Meeting No. 974

THE MINUTES OF THE BOARD OF REGENTS

OF

THE UNIVERSITY OF TEXAS SYSTEM

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December 19, 2003

Austin, Texas

MEETING NO. 974

FRIDAY, DECEMBER 19, 2003.--The members of the Board of Regents of The University of Texas System convened this special called meeting via telephone conference call at 12:46 p.m. on Friday, December 19, 2003, on the Ninth Floor, Ashbel Smith Hall, 201 West Seventh Street, Austin, Texas, with the following in attendance:

ATTENDANCE.--

Present	Absent
Chairman Miller, presiding	
Vice-Chairman Clements	
Vice-Chairman Hunt	
Regent Barnhill	
Regent Caven	
Regent Craven	
Regent Estrada	
Regent Huffines	
Regent Krier	

Counsel and Secretary Frederick

(Regent Huffines joined the meeting for discussion of Item 3.)

WELCOME TO REGENT JOHN W. BARNHILL, JR., AND EXECUTIVE VICE CHANCELLOR SHINE.--Chairman Miller welcomed Regent John W. Barnhill, Jr., to his first meeting of the Board. Mr. Miller also welcomed Kenneth I. Shine, M.D., Executive Vice Chancellor for Health Affairs.

[On November 19, 2003, Governor Rick Perry named Mr. John W. Barnhill, Jr., to the Board of Regents of The University of Texas System for a term to expire February 1, 2009. Regent Barnhill replaces Mr. A. W. "Dub" Riter, Jr., who died in office on September 23, 2003. Mr. Barnhill took the oath of office on November 24, 2003.]

In accordance with a notice being duly posted with the Secretary of State and there being a quorum present, Chairman Miller called the meeting to order.

1. U. T. Board of Regents: Appointment of Regent John W. Barnhill, Jr., to the Board of Trustees of the Texas Growth Fund

In accordance with the requirements of the Regents' Rules and Regulations, Part One, Chapter I, Section 7, Regent John W. Barnhill, Jr., was appointed to the Board of Trustees of the Texas Growth Fund, effective immediately.

Regent Barnhill replaces former Vice-Chairman A. W. "Dub" Riter, Jr., as the U. T. Board of Regents' representative on the Texas Growth Fund Board of Trustees.

2. U. T. Board of Regents: Approval of appointment of members to the Audit and Ethics Committee of The University of Texas Investment Management Company (UTIMCO)

Pursuant to Texas Education Code Section 66.08 and upon recommendation of the Board of Directors of The University of Texas Investment Management Company (UTIMCO), the U. T. Board of Regents approved the appointment of Mr. I. Craig Hester, Mr. James R. Huffines, and Mr. R. H. (Steve) Stevens, Jr., (Chair) to the Audit and Ethics Committee of the UTIMCO Board of Directors.

3. U. T. Board of Regents: Amendment to the Permanent University Fund, General Endowment Fund, Permanent Health Fund, and Long Term Fund Investment Policy Statements (including asset allocation policy); amendment of Liquidity Policy; and approval of Resolution

Upon recommendation of the Board of Directors of The University of Texas Investment Management Company (UTIMCO) and following discussion reported on the following pages, a majority of the U. T. Board of Regents approved amendments to the following Investment Policy Statements and Liquidity Policy as set forth on the referenced pages:

a. Permanent University Fund (PUF) (Pages 18 - 30)

b. General Endowment Fund (GEF) (Pages 31 - 41)

c. Permanent Health Fund (PHF) (Pages 42 - 49)

d. Long Term Fund (LTF) (Pages 50 - 57)

e. Liquidity Policy (Pages 58 - 60)

These amendments include revisions to Policy Targets, Ranges, and Performance Objectives for the asset categories identified (Exhibit A of the PUF and GEF Investment Policy Statements and Exhibit B for the PHF and LTF Investment Policy Statements).

The amendments to the PUF, GEF, PHF, and LTF Investment Policy Statements clarify provisions and definitions related to asset allocation and asset allocation policy and follow an in-depth review of asset allocation, including risk framework, decision factors, and return and risk assumptions for the PUF and the GEF by the UTIMCO Board and UTIMCO staff.

The Liquidity Policy defines liquidity categories and sets asset weight limits for each category in order to control the aggregate amount of liquidity risk that can be assumed in the endowment portfolios. Amendment to the Liquidity Policy changes the liquidity risk measurement from four categories to two, liquid and illiquid, and revises the definitions for the liquid and illiquid categories.

A transcription of the discussion of this item follows:

Transcript of Discussion of Item 3
Special Called Board Meeting
December 19, 2003

Chairman Miller: The last item I'd like to discuss is item three, which relates to the investment policies, including asset allocation targets and ranges, liquidity policy and the additional resolution that I've delivered to the Board this week.

