authorize appropriate officers and employees of the U. T. System as set forth in the Eighteenth Supplemental Resolution to take any and all actions necessary to carry out the intentions of the U. T. System Board of Regents, within the limitations and procedures specified therein, to make certain covenants and agreements in connection therewith; and to resolve other matters incident and related to the issuance, sale, security, and delivery of such Bonds.

The Chancellor also concurs with the recommendation of the Executive Vice Chancellor for Business Affairs that, in compliance with Section 5 of the Amended and Restated Master Resolution Establishing The University of Texas System Revenue Financing System adopted by the U. T. System Board of Regents on February 14, 1991, amended on October 8, 1993, and August 14, 1997, and upon delivery of the Certificate of an Authorized Representative as required by Section 5 of the Master Resolution, the U. T. System Board of Regents resolves that

a. 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 Board relating to the Financing System; and

b. the institutions, which are "Members" as such term is used in the Master Resolution, possess the financial capacity to satisfy their direct obligation as defined in the Master Resolution relating to the issuance by the U. T. System Board of Regents of tax-exempt parity debt.

BACKGROUND INFORMATION

On February 14, 1991, the U. T. System Board of Regents adopted a Master Resolution establishing the Revenue Financing System (RFS) to create a cost-effective, System-wide financing structure for institutions of the U. T. System. Since that time, the Board has adopted 17 supplemental resolutions to provide debt financing for projects that have received the requisite U. T. System Board of Regents and Texas Higher Education Coordinating Board approvals.

Adoption of the Eighteenth Supplemental Resolution (Resolution) would authorize the refunding of certain outstanding RFS Bonds provided that an advance refunding exceed a minimum 3% present value debt service savings threshold. An advance refunding involves issuing bonds to refund outstanding bonds in advance of the call date. Refunding bonds are issued at lower interest rates thereby producing debt service savings. Adoption of this Resolution will provide the flexibility to select the particular bonds to be refunded depending on market conditions at the time of pricing. The particular bonds to be refunded will be called for redemption on the first practical optional redemption date for each series of refunded bonds occurring after the delivery of the refunding bonds.

The Resolution authorizes refunding a portion of the outstanding Revenue Financing System Commercial Paper Notes, Series A, refunding certain outstanding RFS Bonds for savings, and new money to fund construction and acquisition costs of projects in the Capital Improvement Program. Generally, commercial paper debt is issued to fund projects during the construction phase and the debt is not amortized. Once construction is complete, the commercial paper is refunded with bonds. Depending on the level of interest rates at the time of pricing, outstanding commercial paper and new money for construction may be financed with long-term debt.

In addition, the Resolution authorizes remarketing, tender, auction and broker-dealer agreements customarily utilized in connection with the types of variable rate instruments authorized.

The purpose of the proposed standard provisions resolution is to gather provisions that do not change into a single resolution that can be incorporated by reference rather than repeating the standard provisions in each subsequent supplemental resolution.

The proposed Eighteenth Supplemental Resolution and standard provisions resolution have been reviewed by outside bond counsel and the U. T. System Office of General Counsel.

> Note: The Eighteenth Supplemental Resolution, standard provisions resolution, and forms of auction agreement and broker-dealer agreement contain terms that are substantially the same as those contained in the Thirteenth through Seventeenth Supplemental Resolutions and forms of auction agreement and broker-dealer agreement previously approved by the Board on November 13, 2003, for use as standard agreements. These documents have not been included as part of the Agenda materials, but are available upon request.

11. U. T. System Board of Regents: Report on Treasury Working Group

Executive Vice Chancellor Kelley will discuss the progress to date of the U. T. System Treasury Working Group, headed by Mr. Philip R. Aldridge, Associate Vice Chancellor for Finance.

REPORT

On July 8, 2005, the Board of Regents asked the Office of Finance to explore the multiple banking relationships throughout the U. T. System and determine if there are ways to increase efficiency and lower costs for these services. Treasury Strategies, Inc. (TSI) was hired to perform a "Best Practices Review" of treasury services at the U. T. System institutions and at U. T. System Administration. TSI's report and recommendations were reviewed with the U. T. System Board of Regents on November 16, 2006. At that meeting, the Board authorized the Office of Finance to move forward and "standardize" certain treasury functions throughout the U. T. System.

In recent months, the Office of Finance has been leading an implementation team, consisting of cash managers from many of the U. T. System institutions, representatives from U. T. System Administration, and Ms. Linda Patterson of Patterson & Associates. Patterson & Associates is an Austin-based treasury advisory firm and was selected through a formal Request for Qualifications (RFQ) process based on its extensive experience in municipal treasury management. The implementation team is in the process of achieving the following objectives:

1. the creation of new treasury policies to upgrade and standardize treasury practices relating to collections and deposits, collateral standards, cash handling, cash flow forecasting, petty cash, and transport of assets;

2. the creation of a System-wide banking Request for Proposals (RFP) to leverage the negotiating power of the U. T. System to standardize and reduce banking fees, maximize interest income, and reduce the number of banks serving U. T. System institutions while increasing the minimum service level standards;

3. assurance that each U. T. System institution has a formal treasury operations disaster recovery plan;

4. assurance that treasury operations will be regularly audited and reviewed for compliance purposes;

5. a review of the U. T. System-wide merchant card services agreement, and;

6. an upgrade of the U. T. System collateral tracking system for banking deposits.

Substantial progress has been made by the working group on each of these items. The U. T. System-wide treasury policies have been drafted and will be effective September 1, 2007. Among other requirements, the new treasury policies will require that regular audits are performed for treasury activities. The U. T. System-wide banking RFP is in final form and ready to be distributed to the banking community. It is anticipated that the RFP responses will be received in early October, with the selection of new banking institutions effective on or before March 1, 2008. The banking RFP includes a solicitation of new pricing for merchant card services. Surveys have been conducted to confirm the existence of treasury disaster recovery plans at all the U. T. System institutions and System Administration, most of which were created as part of the U. T. System-wide business continuity planning process. A new collateral system has been created and rolled out by the Office of Finance for use by the U. T. System institutions to streamline the collateral process. In addition, the need for collateral will be minimized through implementation of the banking RFP, which requires "sweep" accounts where possible. A final report on the results of the Treasury Working Group will be presented to the U. T. System Board of Regents in Spring 2008.

Supplemental Materials: The Cash Management and Cash Handling Policy and the Banking Services Policy on Pages 84 - 104 of Volume 2.

12. **U. T. System Board of Regents: Approval of amendments to the Allocation Policy for Non-Endowment Funds**

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Business Affairs that the U. T. System Board of Regents approve amendments to The University of Texas System Allocation Policy for Non-Endowment Funds (Allocation Policy), as set forth in congressional style on Pages 109 - 110. The amendments to the Allocation Policy are to be effective September 1, 2007.

BACKGROUND INFORMATION

The Allocation Policy was approved by the U. T. System Board of Regents on November 10, 2005, and implemented on February 1, 2006, as part of the centralization of non-endowment funds. The Allocation Policy is intended to ensure that sufficient liquidity is available at all times to meet the needs of the U. T. System institutions and U. T. System Administration, while ensuring that all funds not needed for short-term liquidity purposes are invested with an appropriate time horizon to enhance the total return of the non-endowment funds. Eligible U. T. System institutions with at least $5 million of non-endowment funds on the last day of a calendar month and a current financial condition rating from the U. T. System Office of the Controller of "Watch" or better invest in the Intermediate Term Fund (ITF) pursuant to the Allocation Policy. Currently, 85% of an institution's non-endowment funds are to be invested in the Intermediate Term Fund with a corresponding target allocation for the AAA-rated money market Short Term Fund of 15% (within a range of 10-20%).

The primary proposed amendment to the Allocation Policy is to increase the target allocation in the Intermediate Term Fund from 85% to 90%, with the remaining 10% in the Short Term Fund (within a range of 5-15%). This recommendation is based on a review of actual daily data dating back to 2002. During the first 12 months of operation of the Intermediate Term Fund, the maximum daily outflow represented just 2.6% of the combined non-endowment funds (Intermediate Term Fund and Short Term Fund). The 10% target in the Short Term Fund (plus debt proceeds) should provide more than ample operating liquidity going forward. All other changes to the Allocation Policy are editorial in nature.

The University of Texas System Allocation Policy for Non-Endowment Funds

Purpose

The University of Texas System Allocation Policy for Non-Endowment Funds ("Allocation Policy") is intended to ensure that sufficient liquidity is available at all times to meet the needs of the institutions and System Administration, while ensuring that all funds not needed for short-term liquidity purposes are invested with an appropriate time horizon to enhance the total return of the Non-Endowment Funds. Eligible Institutions with at least $5 million of Non-Endowment Funds on the last day of a calendar month and a current financial condition rating from the System Administration Office of the Controller of "Watch" or better will invest in the Intermediate Term Fund ("ITF") pursuant to this policy. Exceptions for funds that would otherwise be invested pursuant to this policy may be made only with the approval of an Authorized Representative.

Allocation and Rebalancing

At the beginning of each month, each institution shall have a minimum of $5 million invested in the Short Term Fund ("STF"). The target allocation for Non-Endowment Funds ~~in excess of $5 million~~ held by Eligible Institutions shall be ~~15%~~10% in the STF and ~~85%~~90% in the ITF. Institutions that are ineligible to invest in the ITF shall be 100% invested in the STF. If an institution ceases being an Eligible Institution as measured on the last day of any month, then it must rebalance such that 100% of its Non-Endowment Funds are in the STF, unless approval is obtained from an Authorized Representative.

Eligible Institutions are required to rebalance when the projected allocation to the STF at month-end is less than ~~10%~~5% or greater than ~~20%~~15% of the institution's Non-Endowment Funds, or when a cash inflow or outflow is scheduled to occur during the next calendar month that is likely to result in the institution having less than ~~10%~~5% or more than ~~20%~~15% of its Non-Endowment Funds in the STF at the end of the next calendar month. Each Chief Business Officer is responsible for rebalancing to ensure the institution's Non-Endowment Funds are within this target range, which will be reviewed on a monthly basis by the System Administration Office of Finance. At least five days prior to the end of each month, each institution should check its balance in the STF and the ITF to determine if rebalancing will be necessary. If necessary, ITF transactions should be initiated on or before the last business day of the month. ITF transactions will be effective on the first business day of the following month. For ITF transactions greater than ~~$10~~$25 million ~~(redemptions or withdrawals)~~, the institution should provide notice to The University of Texas Investment Management Company (UTIMCO) at least ~~five~~ three business days in advance to facilitate UTIMCO's ability to transact efficiently.

Sharing of Investment Returns

If the total investment return on the ITF in a fiscal year is in excess of the ~~primary~~ national Consumer Price Index ("CPI-U") published by the Bureau of Labor Statistics plus 3.0%, then the amount in excess of the CPI-U plus 3.0% will be split, with 90% of the excess return being retained by the institutions and 10% being distributed to System Administration. Any funds distributed to System Administration will be used exclusively for strategic initiatives that benefit the institutions, and all expenditures of the funds by System Administration will require approval of the Board of Regents.

No excess returns will be distributed to System Administration unless the cumulative total investment return of the ITF, measured from the inception date of ~~this policy~~ <u>the ITF</u> through the most recent fiscal year end, is <u>also</u> in excess of the ~~monthly compounded~~ cumulative <u>total</u> return of the CPI-U plus 3.0% <u>(per year)</u> for the same period.

Definitions

Authorized Representative – The Executive Vice Chancellor for Business Affairs at System Administration or the Associate Vice Chancellor for Finance at System Administration.
Eligible Institutions – Institutions with at least $5 million of Non-Endowment Funds on the last day of a month and a current financial condition rating from the System Administration Office of the Controller of "Watch" or better.
Intermediate Term Fund (ITF) – The ITF is a pooled fund for the investment of Non-Endowment Funds that are not required to be invested in the Short Term Fund. Refer to the ITF Investment Policy for more information.
Non-Endowment Funds – Non-Endowment Funds include all non-endowment monies owned by the Board of Regents or under the control of the Board of Regents. Funds that are legally required to be invested elsewhere, such as funds held at the State Treasury and certain trust funds, are excluded from this policy. Due to Internal Revenue Service restrictions governing tax-exempt debt such as yield restriction and spend-out requirements, debt-related funds are also specifically excluded from this policy. Exceptions for Non-Endowment Funds that would otherwise be invested pursuant to this policy may be made only with the approval of an Authorized Representative.
Short Term Fund (STF) – The STF is an institutional money market mutual fund, currently the Dreyfus Institutional Preferred Money Market Fund (Dreyfus Fund). The STF provides daily liquidity and safety of principal by investing in short-term money market obligations. Refer to the STF Investment Policy for more information.

13. U. T. System Board of Regents: Investment Reports for the fiscal quarter ended May 31, 2007, and The University of Texas Investment Management Company (UTIMCO) Performance Summary Report

REPORT

The Investment Reports for the fiscal quarter ended May 31, 2007, are set forth on Pages 113 - 117.

Item I on Page 113 reports activity for the Permanent University Fund (PUF) investments. The PUF's net investment return for the quarter was 6.74% versus its composite benchmark return of 5.89%. The PUF's net asset value increased by $705.0 million since the beginning of the quarter to $11,763.6 million. This change in net asset value includes increases due to contributions from PUF land receipts and net investment return, and the third payment of the annual distribution to the Available University Fund (AUF) for $100.2 million.

Item II on Page 114 reports activity for the General Endowment Fund (GEF) investments. The GEF's net investment return for the quarter was 6.77% versus its composite benchmark return of 5.89%. The GEF's net asset value increased during the quarter to $6,435.5 million.

Item III on Page 115 reports activity for the Intermediate Term Fund (ITF). The ITF's net investment return for the quarter was 4.06% versus its composite benchmark return of 2.84%. The net asset value has increased to $3,740.0 million due to net contributions ($173.3 million), net distributions (-$27.1 million), and net investment return ($154.6 million).

Item IV on Page 116 presents book and market value of cash, debt, equity, and other securities held in funds outside of internal investment pools. Total cash and equivalents, consisting primarily of institutional operating funds held in the Dreyfus money market fund, increased by $.3 million to $1,621.0 million during the three months since the last reporting period. Market values for the remaining asset types were debt securities: $33.9 million versus $32.4 million at the beginning of the period; equities: $73.9 million versus $72.1 million at the beginning of the period; and other investments: $.1 million versus $1.6 million at the beginning of the period.

The May 31, 2007, UTIMCO Performance Summary Report is attached on Page 117. The Dow Jones Wilshire Real Estate Securities Index (the DJWRESI) is the approved benchmark for the REITS (Real Estate Investment Trust) asset class, included in the Endowment Investment Policy Portfolios and reported for comparison with REIT manager returns. Effective July 1, 2007, the DJWRESI has undergone a routine minor change in the construction of its underlying holdings. UTIMCO staff, in concurrence with U. T. System staff and Mr. Bruce Myers from Cambridge Associates, has determined that this change does not constitute a "change in a benchmark" requiring action by the

UTIMCO Board and U. T. System Board of Regents. No prior period index or benchmark returns will be restated; the same index, constructed under a slightly different methodology will continue to be used on a go-forward basis.

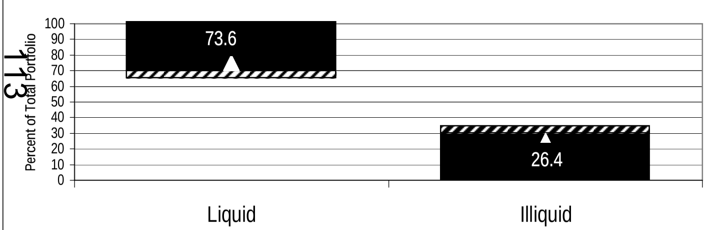
I. PERMANENT UNIVERSITY FUND
Investment Reports for Periods Ended May 31, 2007
Prepared in accordance with *Texas Education Code* Sec. 51.0032

Summary of Capital Flows

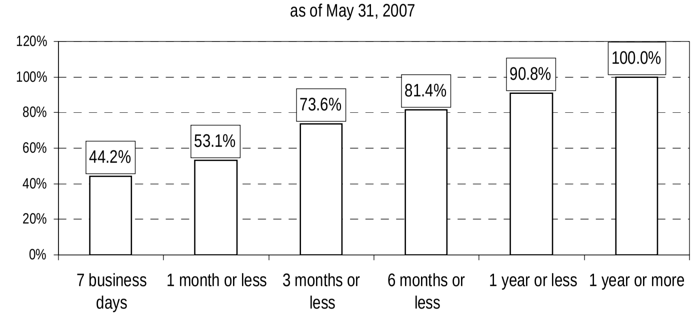
($ millions)	Fiscal Year Ended August 31, 2006	Quarter Ended May 31, 2007	Fiscal Year Ended August 31, 2007
Beginning Net Assets	$ 9,426.7	$ 11,058.6	$ 10,313.4
PUF Lands Receipts	214.9	71.2	207.2
Investment Return	1,111.7	759.9	1,603.2
Expenses	(82.6)	(25.9)	(59.7)
Distributions to AUF	(357.3)	(100.2)	(300.5)
Ending Net Assets	$ 10,313.4	$ 11,763.6	$ 11,763.6

	May 31, 2007		Fiscal Year to Date: Returns		Fiscal Year to Date: Value Added		
	Portfolio Exposure	Policy Target	Portfolio	Policy Benchmark	From Asset Allocation	From Security Selection	Total
Cash and Cash Equivalents	4.42%	0.00%	4.01%	3.90%	-0.35%	0.00%	-0.35%
U.S. Equities	23.08%	20.00%	19.45%	19.55%	0.11%	-0.02%	0.09%
Non-U.S. Developed Equity	11.49%	10.00%	18.14%	22.25%	0.05%	-0.39%	-0.34%
Emerging Markets Equity	8.14%	7.00%	31.76%	33.15%	0.33%	-0.09%	0.24%
Directional Hedge Funds	9.69%	10.00%	16.40%	8.60%	-0.01%	0.79%	0.78%
Absolute Return Hedge Funds	14.00%	15.00%	13.56%	8.60%	0.00%	0.76%	0.76%
REITS	4.62%	5.00%	18.47%	15.02%	-0.02%	0.16%	0.14%
Commodities	3.50%	3.00%	-11.51%	-6.76%	-0.43%	-0.17%	-0.60%
TIPS	3.49%	5.00%	0.83%	0.74%	0.15%	0.01%	0.16%
Fixed Income	7.00%	10.00%	3.16%	3.43%	0.28%	-0.03%	0.25%
Total Marketable Securities	**89.43%**	85.00%	**14.61%**	**13.33%**	**0.11%**	**1.02%**	**1.13%**
Private Capital	10.57%	15.00%	19.83%	16.46%	-0.31%	0.51%	0.20%
Total	**100.00%**	100.00%	**15.14%**	**13.81%**	**-0.20%**	**1.53%**	**1.33%**

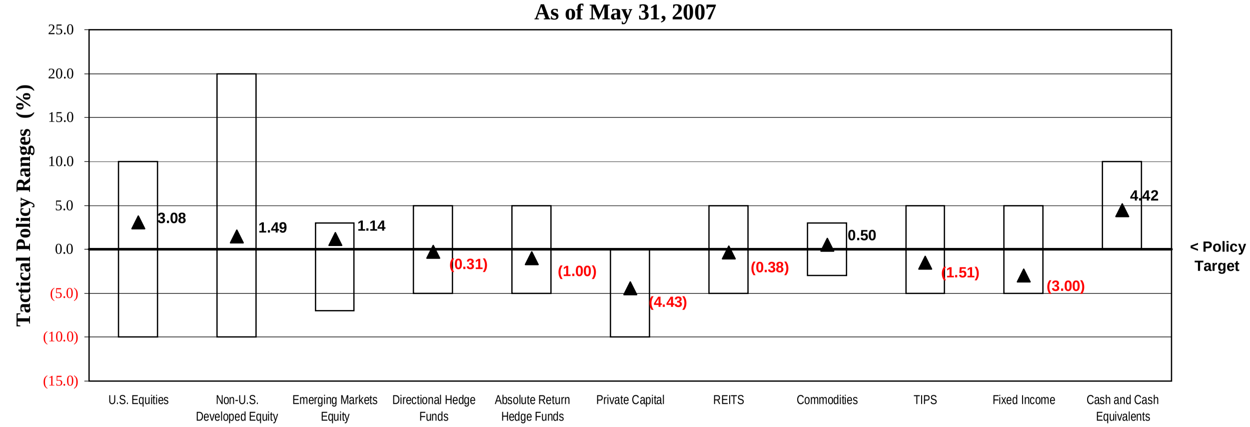
PUF Liquidity Policy Profile
As of May 31, 2007



PUF Detailed Liquidity Profile
as of May 31, 2007



Deviations From Policy Targets Within Tactical Policy Ranges
As of May 31, 2007



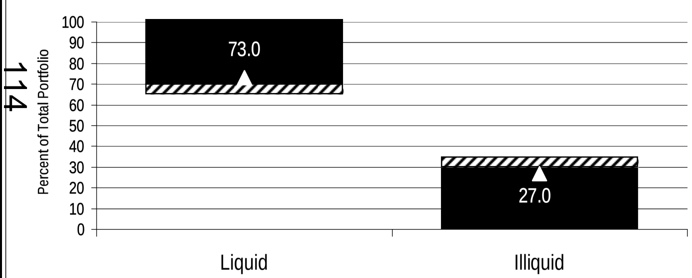
II. GENERAL ENDOWMENT FUND
Investment Reports for Periods Ended May 31, 2007
Prepared in accordance with *Texas Education Code* Sec. 51.0032

Summary of Capital Flows

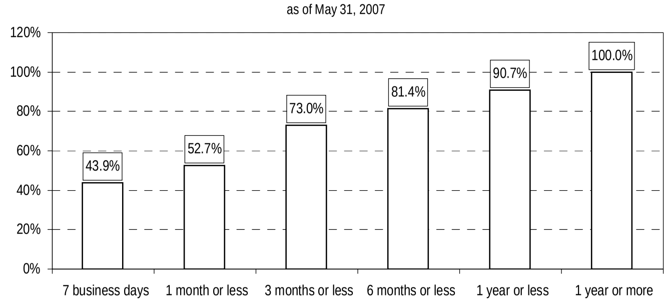
($ millions)	Fiscal Year Ended August 31, 2006	Quarter Ended May 31, 2007	Fiscal Year Ended August 31, 2007
Beginning Net Assets	$ 4,926.8	$ 5,996.8	$ 5,427.8
Contributions	273.9	89.6	316.4
Withdrawals	(108.0)	-	(1.9)
Distributions	(220.0)	(60.3)	(178.8)
Investment Return	593.3	421.2	898.9
Expenses	(38.2)	(11.8)	(26.9)
Ending Net Assets	$ 5,427.8	$ 6,435.5	$ 6,435.5

	May 31, 2007		Fiscal Year to Date: Returns		Fiscal Year to Date: Value Added		
	Portfolio Exposure	Policy Target	Portfolio	Policy Benchmark	From Asset Allocation	From Security Selection	Total
Cash and Cash Equivalents	3.01%	0.00%	4.01%	3.90%	-0.28%	0.00%	-0.28%
U.S. Equities	23.54%	20.00%	19.32%	19.55%	0.14%	-0.05%	0.09%
Non-U.S. Developed Equity	11.23%	10.00%	18.17%	22.25%	0.03%	-0.39%	-0.36%
Emerging Markets Equity	8.35%	7.00%	31.92%	33.15%	0.28%	-0.08%	0.20%
Directional Hedge Funds	9.84%	10.00%	16.41%	8.60%	0.00%	0.79%	0.79%
Absolute Return Hedge Funds	14.23%	15.00%	13.56%	8.60%	0.00%	0.77%	0.77%
REITS	4.62%	5.00%	18.53%	15.02%	-0.03%	0.17%	0.14%
Commodities	3.56%	3.00%	-11.55%	-6.76%	-0.40%	-0.17%	-0.57%
TIPS	3.40%	5.00%	0.86%	0.74%	0.18%	0.01%	0.19%
Fixed Income	7.01%	10.00%	3.18%	3.43%	0.28%	-0.03%	0.25%
Total Marketable Securities	**88.79%**	**85.00%**	**14.73%**	**13.33%**	**0.20%**	**1.02%**	**1.22%**
Private Capital	11.21%	15.00%	22.21%	16.46%	-0.37%	0.86%	0.49%
Total	**100.00%**	**100.00%**	**15.52%**	**13.81%**	**-0.17%**	**1.88%**	**1.71%**