Ms. Frederick: Mr. Huffines is with us.

Chairman Miller: Thank you. Welcome, James.

Regent Huffines: Good afternoon.

Chairman Miller: Good afternoon. We've covered all items except item three, which I took out of order and I did that partially because I sent out some material and revised the agenda very late and I think it deserves a fair amount of discussion. There are two parts to that, I believe. One is the investment policies, including asset allocation targets and ranges, and then a resolution that I put out for the Board to consider.

If there are no objections I would like to be able to put out two things for a possible motion and a second and then have a discussion. I'd like to recognize just that motion and second, have the discussion, and then recognize anybody after that for either amendment or other motion. It's hard to do that with the telephone and I'd like to be able to weigh in with some comments myself if there are no objections to doing it that way. I'm going to be sure to give everybody access properly to whatever comments anybody needs to make.

Going forward, on the investment policy is there a motion to be made concerning that?

VC Hunt: Mr. Chairman, this is Woody. I don't have one in front of me here, but I would recommend that we proceed with the recommended asset allocation and the changes to the investment policies that would reflect that.

Chairman Miller: Could I suggest a change or at least an amendment to that policy to get it on there and you can say yes or no to accept it?

VC Hunt: Okay.

Chairman Miller: There's a range in two parts of the investment policy that I feel, I'm speaking for me personally, on commodities and fixed income policy. I would like to see a range on commodities of zero percent to 5% instead of zero percent to 10% and a range on fixed income to have a minimum of 15% instead of 10%. I think it's prudent. We've had a chance to discuss some of that. I think it's sound policy and it doesn't change the long-term potential in any significant way, but I believe it's more prudent.

VC Clements: Chairman Miller, would you repeat that? Under commodities, you would recommend what?

Chairman Miller: A zero percent to 5% range.

VC Clements: Zero to 5%. And what about fixed income?

Chairman Miller: Fifteen percent to whatever the high number is. I think it's 30% or more.

VC Hunt: It's 30%. It is 30%.

Chairman Miller: The low number, the lowest, is 10% and I personally think that's too low a number. I've looked at the ranges of what other major institutions do and I just think today there's no proposal and a target to do either of those low or high numbers, so I think it fits the target allocation and I think it's better target policy.

Woody?

VC Hunt: I would have no objection to, on the commodities, reducing it from 10% to 5%. We currently, I believe, have only about one percent invested in commodities against our target portfolio of 3%.

I would say on the fixed income that there was a lot of discussion of that at the UTIMCO Board meeting where we set these. Our independent, active, outside money managers, of which we have four, were those that argued in favor toward a lower fixed income allocation based on their expectations of the investment marketplace over the next 12 to 24 months. I just lay that out, I guess, as a background that we did not come to this range or to the 15% target without considerable discussion at the UTIMCO Board meeting. I welcome comments from Rita or James or Scott, all of whom participated in the asset allocation process that began late spring/early summer and concluded with our December 4th approval of this recommended asset allocation policy.

Regent Caven: I would concur with Regent Hunt. I believe that you will have no objection, or at least not from me, from the reduction in the range of the commodities. On the other hand, I certainly recognize exactly what Regent Hunt has said. There was an enormous amount of discussion, particularly from the professional investors. We are at a 45-year low in interest rates. The return on fixed income is dismal at this point in time. That's not to say that from a portfolio-balancing point of view we certainly follow the steps...the tactical ability at periods of very low interest rates, when every indication is that the next step is going to be up rather than down, is to have a little bit more flexibility on the down side while leaving the target currently at 15%.

VC Clements: I would agree with both Woody and Scott on this.

Chairman Miller: I take that as a second too, so we have the discussion now. It's been moved and seconded. Any other comments? I'm going to just, with no objection, make my own comments before our vote.

I think the range is too low a number, 10%. I don't think traditionally investment funds, these kinds or others, do that low a fixed income allocation. It's not an issue about outlook; it's an issue about diversification. The current target of 15% I'd have no objection to, but personally I'm going to vote against the 10% low allocation of fixed income. I don't consider it prudent to have that low of an allocation in a balanced or an endowment fund with our goals.

Any other comments? All in favor say, "Aye."

Regent Huffines: Wait. I'm not sure what we're voting on.

Ms. Frederick: Mr. Chairman, if I might restate it, I believe the motion in front of the group is to accept the UTIMCO recommendation with the modification accepted by Mr. Hunt to agree to the change in the range on commodities.

Chairman Miller: But not on fixed income.

Ms. Frederick: Correct.