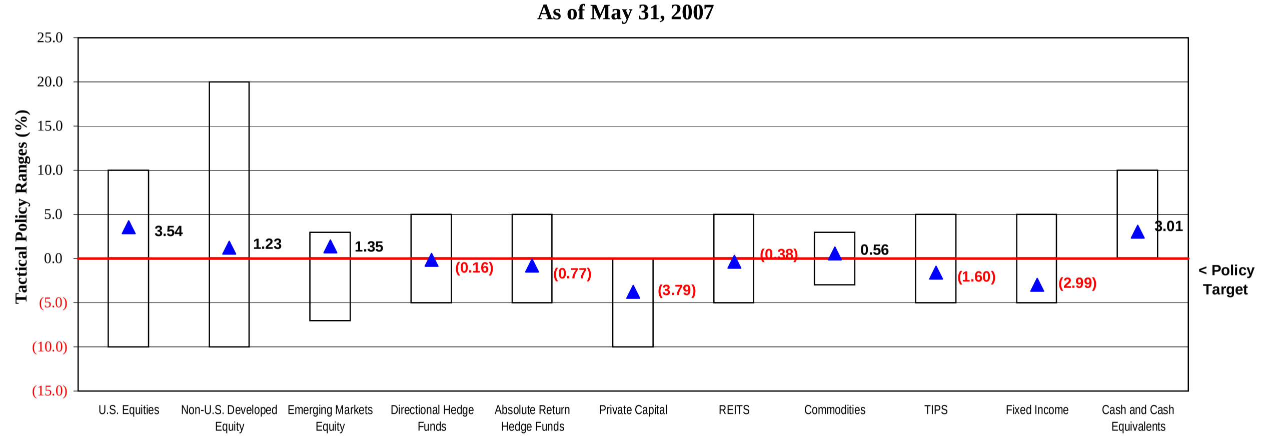
GEF Liquidity Policy Profile
As of May 31, 2007



GEF Detailed Liquidity Profile
as of May 31, 2007



Deviations From Policy Targets Within Tactical Policy Ranges
As of May 31, 2007

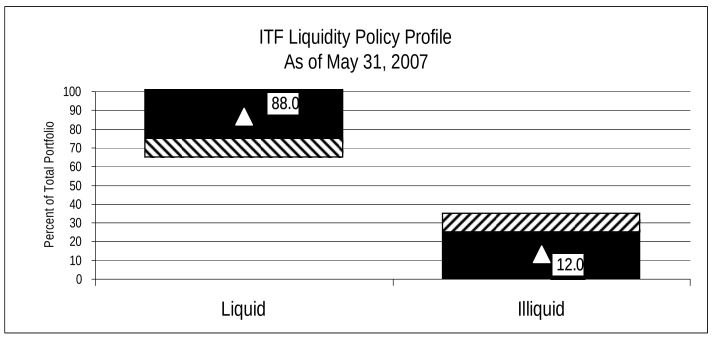


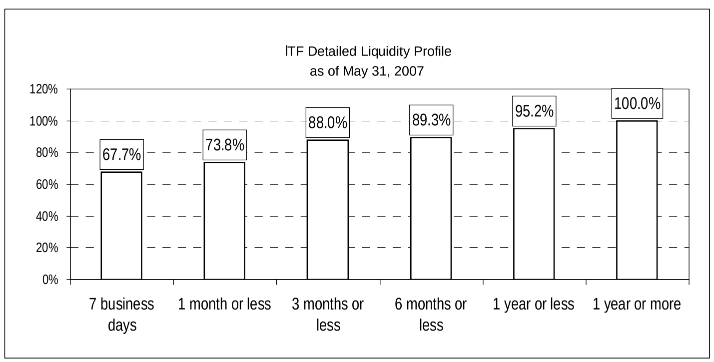
III. INTERMEDIATE TERM FUND
Investment Reports for Periods Ended May 31, 2007
Prepared in accordance with *Texas Education Code* Sec. 51.0032

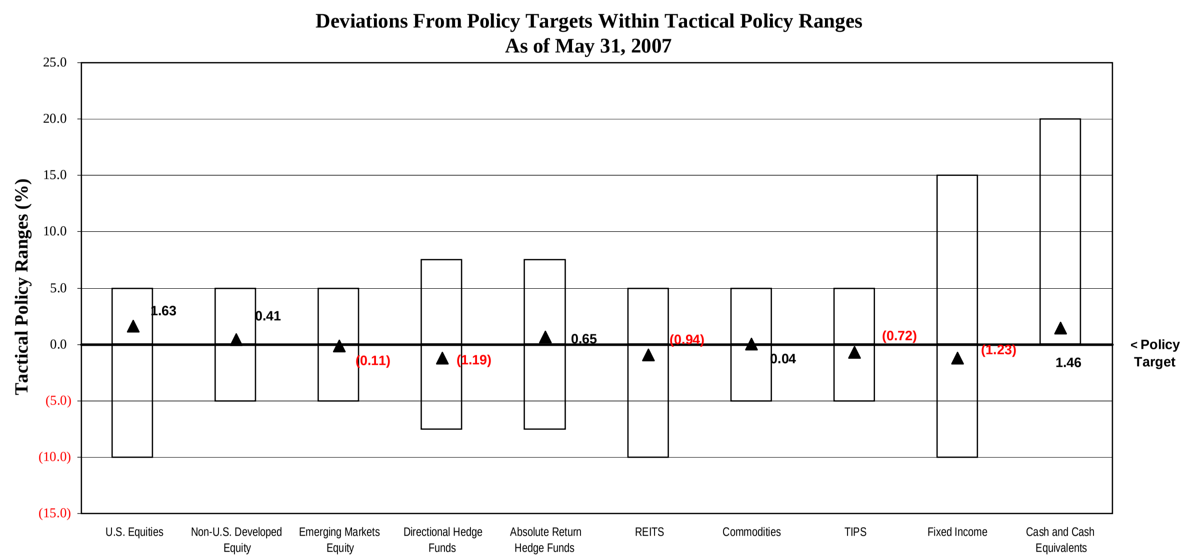
Summary of Capital Flows

($ millions)	Fiscal Year Ended August 31, 2006	Quarter Ended May 31, 2007	Fiscal Year Ended August 31, 2007
Beginning Net Assets	$ -	$ 3,519.2	$ 3,048.8
Contributions	3,112.3	173.3	603.2
Withdrawals	(111.2)	(69.2)	(189.5)
Distributions	(52.7)	(27.1)	(76.0)
Investment Return	115.4	154.6	381.8
Expenses	(15.0)	(10.8)	(28.3)
Ending Net Assets	$ 3,048.8	$ 3,740.0	$ 3,740.0

	May 31, 2007		Fiscal Year to Date: Returns		Fiscal Year to Date: Value Added		
	Portfolio Exposure	Policy Target	Portfolio	Policy Benchmark	From Asset Allocation	From Security Selection	Total
Cash and Cash Equivalents	1.46%	0.00%	4.01%	3.90%	-0.10%	0.00%	-0.10%
U.S. Equities	16.63%	15.00%	19.64%	19.55%	0.07%	0.01%	0.08%
Non-U.S. Developed Equity	5.41%	5.00%	19.75%	22.25%	0.02%	-0.11%	-0.09%
Emerging Markets Equity	4.89%	5.00%	31.32%	33.15%	-0.05%	-0.08%	-0.13%
Directional Hedge Funds	11.31%	12.50%	16.42%	8.60%	-0.10%	0.96%	0.86%
Absolute Return Hedge Funds	13.15%	12.50%	13.23%	8.60%	0.01%	0.58%	0.59%
REITS	9.06%	10.00%	17.68%	15.02%	0.03%	0.23%	0.26%
Commodities	5.04%	5.00%	-9.99%	-6.76%	-0.02%	-0.18%	-0.20%
TIPS	9.28%	10.00%	0.80%	0.74%	0.02%	0.01%	0.03%
Fixed Income	23.77%	25.00%	3.23%	3.43%	0.00%	-0.05%	-0.05%
Total	**100.00%**	100.00%	**11.02%**	**9.77%**	**-0.12%**	**1.37%**	**1.25%**







IV. SEPARATELY INVESTED ASSETS

Summary Investment Report at May 31, 2007

Report prepared in accordance with *Texas Education Code* Sec. 51.0032

($ thousands)

FUND TYPE

	CURRENT PURPOSE DESIGNATED		CURRENT PURPOSE RESTRICTED		ENDOWMENT & SIMILAR FUNDS		ANNUITY & LIFE INCOME FUNDS		AGENCY FUNDS		TOTAL EXCLUDING OPERATING FUNDS		OPERATING FUNDS (SHORT TERM FUND)		TOTAL	
ASSET TYPES																
Cash & Equivalents:	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET
Beginning value 02/28/07	1,727	1,727	2,320	2,320	79,933	79,933	7,311	7,311	2,877	2,877	94,168	94,168	1,266,676	1,266,676	1,360,844	1,360,844
Increase/(Decrease)	126	126	(482)	(482)	(51,297)	(51,297)	401	401	19,985	19,985	(31,267)	(31,267)	291,420	291,420	260,153	260,153
Ending value 05/31/07	1,853	1,853	1,838	1,838	28,636	28,636	7,712	7,712	22,862	22,862	62,901	62,901	1,558,096	1,558,096	1,620,997	1,620,997
Debt Securities:																
Beginning value 02/28/07	-	-	263	222	17,817	18,240	13,890	13,964	-	-	31,970	32,426	-	-	31,970	32,426
Increase/(Decrease)	-	-	-	-	560	421	1,386	1,082	-	-	1,946	1,503	-	-	1,946	1,503
Ending value 05/31/07	-	-	263	222	18,377	18,661	15,276	15,046	-	-	33,916	33,929	-	-	33,916	33,929
Equity Securities:																
Beginning value 02/28/07	29	8,143	509	587	32,855	38,568	19,512	24,797	-	-	52,905	72,095	-	-	52,905	72,095
Increase/(Decrease)	(5)	(514)	219	241	(258)	2,218	(1,487)	(164)	-	-	(1,531)	1,781	-	-	(1,531)	1,781
Ending value 05/31/07	24	7,629	728	828	32,597	40,786	18,025	24,633	-	-	51,374	73,876	-	-	51,374	73,876
Other:																
Beginning value 02/28/07	-	-	527	527	4	4	272	116	918	918	1,721	1,565	-	-	1,721	1,565
Increase/(Decrease)	-	-	(511)	(511)	-	-	11	-	(918)	(918)	(1,418)	(1,429)	-	-	(1,418)	(1,429)
Ending value 05/31/07	-	-	16	16	4	4	283	116	-	-	303	136	-	-	303	136
Total Assets:																
Beginning value 02/28/07	1,756	9,870	3,619	3,656	130,609	136,745	40,985	46,188	3,795	3,795	180,764	200,254	1,266,676	1,266,676	1,447,440	1,466,930
Increase/(Decrease)	121	(388)	(774)	(752)	(50,995)	(48,658)	311	1,319	19,067	19,067	(32,270)	(29,412)	291,420	291,420	259,150	262,008
Ending value 05/31/07	1,877	9,482	2,845	2,904	79,614	88,087	41,296	47,507	22,862	22,862	148,494	170,842	1,558,096	1,558,096	1,706,590	1,728,938

Details of individual assets by account furnished upon request.

UTIMCO 7/10/2007

UTIMCO Performance Summary

May 31, 2007

	Net Asset Value 5/31/2007 (in Millions)	Periods Ended May 31, 2007 (Returns for Periods Longer Than One Year are Annualized)										
ENDOWMENT FUNDS		One Month	Three Months	Calendar Year To Date	Six Months	Fiscal Year To Date	One Year	Two Years	Three Years	Four Years	Five Years	Ten Years
Permanent University Fund	$ 11,763.6	2.10	6.74	9.09	10.26	15.14	17.85	16.23	15.28	16.45	12.45	9.72
General Endowment Fund		2.09	6.77	9.30	10.50	15.52	18.23	16.35	15.35	16.55	12.62	N/A
Permanent Health Fund	1,107.3	2.07	6.71	9.23	10.41	15.45	18.17	16.27	15.28	16.44	12.51	N/A
Long Term Fund	5,328.2	2.07	6.71	9.23	10.41	15.46	18.17	16.28	15.28	16.45	12.53	10.28
Separately Invested Funds	170.8	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Total Endowment Funds	**18,369.9**											
OPERATING FUNDS												
Short Term Fund	1,558.1	0.45	1.33	2.19	2.65	4.01	5.38	4.72	3.79	3.09	2.78	3.97
Intermediate Term Fund	3,740.0	1.20	4.06	6.13	6.21	11.02	14.17	N/A	N/A	N/A	N/A	N/A
Total Operating Funds	**5,298.1**											
Total Investments	**$ 23,668.0**											
BENCHMARKS (1)												
Permanent University Fund: Policy Portfolio		1.97	5.89	7.29	8.15	13.81	16.95	15.52	14.33	14.41	10.85	10.06
General Endowment Fund: Policy Portfolio		1.97	5.89	7.29	8.15	13.81	16.95	15.52	14.33	14.41	10.85	9.68
Short Term Fund: 90 Day Treasury Bills Average Yield		0.44	1.34	2.14	2.59	3.90	5.20	4.51	3.66	3.00	2.71	3.79
Intermediate Term Fund: Policy Portfolio		0.84	2.84	4.68	4.62	9.77	12.98	N/A	N/A	N/A	N/A	N/A
VALUE ADDED (2)												
Permanent University Fund		0.13	0.85	1.80	2.11	1.33	0.90	0.71	0.95	2.04	1.60	(0.34)
General Endowment Fund		0.12	0.88	2.01	2.35	1.71	1.28	0.83	1.02	2.14	1.77	N/A
Permanent Health Fund		0.10	0.82	1.94	2.26	1.64	1.22	0.75	0.95	2.03	1.66	N/A
Long Term Fund		0.10	0.82	1.94	2.26	1.65	1.22	0.76	0.95	2.04	1.68	0.60
Short Term Fund		0.01	(0.01)	0.05	0.06	0.11	0.18	0.21	0.13	0.09	0.07	0.18
Intermediate Term Fund		0.36	1.22	1.45	1.59	1.25	1.19	N/A	N/A	N/A	N/A	N/A

(1) - Effective May 6, 2004, benchmark returns for the PUF policy portfolio have been restated for prior periods beginning June 1, 1993 through September 30, 2000 and for the GEF/LTF policy portfolio for prior periods beginning June 1, 1993 through September 30, 2001 to correct the following technical errors in benchmark construction and calculation: (a) to reflect actual asset class target allocations which were in place, or the practical implementation of changes to those policy allocations, and (b) to distinguish between PUF and GEF/LTF historical investment objectives and distribution policies by accurately representing actual asset class allocations during those periods.

Benchmark returns for the PUF and GEF/LTF policy portfolios were also restated for all prior periods beginning June 1, 1993 through December 31, 2003 to replace various benchmark returns reported previously for the Private Capital asset class. Specifically, the Wilshire 5000 + 4%, the benchmark used prior to January 1, 2004, was replaced with the Venture Economics Periodic IRR Index, a more appropriate benchmark measure for the actual Private Capital portfolio.

Effective August 10, 2006, benchmark returns for the PUF and GEF policy portfolios were also restated for periods beginning January 1, 2006 through April 30, 2006, and for the ITF policy portfolio for periods beginning February 1, 2006 to April 30, 2006, to replace benchmark returns for the Hedge Fund asset class due to integrity concerns regarding existing benchmarks. Specifically, composites of Standard & Poor's investable hedge fund indices were replaced with the MSCI Investable Hedge Fund Index.

Complete details of the restatements and previous policy portfolio benchmark history are documented on the UTIMCO website at www.UTIMCO.org or are available upon request.

(2) - Value added is a measure of the difference between actual returns and benchmark or policy portfolio returns for each period shown. Value added is a result of the active management decisions made by UTIMCO staff and external managers.

UTIMCO 7/10/2007

14. 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 120, which includes the capital expenditures budget, and the Annual Fee and Allocation Schedule for the fiscal year ending August 31, 2008, as set forth on Page 123.

BACKGROUND INFORMATION

A proposed Annual Budget of $64.6 million for Fiscal Year 2008 was approved by the UTIMCO Board on July 11, 2007. The proposed Budget is an increase of $16.8 million or 35% from the Fiscal Year 2007 Forecast.

Of the $64.6 million Fiscal Year 2008 Budget, however, only $15.4 million is for UTIMCO services and $6.5 million is for non-investment manager services such as custodial, legal, audit, and consulting services charged to the Funds. This combined $21.9 million compares to the $17.5 million Fiscal Year 2007 Forecast or an increase of $4.4 million, $3.1 million of which is compensation-related resulting from budgeting to fill open positions and promotions/raises for existing staff.

The remainder of the Budget is for investment manager annual and performance fees charged directly to the Funds. The budgeted increase is primarily driven by fund performance assumptions.

Discussion materials presented by UTIMCO President, Chief Executive Officer, and Chief Investment Officer Bruce Zimmerman are on Pages 119 - 123.

The proposed Annual Fee and Allocation Schedule shows the allocation of the proposed budgeted expenses among U. T. System funds. The fees are to be paid quarterly.

The proposed capital expenditures budget totaling $.4 million is included in the total Annual Budget.

The Office of Finance Review of the UTIMCO Budget FY 2008 is on Pages 124 - 139.

Budget materials prepared by UTIMCO

THE UNIVERSITY OF TEXAS INVESTMENT MANAGEMENT COMPANY

($ in millions)	2006/07 Budget	2006/07 Forecast	2007/08 Budget	2007/08 Budget vs 2006/07 Forecast	
UTIMCO Services	$	$	$	$	%
Salaries	$ 5.9	$ 5.0	$ 6.0	$ 1.0	21%
Bonus	2.9	1.8	3.3	1.5	82%
Employee Benefits	1.0	0.8	1.2	0.4	56%
Payroll taxes	0.4	0.3	0.4	0.1	37%
Total Compensation	10.2	7.9	10.9	3.0	39%
Other Personnel Related Costs	0.6	0.6	0.7	0.1	9%
Occupancy	1.2	1.4	1.6	0.2	15%
Travel	0.4	0.2	0.4	0.2	98%
Other Direct	1.5	1.9	1.8	(0.1)	-6%
Total UTIMCO Services	**13.9**	**12.0**	**15.4**	**3.4**	**28%**
Direct Costs to Funds				$	%
Custodian Fees and Other Direct Costs	1.3	1.5	1.5	$ -	4%
Performance & Risk Measurement and Analytics	1.8	1.4	1.5	0.1	7%
Consultant Fees	1.4	1.2	1.3	0.1	7%
Legal & Audit	1.3	1.2	1.9	0.7	62%
Other	0.3	0.2	0.3	0.1	20%
Cost to Funds Excluding Investment Manager Fees	**6.1**	**5.5**	**6.5**	**1.0**	**18%**
UTIMCO + Non-Investment Manager Cost to Funds	**20.0**	**17.5**	**21.9**	**4.4**	**25%**
Investment Manager Fees Charged to Funds	16.8	16.8	19.0	2.2	13%
Inv Mgr Performance Fees Charged to Funds	20.6	13.5	23.7	10.2	76%
Total Investment Manager Fees	**37.4**	**30.3**	**42.7**	**12.4**	**41%**
Grand Total	**$ 57.4**	**$ 47.8**	**$ 64.6**	**$ 16.8**	**35%**

Capital Expenditures				$	%
Ongoing	$ 0.2	$ 0.2	$ 0.2	$ -	0%
Expansion	-	-	0.2	0.2	100%
Total Capital Expenditures	**$ 0.2**	**$ 0.2**	**$ 0.4**	**$ 0.2**	100%

The University of Texas Investment Management Company

($ in millions)	Actual					Projected	Budget - AUM Flat	Budget - AUM 3%
	FY 02	FY 03	FY 04	FY 05	FY 06	FY 07	FY 08	FY 08
Average Total Assets Under Management (AuM):	**$ 13,716**	**$ 14,034**	**$ 15,470**	**$ 17,245**	**$ 19,372**	**$ 22,162**	**$ 22,162**	**$ 22,827**
Costs excluding Investment Manager Expenses								
UTIMCO Services	$5	$7	$8	$10	$11	$12	$15	$15
Costs to Funds (Other than Investment Manager)	5	4	4	5	5	6	7	7
UTIMCO + Non-Investment Manager Cost to Funds	$10	$11	$12	$15	$16	$18	$22	$22
Costs/AuMs (basis points)								
UTIMCO Services	3	5	5	6	6	5	7	7
Costs to Funds (Other than Investment Manager)	4	3	3	3	2	3	3	3
UTIMCO Services + Costs to Funds	**7**	**8**	**8**	**9**	**8**	**8**	**10**	**10**
Investment Manager Fees								
Annual Management Fees								
Netted Against Net Asset Value/Capital Balance	$51	$53	$62	$77	$111	$149	$170	$170
Charged to Funds	11	9	13	13	18	17	19	19
Total Annual Management Fees	**$62**	**$62**	**$75**	**$90**	**$129**	**$166**	**$189**	**$189**
Performance Fees								
Netted Against Net Asset Value/Capital Balance	$12	$44	$57	$91	$81	$234	$158	$158
Charged to Funds	4	3	9	16	30	13	24	24
Total Performance Fees	**$16**	**$47**	**$66**	**$107**	**$111**	**$247**	**$182**	**$182**
Total Investment Manager Fees	**$78**	**$109**	**$141**	**$197**	**$240**	**$413**	**$371**	**$371**
Costs/AuMs (basis points)								
Annual Management Fees	**45**	**44**	**48**	**52**	**67**	**75**	**85**	**83**
Performance Fees	**12**	**33**	**43**	**62**	**57**	**111**	**82**	**80**
Total Fees	**57**	**77**	**91**	**114**	**124**	**186**	**167**	**163**

Active Management Value Added

PUF & GEF	Return Year ending August 31, 2002	Return Year ending August 31, 2003	Return Year ending August 31, 2004	Return Year ending August 31, 2005	Return Year ending August 31, 2006	Return 10 months ending June 30, 2007
Passive Portfolio Return *(70% S&P 500; 30% Lehman Agg Bond)*	-10.49%	10.23%	9.95%	10.07%	6.72%	12.77%
PUF & GEF Actual Return *Net of Fees*	-7.28%	12.21%	14.68%	18.78%	11.13%	15.19%
Active Management Net Value Added Return	**3.21%**	**1.98%**	**4.73%**	**8.71%**	**4.41%**	**2.42%**
Net Value Added Fiscal YTD ($ in thousand)	$ 358,301	$ 201,473	$ 520,522	$ 1,060,864	$ 630,702	$ 386,811
"Tactical" Allocation Decisions YTD	$ -	$ -	$ -	$ (87,461)	$ (40,227)	$ (73,080)
Net Value Added Excluding *Tactical Decisions	**$ 358,301**	**$ 201,473**	**$ 520,522**	**$ 1,148,325**	**$ 670,929**	**$ 459,891**

UTIMCO Budget
Annual Fee and Allocation Schedule
For the fiscal year ending August 31, 2008

($ millions)	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
Market Value 2/28/07	**$ 11,059**	**$ 1,047**	**$ 4,950**	**$ 5,997**	**$ 3,519**	**$ 1,267**	**$ 200**	**$ 22,042**
UTIMCO Management Fee (includes all operating expenses associated with the general management of the Funds)	**$ 7.5**	**$ 0.9**	**$ 4.4**		**$ 2.6**			**$ 15.4**
Allocation Ratio	**49%**	**6%**	**29%**		**17%**			**100%**
Direct Expenses of the Fund								
External Management Fees	$ 9.7	$ -	$ -	$ 5.3	$ 4.0			$ 19.0
External Management Fees - Performance Based	12.8	-	-	6.8	4.1			23.7
Other Direct Costs	3.2	-	0.2	2.1	1.0			6.5
Total Direct Expenses of the Fund	25.7	-	0.2	14.2	9.1		-	49.2
TOTAL	**$ 33.2**	**$ 0.9**	**$ 4.6**	**$ 14.2**	**$ 11.7**		**-**	**$ 64.6**
<u>Percentage of Market Value (in basis points)</u>								
UTIMCO Services	6.8	8.6	8.8	-	7.2			7.0
Direct Expenses of the Fund	23.3	23.9	24.0	-	26.0			22.3
TOTAL	**30.1**	**32.5**	**32.8**	**-**	**33.2**			**29.3**

Budget Review prepared by the Office of Finance

July 17, 2007

Fiscal Year 2008

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 17, 2007

Fiscal Year 2008
UTIMCO BUDGET REVIEW

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Fiscal Year 2008 UTIMCO BUDGET REVIEW

I. EXECUTIVE SUMMARY

This review, prepared for the U. T. System Board of Regents and the Chancellor, offers information and analysis to help address fiduciary duties to manage and control investment management costs, making a reasonable effort to determine that the costs are "reasonable and appropriate," as required by the new Texas Uniform Prudent Management of Investment Funds Act (UPMIFA).