Chairman Miller: Any other comments?

VC Hunt: Chairman Miller, as far as the vote, are we going to do a roll call since we might have a difference of opinion here or how are you going to handle it?

Chairman Miller: I think if I can tell by voice vote it's approved or disapproved I would do that, but thank you for offering that. If there's a close call or people want to go on record I could always have a roll call vote.

VC Hunt: Okay.

Chairman Miller: I was going to tell the Board I didn't want to surprise people at the end and this is hard to do with a telephonic meeting and I appreciate your flexibility. I just want to be sure that people understand that if we have that low of a range on fixed income I'm going to just vote against it. It doesn't matter about the roll call. If we have a close call or it can't be told I'll take a roll call. Is that okay with everybody?

VC Hunt: That's fine.

Chairman Miller: All in favor say, "Aye."

Participants: Aye.

Chairman Miller: Opposed?

Regent Krier: Nay.

Chairman Miller: Pardon me?

Regent Krier: Nay.

[Note: Later in the meeting, Regent Estrada noted that he voted "nay". See Page 10 .]

Chairman Miller: The next item on the agenda has to do with the resolution I sent out and I know it's late to do that. I would like to ask for a motion to deal with that resolution and a second and then have a discussion for everybody to have a chance to weigh in. If there are no objections I can make an introductory statement about why I put the resolution on the table or I can wait until later, but I think it might help before a motion is made for me to do that.

The University of Texas System has been extensively engaged in an ongoing examination and updating of a broad array of its oversight in governance functions over the past two years, including update or revision of the Regents' Rules, creation of the new Audit, Compliance, and Management Review Committee of the Board of Regents; implementing a System-wide policy of conducting a management audit upon change of senior management at all U. T. System institutions; development of a policy of providing System assistant management audit teams to institutions facing extraordinary circumstances; development and voluntary adoption of a public institution version of the Sarbanes-Oxley oversight process; creation of a performance review process for evaluation of institution and leadership performance, that's the system installed by the Chancellor; the creation of a higher education accountability system; and an extensive review of the structure and governance of internal foundations or related organizations. We're still doing that and that's the study of all of the types of foundations like we recently did the Hogg Foundation and other related organizations. A thorough review and evaluation of the individual institutions' development boards and similar entities; for example, a board of visitors at a health institution. We're looking at things like the bylaws and the legal structure and so on. Then, of course, the reorganization of The University of Texas System staff and its financial structure that's been ongoing in the last year. And finally, to make a connection in the Baker Botts outside legal review report on UTIMCO's fiduciary relationship with The University of Texas System Board of Regents and all of the accounts and portfolios that we're responsible for.

I consider this resolution proposed. It's not before the Board officially yet. It represents just another step in an ongoing review of one of the Board's most important responsibilities of governance. The Board's fiduciary responsibility, including oversight of the Permanent University Fund, endowments and gifts, and other public funds that have been entrusted to us by the State of Texas and our many benefactors is perhaps one of the most significant obligations of the Board. I have a couple of other comments and a statement, so that's the reason for doing it and the timeliness of it is clear in the sense of the broad issues of governance in the land. Virtually every day we see some things about that and so this is a tier on the prudent step and I'd like to call on Regent Huffines with a possible motion.

Regent Huffines: Mr. Chairman, do we need a motion before we have discussion? I'm not real clear on it.

Chairman Miller: It's not necessary if the Board agrees. With no objections I don't mind having a discussion about it.

Francie, that's not improper, is it?

Ms. Frederick: No, sir, with the consent of the Board. If anyone objects we'd have to regroup.

Regent Huffines: I do have a motion after discussion though.

Chairman Miller: Why don't we do that? We could either start with you or ask the people to go around. I'd like to be sure that everybody knows about the resolution that I've put out there. Why don't we do that? Let's start a discussion.

Regent Huffines: That'd be fine. If I may start then, Mr. Chairman? There's been a lot of discussion on this over the last few months and I have said publicly and privately that I do think we need to do an ongoing review of governance issues on everything that we're looking at and UTIMCO would fall into that category.

I know there have been various drafts of the resolution that you refer to circulated and I'm prepared and I support a review of the governance issues that you outlined and I support those specific items mentioned in the resolution. I have, I guess it would be a revised resolution somewhat (different) from the one that was circulated possibly a few days ago. I can either put that on the table now or wait until after discussion, Mr. Chairman. I'll just follow …

Chairman Miller: I think, since you mentioned it, put it on the table and let's have a discussion. Then there will be two versions of a resolution and we can all talk about any or all of it.