This report reviews The University of Texas Investment Management Company (UTIMCO) staff's proposed **$64.6 million FY08 budget**, consisting of **UTIMCO Services** (corporate) and **Direct Costs to U. T. System Funds** (third party management and performance fees, custodial, consulting, direct legal, audit, and risk management). **Capital expenditures** totaling nearly **$356k** are also reviewed. FY07 projections provided by UTIMCO staff are based on actual UTIMCO Services expenses through April 30 and actual Direct Costs to Funds through May 31, 2007.

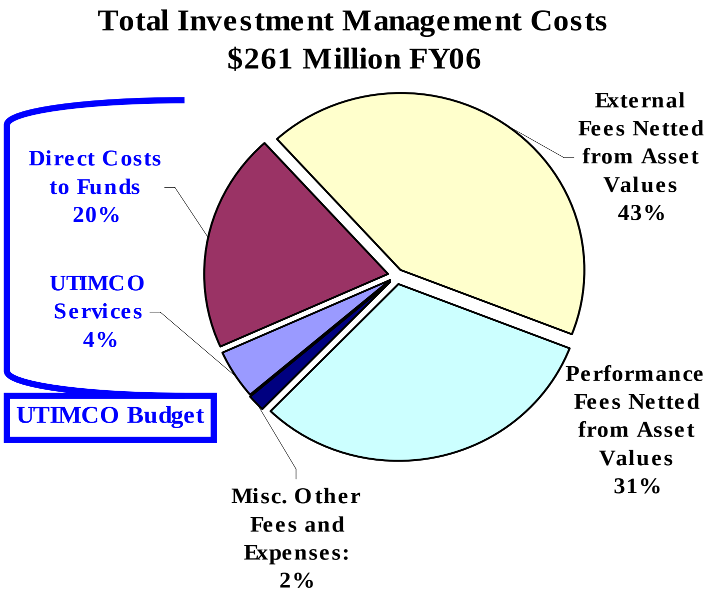
Total investment management costs through FY06 are briefly summarized on page 2. The Office of Finance will update and further analyze total costs in comparison to performance and value added when audited financials for FY07 are available, and report the results during the second fiscal quarter of FY08.

<u>Highlights</u>: Although the timing of the budget presentation was delayed for revisions, we appreciate UTIMCO staff's efforts to provide full detailed disclosure of operations and assumptions.

- **UTIMCO Costs in FY07** are projected to be nearly 17% under budget overall.
- **Average Assets Managed per Employee** increased 29% from FY03 - FY07, evidencing some economies of scale. This was accomplished even with centralization of operating funds implemented during FY06, which required a major commitment by UTIMCO staff to fully invest the new Intermediate Term Fund's more than $3 billion in a diversified portfolio asset allocation.
- **Total Costs FY02 - FY06** (page 2): Total costs, dominated by external management and performance fees, more than doubled as a percentage of average assets under management from **0.66% in FY02 to 1.35% in FY06**.
- **Salaries** (page 5)**:** Nearly half of the **20.6%** increase in budgeted salaries ($1.0 million) relates to filling 11 open positions and three new budgeted positions; the balance reflects **12.1%** average salary increases for existing staff overall (including promotions, but excluding the president).
- **Lease Expense** (page 6): Lease expenses are continuing to escalate per the original lease terms.
- **Risk Management** (pages 7-8)**:** Expenditures that are chronically below budgeted amounts for risk analytic tools raise questions about transparency of private holdings for risk management purposes.
- **Audit and Legal** (page 8)**:** Audit and controls assessment fees are budgeted at more than double last year due to changing audit firms and additional time required to audit valuations of alternative investments. The trend to higher legal fees is also expected to continue with the increasing asset base and continuing shift to more complex alternative investments throughout the portfolios.
- **UTIMCO fee allocation** (page 9): The **$15.4 million** UTIMCO Services fee is a 10.3% increase over the FY07 fee in dollar terms; however, at 0.070% of February 28, 2007 assets under management (AUM), the UTIMCO Services fee is slightly lower than this year's 0.072% of mid-year FY06 AUM.
- **UTIMCO Reserves** (Exhibit D)**:** UTIMCO staff's analysis of the UTIMCO fiscal year-end balance sheet estimates **$875k** in available cash reserves. In 2004 and 2005, a total of $8 million in surplus UTIMCO corporate reserves ($4 million each year) were distributed back to the U. T. System Funds. There was no distribution in 2006 and we recommend no distribution again this year.

II. Total Investment Management Costs

UTIMCO budgeted costs 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. Proposed capital expenditures are also discussed.



The chart illustrates that in FY06, UTIMCO Services and direct budgeted costs represented only 24% of the $261 million in total costs. Investment fund management fees and expenses for partnerships, hedge funds, mutual funds that are netted from reported investment results are not budgeted because they are not paid directly by U. T. System Funds. These expenses in FY06 were 74% of total investment management costs. Other expenses budgeted by the U. T. System (2% of total costs) are fees for education and endowment compliance (LTF only), and investment oversight.

Table 1 below shows the trend of total actual investment management costs as a percentage of average assets under management (AUM) [**from 0.66% of AUM ($90.6 million) in FY02 to 1.35% of AUM ($260.9 million) in FY06**]. Increases in external management and performance fees reflect the shift to alternative investments throughout the portfolios. We are recommending that investment management costs be benchmarked against peers again in FY08.

Table 1
UTIMCO Total Investment Cost Summary Trend FY02 - FY06 ($ Millions)

	FY02	FY03	FY04	FY05	FY06	% of Total Costs
UTIMCO Services	5.0	7.6	8.8	10.2	11.3	**4%**
Direct Costs to Funds	20.1	16.0	25.5	33.8	52.3	**20%**
External Fees Netted from Asset Values	50.6	52.7	62.5	76.5	111.3	**43%**
Performance Fees Netted from Asset Values	12.0	44.0	56.9	90.5	81.6	**31%**
Miscellaneous Other Fees and Expenses:	2.9	3.0	3.0	3.8	4.4	**2%**
Total Investment Management Costs	**90.6**	**123.3**	**156.7**	**214.8**	**260.9**	**100%**
Total % of Average Assets Under Management *	**0.66%**	**0.88%**	**1.01%**	**1.25%**	**1.35%**	

**Average assets under management were calculated using beginning and ending FY totals as of August 31 and dividing by two.*

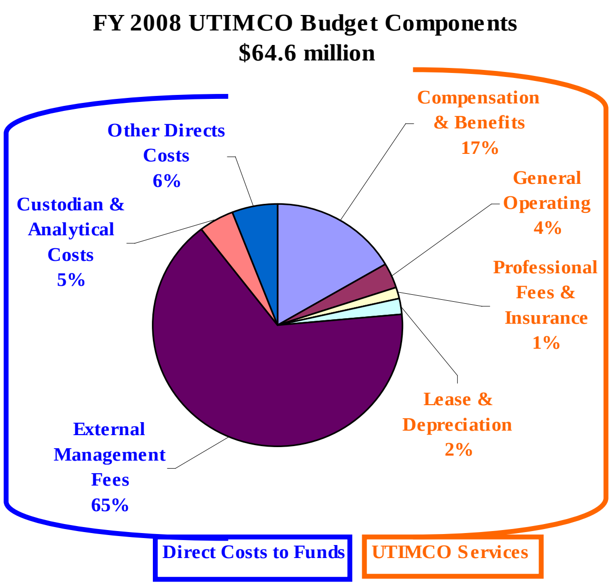
III. UTIMCO Operating Budget Analysis and Trends

UTIMCO proposes a total budget for FY08 (excluding capital expenditures) of **$64.6 million**. Table 2 on page 3 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. Total budgeted investment management costs peaked in FY06, are projected to normalize in FY07, returning to peak levels budgeted for FY08.

Table 2
UTIMCO Budgeted Investment Management Cost Trend FY02 - FY08 ($ Millions)

	Actual					Projected	Budget
	FY02	FY03	FY04	FY05	FY06	FY07	FY08
Average Total Assets Under Management (AUM) *	13,716	14,034	15,470	17,245	19,372	22,042	22,042
% Change in AUM	-8%	2%	10%	11%	12%	14%	0%
UTIMCO Services	5.0	7.6	8.8	10.2	11.3	12.0	15.4
% Change in UTIMCO Services		53%	16%	16%	11%	6%	28%
UTIMCO Services % of AUM	0.036%	0.054%	0.057%	0.059%	0.058%	0.054%	0.070%
Direct Costs to Funds	20.1	16.0	25.5	33.8	52.3	35.8	49.2
% Change in Direct Costs to Funds		-20%	59%	33%	55%	-32%	37%
Direct Costs to Funds % of AUM	0.147%	0.114%	0.165%	0.196%	0.270%	0.162%	0.223%
Total Budgeted Costs	**25.1**	**23.6**	**34.3**	**44.0**	**63.6**	**47.8**	**64.6**
% Change in Total Budgeted Costs		-6%	45%	28%	45%	-25%	35%
Total Budgeted Costs % of AUM	**0.183%**	**0.169%**	**0.222%**	**0.255%**	**0.328%**	**0.217%**	**0.293%**

**Total average assets under management (AUM) were calculated for FY 2003-2006 using beginning and ending FY totals as of August 31 and dividing by two. Values shown for FY07 and FY08 are actual total assets as of February 28, 2007. Actual total AUM as of May 31, 2007 were $23.668 billion.*



The chart shows the breakdown of the total UTIMCO budget. The UTIMCO Services operating budget accounts for 24% of the total, with personnel costs the largest component. Direct Costs to Funds include external management and performance fees paid directly, custodial, consulting, legal, analytical, and other direct costs. External management fees paid directly dominate the total budget (65%). UTIMCO retains external managers for approximately 76% of the $23.7 billion in assets (including operating funds), as of May 31, 2007; internal staff manages 24% of fund assets, plus approximately **$4.8 billion** in gross-weighted derivatives positions (as of 5/31/07).

Last Year's Forecast for FY06: This time last year UTIMCO staff forecast UTIMCO budgeted costs for FY06 to be $53.9 million, nearly 11% over the $48.5 million budgeted. Actual total UTIMCO FY06 costs were $63.6 million – $15 million (31%) over budget and nearly $10 million (18%) higher than forecast. Higher third party manager fees accounted for 90% of the forecast variance and were underestimated by more than $9 million (24%). Direct costs forecast at $43.4 million (0.21% of AUM) were actually $52.3 million (0.27% of AUM).

Table 3 below compares summary FY07 budget, FY07 projected actual expenses, and the proposed FY08 budget. Refer to Exhibits A and B (pages 11 and 12) for more detailed FY07 forecast, FY08 proposed budget, and six-year trends for FY03-FY08.

Table 3
UTIMCO FY07 Projected Actual and FY08 Budget Overview

	FY07				FY08			
	$ Budget	Projected $ Actual	$ Change vs FY07 Budget	% Change vs FY07 Budget	$ Budget	$ Change vs FY07 Projected	% Change vs FY07 Projected	% Change vs FY07 Budget
UTIMCO Services	13,940,638	12,007,190	(1,933,448)	-13.9%	15,369,830	3,362,640	28.0%	10.3%
Direct Costs to Funds	43,419,269	35,841,739	(7,577,529)	-17.5%	49,225,813	13,384,073	37.3%	13.4%
Total Budget	57,359,907	47,848,929	(9,510,978)	-16.6%	64,595,642	16,746,713	35.0%	12.6%

<u>FY07 Forecast versus Budget</u>: UTIMCO staff estimates that actual FY07 expenses will be approximately **$47.85 million** or **$9.5 million (17%) below** the total FY07 budget of $57.4 million.

- **UTIMCO Services** corporate expenses are projected to be under budget by **$1.9 million (14%)**
  - Unfilled positions, associated personnel costs, and reduced bonus expectations create nearly **$2.4 million** in budget savings.
  - Savings are partly offset by corporate legal expenses at 100% ($294k) over-budget, and excess recruiting and relocation costs.
- **Direct Costs to Funds** overall are projected to be under budget by **$7.6 million (17.5%).**
  - **External management and performance fees** are projected to be more than **$7.1 million (19%)** under budget in FY07.
  - **Risk measurement** costs are projected at nearly **$210k or 25% below budget**.
  - **Direct legal expenses** are nearly 18% below budget.
  - Custodial costs, on the other hand, are nearly 18% over budget.
- **Capital Expenditures** are substantially under budget year-to-date, but UTIMCO staff indicates that capital needs of **$115k** over the next two months (primarily IT upgrades) will use the balance of the $167k FY07 capital budget.

<u>FY08 Proposed Budget</u>: The proposed **$64.6 million** total UTIMCO budget (excluding capital expenditures) for FY08 is **35%** higher than FY07 projected actual expenses, **12.6%** higher than the FY07 budget, but less than **4%** higher than actual FY06 comparable costs.

- **UTIMCO Services FY08** proposed budget is an **increase of 28%** over FY07 projected actual costs, primarily due to increases in personnel-related costs, and corporate lease expenses.
- **Direct Costs to Funds** in total are budgeted to **increase 37%** over actual costs forecast for FY07, mainly due to expected increases in third party management fees.
- **Capital Expenditures** of **$356k** include IT planned upgrades, equipment and furniture for new staff.

IV. UTIMCO Services

This fiscal year FY07's budget was increased **$669k** last fall to accommodate retention bonuses and other expenses that accompanied staff turnover starting in September 2006. FY07 UTIMCO Services are now projected to be below the revised budget by $2.1 million excluding depreciation, and $1.9 million (14%) overall. Nearly 71% of the FY08 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 4 on page 5. Staffing of 44 employees at yearend FY07 is understated, with 11 open positions due to staff turnover (56 budgeted positions). Average total assets under management (AUM) were calculated for FY 2003-2006 using beginning and ending FY totals as of August 31 and dividing by two. Values shown for FY07 and FY08 are actual assets as of mid-year February 28, 2007 ($22.0 billion). The lag in estimated FY08 AUM results in understating FY08 AUM per employee and growth in AUM. [AUM as of May 31, 2007 is $23.7 billion.] Subject to these limitations of understated FY07 staffing and FY08 AUM, we observe the following trends:

- UTIMCO staff has grown 22% from FY03 to FY07, while managed funds increased 57% in that same period. Budgeted staffing in FY08 of 58 employees represents an increase of 32% over FY07.
- Funds managed per employee increased 29% from FY03 to FY07.
- Total compensation increased 62% in the aggregate since FY03, at an annualized rate of 12.8%.
- Average total compensation per employee increased 32% since FY03 to more than $154k forecast in FY07 - an annualized growth rate of 7.2%.
- Bonus compensation increased 64% since FY03 based on FY07 projected actual (13.2% annualized).
- Budgeted salaries increase 21% in FY08; bonuses increase 82%; and total compensation is budgeted at a one-year increase of 37%.

Table 4
UTIMCO Compensation and Headcount FY03 - FY08

	FY03 Actual	FY04 Actual	FY05 Actual	FY06 Actual	FY07 Projected	Growth Rate Since FY03	Growth Rate (annualized)	FY08 Budget*	FY08 % Increase from FY07
Employees (as of year end)	36	36	43	41	44	22%	5.1%	58	32%
Average Total AUM ($Millions) *	14,034	15,470	17,245	19,372	22,042	57%	11.9%	22,042	0%
Average AUM/Employee ($Millions)	390	430	401	472	501	29%	6.5%	380	-24%
Salaries and Wages	3,102,883	3,773,961	4,203,100	4,492,078	4,985,344	61%	12.6%	6,011,318	21%
Bonus Compensation	1,089,333	1,858,653	2,094,447	2,164,963	1,791,678	64%	13.2%	3,258,381	82%
Total Compensation	4,192,216	5,632,614	6,297,547	6,657,040	6,777,021	62%	12.8%	9,269,699	37%
Total Compensation per Employee	116,450	156,462	146,455	162,367	154,023	32%	7.2%	159,822	4%
Bonus as % of Salaries and Wages	35%	49%	50%	48%	36%			54%	
Bonus as % of Total Compensation	26%	33%	33%	33%	26%			35%	

Staffing: In FY07 the budget was based on staffing of 55 employees; actual staffing is projected to be 44 employees at fiscal year-end 2007. Staff turnover during FY07 saved nearly $2.4 million in budgeted personnel related costs, leaving an estimated 11 unfilled budgeted positions at year-end. UTIMCO staff provided a list of current budgeted unfilled positions and proposed new positions for FY08. Three budgeted positions have been open for at least three years. The FY08 budget adds three new positions and assumes that all open budgeted positions are filled for three quarters of the year.

Compensation: The FY08 budget for total compensation and employee benefits, representing 71% of the total UTIMCO Services budget, increased $3.0 million (39%) to $10.9 million from a projected $7.8 million in FY07.

- **Salaries and Wages** are projected to be approximately $925k (16%) under budget in FY07 because of staff turnover and unfilled positions. Nearly half of the overall budgeted increase in salaries of more than $1.0 million (**20.6%**) results from new staffing; the remaining $517k represents **12.1%** overall salary increases for existing staff (excluding the president), comprised as follows:
  - Promotions for seven key employees with increased responsibility (average raise **34%**).
  - Base salary increases averaging **9.7%** for 13 other performance plan participants.
  - Average base wage increases budgeted at **4.82%** for non-participants in the performance plan.

- **Bonus compensation** for FY07 based on performance year-to-date (including deferred bonuses earned in prior years and related investment income) is forecast at $1.8 million - nearly $1.1 million (38%) under budget and on average 36% of total salaries and wages - because of eligible staff departures, unfilled positions, and performance below budgeted expectations.

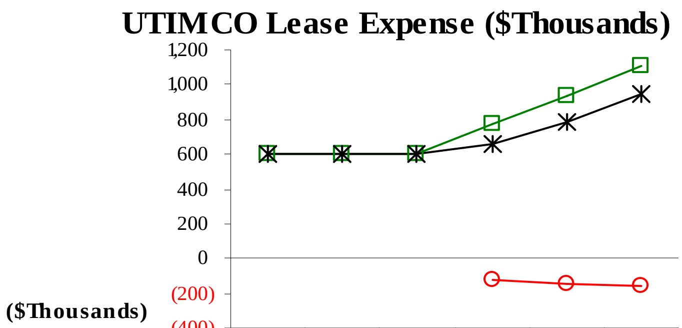
  The FY08 budget of nearly **$3.3 million** in bonuses is **82% higher** than projected FY07 actual bonuses, assuming that all eligible participants earn **70% of the maximum** incentive award and 30% of that earned amount is deferred, budgeted, and paid over the next three fiscal years. The FY08 budget also includes deferred bonuses earned by employees in prior years, related investment income (at 8.5%), and funds for a discretionary bonus pool up to 15% of salaries for employees not eligible to participate in the formal incentive plan.

  In FY07 UTIMCO budgeted for 50% of the incentive award opportunity to be paid under the incentive bonus plan. This increase from 50% to 70% budgeting is based on the trend rate for actual bonuses earned by participants as a percentage of maximum (68.0% for FY06 and 69.5% for FY05).

- **Employee Benefits** are expected to be under budget in FY07 by $281k (27%) due to unfilled existing positions. Employee Benefits costs are budgeted to increase 59% to $1.2 million in FY08, reflecting increased staffing and higher costs. Employee Benefits budgeted for FY08 cost roughly 19% of proposed base compensation. 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.

General Operating Expenses are on target with the budgeted amount for FY07 of $1.9 million. The FY08 budget proposes a 14% increase, primarily due to increased staffing, for on-line data, contract services, recruiting and relocation expenses, and travel.

Lease Expense: The chart illustrates that lease expenses have started and will continue to escalate:



	FY03	FY04	FY05	FY06	FY07	FY08
Gross Lease Expense	606	599	601	779	937	1,105
Deferred Rent Credit				(124)	(149)	(162)
Reported Lease Expense	606	599	601	655	788	943

- Base rent and parking costs are increasing.
- Rent for an additional 3,157 square feet of space commences in January 2008.
- Operating expenses that are passed through to tenants are escalating.

Lease expense in FY07 is projected to be 3% under budget; however, the ($148k) amortization of the "deferred rent credit" (14 months of "free rent" plus leasehold improvements) that is recorded in the forecast was budgeted instead to reduce depreciation and amortization.

Gross lease expenses are approximately **$937k** in FY07 ($779k in FY06). FY08 budgeted lease expense of **$943k** includes a **($162k)** credit for deferred rent amortization. Lease operating expenses are estimated at 22% over budget in FY07 and budgeted to increase another 35% in FY08. Property taxes have already doubled since UTIMCO took occupancy, and UTIMCO staff is negotiating with management regarding last year's pass-through charges (taxes insurance, utilities, management, etc.)

UTIMCO's move in the fall of 2005 (FY06) to 70% larger space in the Frost Bank Tower was intended to accommodate staffing growth over the 11-year lease term. At budgeted staffing of 58 employees in FY08, the 29,000+ square foot space allows an average of more than 500 square feet per employee, including executive offices, conference spaces, and other common areas already completed; 3,157 square feet more space brings this average to more than 550 square feet per budgeted full time employee.

Professional Fees: Total Professional Fees are expected to be $666k in FY07, **79% higher** than the budgeted amount of $371k. Legal fees account for this difference, at 100% over budget mainly due to staff turnover during the year, legislative session, and other issues. Budgeted cost savings related to the recent addition of in-house counsel at UTIMCO are reflected in UTIMCO services proposed FY08 budget, at $230k less than projected FY07 actual fees.

V. UTIMCO Capital Expenditures

Capital expenditures of nearly **$356k** requested for FY08 are detailed in Exhibit C and summarized in Table 5 on page 7. Approximately $194k in proposed expenditures include ongoing planned IT upgrades, and $160k proposed for expansion includes equipment and furniture for new staff, and leasehold improvements for the additional 3,157 square feet of office space.

Capital Expenditures associated with the office move to the Frost Bank Tower through FY06 were approximately $2.7 million, of which $1.6 million was credited toward rent as an allowance for leasehold improvements. UTIMCO staff advises that leasehold improvements up to a maximum of the **$55 psf** landlord allowance for the additional space will not require supplemental capital and will only be spent as needed to accommodate new staff.

Table 5
UTIMCO Capital Expenditures and Depreciation

	Budget FY06	Actual FY06	Variance	Budget FY07	Projected FY07	Variance	Budget FY08	Variance vs Projected FY07
Leasehold Improvements (net)	786,452	637,811	-19%	-	1,943	N/A	5,000	157%
Furniture & Fixtures (including artwork)	485,000	499,461	3%	47,000	41,170	-12%	104,599	154%
Office Equipment, Computers & Software	366,000	267,506	-27%	120,000	121,040	1%	245,970	103%
Total Capital	1,637,452	1,404,778	-14%	167,000	164,153	-2%	**355,569**	117%
Total Depreciation/amortization	535,900	504,637	-6%	410,720	564,487	37%	**607,500**	8%

Depreciation is projected to be over budget by about $154k (37%) in FY07 because the amortization of deferred rent credit that was budgeted to reduce depreciation and amortization is reported as a credit against lease expense in FY07. “Deferred rent expense” ($1.8 million) that includes allowances for leasehold improvements is amortized over the life of the lease.

VI. Direct Costs to Funds

Direct Costs to Funds for FY07, including centralized operating funds, are projected at $35.8 million or 17.5% below a budgeted $43.4 million. The FY08 budget increases 37% from projected FY07 costs. We are not prepared at this writing to review incremental direct costs for centralized operating funds.

Base and Performance Management Fees paid to external managers continue to increase in both dollar terms (Exhibit B page 11) and as a percentage of assets. These fees, projected at $30.3 million in FY07 (19% below budget) and budgeted at $42.7 million, represent approximately 86% of Direct Costs to Funds budgeted in FY08. UTIMCO staff estimates base and performance fees in detail, based on each manager’s fee structure and asset base. Performance fees in particular are very difficult to forecast.

Custodial and performance measurement costs: Mellon custodial fees were reduced as a consequence of the RFP process completed in FY06. Competitive fee savings have been offset, however, by increasing assets and services, and custodial fees are forecast at $1.5 million - $221k (17.6%) over budget. The FY08 budget estimates these costs will increase only 4% over FY07 levels. Performance measurement expenses paid to Mellon in FY07 projected to be 21% below budget at $419k, on the other hand, are budgeted in FY08 to increase 28% to $537k.

Timely independent verification of performance and asset allocation information and close monitoring of internal derivative positions are critical to support UTIMCO's increasingly active management style. Internal derivatives positions of approximately **$4.84 billion** gross-weighted (20% of U. T. System total assets as of May 31, 2007) 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: Risk Management System expenses charged to the funds are expected to be **25% ($210k) under budget** again this fiscal year. Actual costs in FY06 were 66% below budget. Risk system costs for FY07 were budgeted at $400k for the traditional portfolio and $450k for 31 hedge funds (14 existing, 17 new) for a total of $850k.

We have been concerned that FY07 projected expenditures are significantly below budget because transparency of external hedge fund holdings is lagging budgeted expectations. All public markets managers now report holdings for analysis in the risk model as of the end of each month, either to UTIMCO or directly to IFS; however, only **six of 48 hedge funds** are reporting holdings ($335 million). The FY08 budget reflects costs of nine more funds reporting.

Absent actual holdings data, UTIMCO's risk model uses proxy indices and Albourne's proprietary factor- and return-based risk statistics to simulate the risk profile for **nearly one third of the U. T. System assets**: 42 hedge funds (approximately **$5.65 billion** in U. T. System assets as of 6/30/07) and all private capital funds (**$1.96 billion**). Concerns about the reliability of available data include:

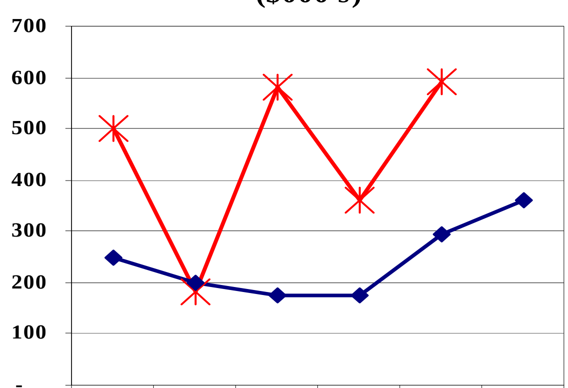
- Broad range of strategies with varying leverage and other risk factors among private capital and hedge funds.
- Broad range of returns, volatility, and correlation statistics among managers/funds.
- Flexibility of hedge fund managers to alter strategies and shift risk profiles dramatically and rapidly.
- Monthly reporting of risk statistics, available approximately three to four weeks after month-end.
- Small cap growth index proxy for private capital investments may not adequately characterize the portfolio risk.

UTIMCO staff's selection process for hedge funds attempts to mitigate portfolio risks by diversifying broadly, minimizing leverage, scrutinizing operational risk factors, and choosing funds with low historical volatility. As UTIMCO staff gains experience with the behavior of the proxy and consultant data relative to that of the actual hedge fund portfolios, confidence is increasing that these are reliable (arguably superior) substitutes for actual hedge fund holdings reported only once a month. [e.g., Actual annual returns of the hedge fund pool over the past 4 years were 11.9% with volatility of 3.2%, while the proxy showed annual returns of 10.25% with volatility of 3.2%.] More energy is needed, however, to increase confidence in the risk profile of the private capital portfolio.

Audit and Controls Assessment expenses in FY07 of $336k funded Ernst & Young and U. T. System Audit Office fees for Sarbanes-Oxley controls assessments for UTIMCO Corporation, the PUF, GEF, LTF, and PHF. Audit fees for FY08, budgeted at **$754**k, include **$649k** for external auditors, U. T. System Audit Office charges of $30k to assess controls for the ITF, and $75k for an independent consultant to assess investment staff due diligence and monitoring policies and practices. The increase reflects the change in auditors and additional time required to audit valuations of alternative investments.

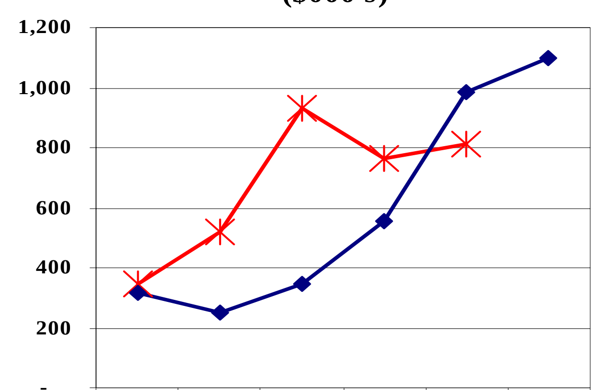
Legal fees: The charts below track budgeted and actual UTIMCO corporate legal fees and direct legal expenses charged to the funds since FY03. The spike in corporate legal fees in 2005 was attributed to disclosure issues related to private capital investments and analysis of centralization options; higher fees again in FY07 are due to staff turnover and legislative session issues. Legal fees paid directly by U. T. System Funds in FY07 are projected to be approximately $810k (18% below budget). The budgeted $290k (36%) increase in direct legal expenses in FY08 is partly due to the estimated $250k cost of anticipated secondary market sales of certain private equity investments.

UTIMCO Services Legal Expenses ($000's)



	FY03	FY04	FY05	FY06	FY07 Fore-cast	FY08 Budget
Actual	501	183	580	362	590	
Budget	250	200	175	175	295	360

Direct Costs to Funds Legal Expenses ($000's)



	FY03	FY04	FY05	FY06	FY07 Fore-cast	FY08 Budget
Actual	344	518	933	762	810	
Budget	315	250	346	555	985	1,100

VII. Proposed UTIMCO Services Fee Allocation

Table 6 shows the allocation formula proposed by UTIMCO staff for FY08, including estimates of direct costs for each of the funds but excluding U. T. System administration education, compliance, and oversight fees and expenses. Note that the UTIMCO Services fee is charged to the PHF and the LTF, not to the GEF where they are pooled; direct costs, on the other hand, are charged to the GEF. The total budgeted expense as a percent of 2/28/07 market values for each fund is shown at the bottom of the table.

The **$15.4 million UTIMCO Services fee** to be allocated to U. T. System funds is a 10.3% increase over the FY07 fee; however, it represents a slight decrease from this fiscal year's estimated 0.072% of 2/28/06 AUM ($19.4 billion). The proposed formula for FY08 allocates 16.5% of budgeted UTIMCO Services expenses to the ITF, reduced from 20% in FY07 -- the first full fiscal year for the fund. The ITF represents approximately 16% of total assets as of February 28, 2007; and the compensation program weights the ITF at 15% for entity performance targets. At 0.072% of total 2/28/07 ITF assets, UTIMCO Services expenses allocated to the ITF are higher than the PUF, lower than the PHF and LTF.

Direct Expenses of the Funds: UTIMCO staff estimates external manager fees from the bottom up, looking at each manager and fund. Alternative investment funds (hedge funds and private equities) "net" fees and expenses from reported asset values, so these expenses are not paid directly by U. T. System funds. Because the ITF has no private equities but does have allocations to hedge funds comparable to the endowments, the proportion of total investment management fees paid directly by the ITF (as opposed to being netted from asset values) is slightly higher than for the other funds (0.260% of market value versus 0.233% estimated for the PUF and 0.236% estimated for the GEF).

Table 6
UTIMCO Fee and Direct Budgeted Expense Proposed Allocation Fiscal Year Ending August 31, 2008

	Fund Name						Separate Funds (SIF)	Total
	PUF	PHF	LTF	GEF (2)	ITF	STF (1)		
Market Value 2/28/07 ($ millions)	**11,059**	**1,047**	**4,950**	**5,997**	**3,519**	**1,267**	**200**	**22,042**
Percent of Total Market Value as of 2/28/07	**50.2%**	**4.8%**	**22.5%**	**27.2%**	**16.0%**	**5.7%**	**0.9%**	**100%**
FY07 UTIMCO Services Allocation Ratio	**46.2%**	**6.0%**	**27.8%**	**33.8%**	**20.0%**	**0.0%**	**0.0%**	**100%**
FY08 Proposed UTIMCO Services Allocation Ratio	**49.1%**	**5.9%**	**28.5%**	**34.4%**	**16.5%**	**0.0%**	**0.0%**	**100%**
FY07 UTIMCO Services Fee Allocation:	**6,445,522**	**835,883**	**3,874,828**		**2,784,405**			**13,940,638**
UTIMCO Services Budgeted FY08	**7,541,715**	**905,220**	**4,380,276**		**2,542,618**			**15,369,829**
Direct Expenses of the Funds Budgeted FY08								
External Management Fees -- Base	9,714,335	0	0	5,251,265	4,023,626	N/A		18,989,226
External Management Fees - Performance Based	12,836,901	0	0	6,813,407	4,075,704			23,726,012
Other Direct Costs	3,186,661	29,705	190,055	2,061,907	1,042,247	0	0	6,510,576
Total Direct Expenses of the Funds	25,737,897	29,705	190,055	14,126,580	9,141,576		0	49,225,813
TOTAL	**33,279,612**	**934,925**	**4,570,331**	**14,126,580**	**11,684,194**	N/A	**0**	**64,595,642**
Percent of Total Direct Expenses of the Funds	**51.5%**	**1.4%**	**7.1%**	**21.9%**	**18.1%**	**0.0%**	**0.0%**	**100.0%**
Budgeted Expense Percent of 2/28/07 Market Value (3)								
UTIMCO Services Percent of 2/28/07 Market Value (3)	**0.068%**	**0.086%**	**0.088%**	**0.000%**	**0.072%**	0%	0%	**0.070%**
Direct Expenses Percent of 2/28/07 Market Value	0.233%	0.003%	0.004%	0.236%	0.260%	0%	0%	0.223%
SUBTOTAL Percent of 2/28/07 Market Value	**0.301%**	**0.089%**	**0.092%**	**0.236%**	**0.332%**	0%	0%	**0.293%**
TOTAL Budgeted Costs % of 2/28/07 Market Values	**0.301%**	**0.325%**	**0.328%**		**0.332%**	**0%**	**0%**	**0.293%**

(1) Money Market Fund Income is net of fees and direct expenses.
(2) Pooled Fund for the collective investment of the PHF and LTF.
(3) Total UTIMCO Services fee of 0.070% compares to 0.072% of $19.4 billion mid-year FY06 AUM; PHF and LTF include GEF expenses.

EXHIBIT A

UTIMCO Operating Expenses/Budgets FY07-FY08

	8/31/2007			Change from 2007 Budget		8/31/2008	Change from 2007 Projected		Change from 2007 Budget
	Budget	YTD*	Projected	$	%	Budget	$	%	%
UTIMCO Services									
Salaries and Wages + Vacation	5,909,955	3,514,309	4,985,344	(924,611)	-15.6%	6,011,318	1,025,974	20.6%	1.7%
Bonus Compensation + Interest	2,870,989	1,144,971	1,791,678	(1,079,311)	-37.6%	3,258,381	1,466,703	81.9%	13.5%
Total Compensation	8,780,944	4,659,279	6,777,021	(2,003,923)	-22.8%	9,269,699	2,492,678	36.8%	5.6%
Total Payroll taxes	379,878	199,070	305,035	(74,843)	-19.7%	418,017	112,982	37.0%	10.0%
403(b) Contributions	426,313	226,893	334,992	(91,321)	-21.4%	461,748	126,755	37.8%	8.3%
Group Health, Dental, AD&D, Life, LTD	608,535	284,105	419,299	(189,236)	-31.1%	715,326	296,027	70.6%	17.5%
Employee Benefits	1,034,848	510,997	754,291	(280,557)	-27.1%	1,177,073	422,782	56.1%	13.7%
On-Line Data & Contract Services	879,861	555,916	830,521	(49,340)	-5.6%	881,304	50,783	6.1%	0.2%
Recruiting and Relocation Expenses	323,500	308,031	529,041	205,541	63.5%	440,004	(89,037)	-16.8%	36.0%
Travel	349,320	118,504	197,152	(152,168)	-43.6%	396,070	198,918	100.9%	13.4%
Phone Equipment and Charges	32,250	29,894	44,819	12,569	39.0%	48,600	3,781	8.4%	50.7%
Computer & Office Supplies	85,325	49,224	73,804	(11,521)	-13.5%	128,472	54,668	74.1%	50.6%
Employee Education	51,175	10,647	17,647	(33,528)	-65.5%	35,200	17,553	99.5%	-31.2%
Repairs/Maintenance	82,950	69,905	104,985	22,035	26.6%	114,000	9,015	8.6%	37.4%
BOD Meetings	37,500	36,064	50,064	12,564	33.5%	57,000	6,936	13.9%	52.0%
Other Operating Expenses	49,053	41,014	54,810	5,757	11.7%	60,440	5,630	10.3%	23.2%
Total General Operating	1,890,934	1,219,199	1,902,843	11,909	0.6%	2,161,090	258,247	13.6%	14.3%
Total Lease Expense	809,739	494,746	788,193	(21,546)	-2.7%	943,042	154,848	19.6%	16.5%
Invest., Hiring & Board Consultants	18,850	10,124	15,124	(3,726)	-19.8%	30,000	14,876	98.4%	59.2%
Legal Expenses	295,000	449,884	589,884	294,884	100.0%	360,000	(229,884)	-39.0%	22.0%
Compensation Consultant	12,500	13,100	13,100	600	4.8%	120,000	106,900	816.0%	860.0%
Accounting fees	45,000	38,240	48,240	3,240	7.2%	31,500	(16,740)	-34.7%	-30.0%
Total Professional Fees	371,350	511,347	666,347	294,997	79.4%	541,500	(124,847)	-18.7%	45.8%
Property/Liability Package	15,750	12,699	18,685	2,935	18.6%	18,407	(278)	-1.5%	16.9%
Umbrella Policy	5,950	3,667	5,500	(450)	-7.6%	5,637	137	2.5%	-5.3%
Workers Compensation	12,250	13,369	18,808	6,558	53.5%	16,725	(2,083)	-11.1%	36.5%
Business Auto	775	515	779	4	0.5%	810	31	4.0%	4.5%
Commercial Bonding Policy	45,000	27,267	40,900	(4,100)	-9.1%	41,922	1,022	2.5%	-6.8%
Prof., D&O & Emp. Practices Liability	182,500	109,533	164,300	(18,200)	-10.0%	168,408	4,108	2.5%	-7.7%
Total Insurance	262,225	167,049	248,971	(13,254)	-5.1%	251,909	2,938	1.2%	-3.9%
Depreciation of Equipment	410,720	376,325	564,487	153,767	37.4%	607,500	43,013	7.6%	47.9%
Total UTIMCO Services	13,940,638	8,138,013	12,007,190	(1,933,448)	-13.9%	15,369,830	3,362,640	28.0%	10.3%
Direct Costs to Funds									
External Management Fees	16,847,098	12,122,601	16,814,781	(32,318)	-0.2%	18,989,226	2,174,445	12.9%	12.7%
External Mgt. Fees-Performance Fees	20,585,849	8,365,012	13,511,475	(7,074,374)	-34.4%	23,726,012	10,214,537	75.6%	15.3%
External Management Fees	37,432,947	20,487,614	30,326,255	(7,106,692)	-19.0%	42,715,238	12,388,983	40.9%	14.1%
Custodian Fees and Other Direct Costs	1,260,072	1,112,366	1,481,423	221,351	17.6%	1,536,375	54,953	3.7%	21.9%
Performance Measurement	530,599	314,152	418,869	(111,730)	-21.1%	536,700	117,830	28.1%	1.1%
Analytical Tools	386,700	275,423	374,990	(11,710)	-3.0%	400,000	25,010	6.7%	3.4%
Risk Measurement	850,000	500,667	639,667	(210,333)	-24.7%	593,500	(46,167)	-7.2%	-30.2%
Custodian and Analytical Costs	3,027,371	2,202,607	2,914,949	(112,423)	-3.7%	3,066,575	151,626	5.2%	1.3%
Consultant Fees	1,356,000	913,029	1,235,227	(120,773)	-8.9%	1,325,000	89,773	7.3%	-2.3%
Auditing	205,000	155,000	211,500	6,500	3.2%	754,000	542,500	256.5%	267.8%
Controls Assessment (Sarbanes-Oxley)	124,000	124,000	124,000	0	0.0%	0	(124,000)	-100.0%	-100.0%
Printing	182,250	178,155	178,155	(4,095)	-2.2%	195,000	16,845	9.5%	7.0%
Legal Fees	985,000	563,296	809,546	(175,454)	-17.8%	1,100,000	290,454	35.9%	11.7%
Background Searches & Other	106,700	20,662	42,108	(64,592)	-60.5%	70,000	27,892	66.2%	-34.4%
Other Direct Costs Total	2,958,950	1,954,142	2,600,536	(358,414)	-12.1%	3,444,000	843,464	32.4%	16.4%
Total Direct Costs to Funds	43,419,269	24,644,363	35,841,739	(7,577,529)	-17.5%	49,225,813	13,384,073	37.3%	13.4%
Total Costs	57,359,907	32,782,376	47,848,929	(9,510,978)	-16.6%	64,595,642	16,746,713	35.0%	12.6%

**Actual UTIMCO Services expenses as of April 30, 2007 and Direct Costs to Funds expenses as of May 31, 2007.*

EXHIBIT B

UTIMCO Operating Expenses/Budgets FY03-FY08

	8/31/2003	8/31/2004	8/31/2005	8/31/2006	8/31/2007	8/31/2008
	Actual	Actual	Actual	Actual	Projected	Budget
UTIMCO Services						
Salaries and Wages + Vacation	3,102,883	3,773,961	4,203,100	4,492,078	4,985,344	6,011,318
Bonus Compensation + Interest	1,089,333	1,858,653	2,094,447	2,164,963	1,791,678	3,258,381
Total Compensation	4,192,216	5,632,614	6,297,547	6,657,040	6,777,021	9,269,699
Total Payroll taxes	195,076	206,777	313,637	312,023	305,035	418,017
403(b) Contributions	219,898	280,400	304,359	327,724	334,992	461,748
Group Health, Dental, AD&D, Life, LTD	201,090	259,932	315,457	406,756	419,299	715,326
Employee Benefits	420,988	540,332	619,816	734,480	754,291	1,177,073
On-Line Data & Contract Services	417,995	598,504	677,346	811,883	830,521	881,304
Recruiting and Relocation Expenses	359,917	2,513	35,600	216,927	529,041	440,004
Travel	109,138	138,855	170,069	205,965	197,152	396,070
Phone Equipment and Charges	41,990	45,660	39,340	46,965	44,819	48,600
Computer & Office Supplies	73,887	58,934	68,431	143,372	73,804	128,472
Employee Education	14,424	20,244	21,814	13,728	17,647	35,200
Repairs/Maintenance	39,453	45,576	56,434	85,412	104,985	114,000
BOD Meetings	29,811	17,541	27,552	52,375	50,064	57,000
Other Operating Expenses	30,044	62,066	52,306	106,401	54,810	60,440
Total General Operating	1,116,659	989,893	1,148,892	1,683,029	1,902,843	2,161,090
Total Lease Expense	606,013	599,047	600,593	655,286	788,193	943,042
Invest., Hiring & Board Consultants	2,000	0	17,500	20,175	15,124	30,000
Legal Expenses	500,823	183,102	579,720	362,045	589,884	360,000
Compensation Consultant	45,200	108,397	33,650	95,920	13,100	120,000
Accounting fees	6,870	12,910	30,135	54,106	48,240	31,500
Total Professional Fees	554,893	304,409	661,005	532,246	666,347	541,500
Property/Liability Package	15,009	16,657	28,797	22,993	18,685	18,407
Umbrella Policy	6,756	7,521	6,720	5,500	5,500	5,637
Workers Compensation	14,109	18,227	17,419	13,109	18,808	16,725
Business Auto	175	186	469	756	779	810
Commercial Bonding Policy	39,138	42,879	28,849	27,752	40,900	41,922
Prof., D&O & Emp. Practices Liability	158,881	173,208	171,959	150,525	164,300	168,408
Total Insurance	234,068	258,678	254,213	220,634	248,971	251,909
Depreciation of Equipment	286,176	261,894	272,836	504,637	564,487	607,500
Total UTIMCO Services	7,606,089	8,793,644	10,168,539	11,299,376	12,007,190	15,369,830
Direct Costs to Funds						
External Management Fees	10,699,801	12,715,126	14,217,736	17,815,353	16,814,781	18,989,226
External Mgt. Fees-Performance Fees	4,467,459	9,165,879	14,898,389	29,648,938	13,511,475	23,726,012
External Management Fees	12,314,265	21,881,005	29,116,125	47,464,291	30,326,255	42,715,238
Custodian Fees and Other Direct Costs	1,351,899	1,043,993	1,506,759	1,634,942	1,481,423	1,536,375
Performance Measurement	261,625	463,238	487,976	484,660	418,869	536,700
Analytical Tools		218,172	284,050	338,630	374,990	400,000
Risk Measurement	335,172	120,000	267,500	276,000	639,667	593,500
Custodian and Analytical Costs	1,948,696	1,845,403	2,546,285	2,734,232	2,914,949	3,066,575
Consultant Fees	1,477,800	900,000	900,000	852,000	1,235,227	1,325,000
Auditing	168,202	205,000	158,309	177,944	211,500	754,000
Controls Assessment (Sarbanes-Oxley)			0	97,110	124,000	0
Printing	99,583	111,431	132,196	163,790	178,155	195,000
Legal Fees	343,849	517,868	932,525	761,764	809,546	1,100,000
Background Searches & Other	30,653	45,534	50,805	59,147	42,108	70,000
Other Direct Costs Total	2,120,087	1,779,833	2,173,835	2,111,755	2,600,536	3,444,000
Total Direct Costs to Funds	16,048,173	25,506,242	33,836,245	52,310,278	35,841,739	49,225,813
Total Costs	23,654,262	34,299,886	44,004,784	63,609,654	47,848,929	64,595,642

EXHIBIT C

UTIMCO Services Capital Expenditures Budget FY08

		FY08 Proposed		FY07 Budget
Ongoing:				
Computer Server Replacements and Related Software Licenses	$	30,000	$	75,000
Staff Computer and Monitor Replacements		80,000		31,000
Penetration Monitoring Equipment and Software		27,000		
Software License Upgrades, Additions		20,000		10,000
Computer Related Equipment		6,000		-
Security Enhancements		6,000		-
Phones and Related Equipment		-		6,000
	$	**169,000**		**122,000**
Allowance for Office Artwork and Framing		5,000		15,000
Office Equipment		5,000		-
Additional Furniture Purchases		10,000		30,000
Leasehold Improvements		5,000		-
	$	**25,000**	**$**	**45,000**
Expansion :				
Phones and Related Equipment	$	8,000	$	-
Office Equipment		38,970		-
Computer Related Equipment		25,000		-
Furniture & Fixtures		89,599		-
Leasehold Improvements		173,415		-
Allowance for buildout		(173,415)		-
	$	**161,569**	**$**	**-**
Total Capital Expenditures	**$**	**355,569**	**$**	**167,000**

EXHIBIT D

UTIMCO Reserves Analysis at August 31, 2007

Cash Reserves at 4-30-2007		
Cash		6,468,831
Investments		0
Prepaids Expenses		395,990
Less: Accounts Payable		(2,141,430)
Deferred Rent		0
Additional Projected Surplus thru August 31, 2007		350,000
Expected Cash Reserves at August 31, 2007		**$ 5,073,391**
2008 Proposed Operating Budget	15,369,830	
Applicable Percentage	25%	3,842,457
2008 Proposed Capital Expenditures	355,569	355,569
Required Cash Reserves		**$ 4,198,026**
Reserves Available for Distribution		**$ 875,365**
Recommended Distribution for FY08		**$ 0**