Regent Huffines: Okay. I'd be happy to. I'd like to read the resolution. Some of you may have it in front of you; some of you may not. It says, "Whereas, The University of Texas System has been extensively engaged in the review of its organizational oversight and responsibility functions for the purpose of improving governance structures in the course of the Board's ongoing accountability activities, and whereas, The University of Texas Investment Management Company was formed in 1995 and has operated under contract with the Board of Regents since 1996 through multiple market cycles and several changes in the management team. Therefore, be it resolved that over the next several months the U. T. Board of Regents will examine and evaluate The University of Texas Investment Management Company as to structure and services, including the following: investment services; administrative services; cost effectiveness; policy-setting procedures; consulting services; legal services; budgeting procedures; oversight and reporting functions; contract, form and legal structure; and then the other relevant structural issues with the goal of defining and structurally improving the investment management function of the U. T. System."

For those that may have a resolution in front of you that was previously circulated, my resolution deletes the final paragraph.

Chairman Miller: Thank you. That's very well done. Now let's see, can we just do a go-around? We can do it in alphabetical order. Does somebody want to speak up about that? We don't have a formal motion in front of us.

VC Hunt: I'd like to make the following comments. One, I am always supportive of best practices whether it's UTIMCO or any other of our components or units within the System of trying to make them work better.

But I do want, one, as the Chairman of UTIMCO and also as the Regent who has been on the UTIMCO Board the longest now, a little over four years, I'd like to make it clear, at least from my perspective, that I do not believe that this should reflect on the performance of UTIMCO or be viewed as performance related. The reasons I make that statement is, when you look at and I invite any of our Regents to talk to our outside, independent directors, I think you will get from them an opinion that in terms of staff quality, motivation, and competitiveness we are in the best shape today at UTIMCO that we've been in our seven plus year history, particularly if you talk to Luther King and Susan Byrne, who have been there that whole time. They will confirm, in their opinion, that we are at that level.

If you want to go from the qualitative evaluation and look at the quantitative and you want to look at a ten-year record and if you look at the endowments that are a billion dollars and over, our rank there is 26 out of 33. If you look at a five-year, we're 24 out of 34. If you look at a three-year, we're up to 13 out of 34. If you look at one year, we're 6 out of 34. If you look at the last quarter, we're 3 out of 34. So the trend to me is unmistakably in the right direction for us to be competitive in the management of our funds and that competitiveness, at least in my view, is very important because it contributes to our ability to compete as an institution in the clause, whether it's academic, research, or improvement of faculty and retention of the faculty, the contribution from our investment results are very important for us in our ability to compete across the board. I think that record in a quantitative sense, although one-quarter, as we all know, doesn't make a record, I think the trend from ten years ago to five to three to one to the last quarter should be reassuring to all of the Board members and their fiduciary responsibilities as far as managing our funds, that we are moving in the right direction. We are doing something right.

But I do not disagree and I am supportive of the resolution, although I would like to add one additional modification and that is in the next to the last (sentence), where we say, "The goal is defining and structurally improving," I would like to modify (what was read by) Regent Huffines to say, "With the goal of improving," and drop out the words "defining and structurally".

Those would be my comments.

Chairman Miller: Well, thank you. That's well said. I thought the timing with you and me coming on the Board nearly five years ago had to do with that performance improvement, especially the short-term performance with Scott and James coming on, but I guess it might have been the UTIMCO management. Thank you.

Other comments, please?

Regent Krier: I have a question.

Chairman Miller: Please.

Regent Krier: Regent Huffines?

Ms. Frederick: Regent Huffines is momentarily out of the room. He'll be right back.

Chairman Miller: We'll wait a second.

Regent Estrada: Francie?

Ms. Frederick: Yes, sir?

Regent Estrada: This is Bob Estrada and I apologize. I didn't realize my phone was still on mute when we voted earlier, the voice vote on the investment policy. It was my intent to be added to the nays on that.

Ms. Frederick: Yes, sir. We will so record that.

Mr. Huffines, Regent Krier had a question for you.

Regent Huffines: Yes, Regent Krier?

Regent Krier: With respect to your amended resolution is it your intent that if we omitted the last paragraph of the draft resolution that UTIMCO could go forward and change its current compensation plan before the review is undertaken? Because that's my concern.

Regent Huffines: No, ma'am. A very good point. It's not my intent. In fact, if this resolution passed I had some prepared, on-the-record comments that I was going to make about that and I'll just say it right now, that I personally would like to go on the record and recommend that we have no changes in the compensation or performance bonus program during Fiscal Year 2004. That's my personal observation; it's my personal comment, but I'd like to go on the record and see that that is in the Minutes.

VC Hunt: I would like to add to that if I could and essentially repeat a statement I made at the last UTIMCO Board meeting and that is that there should be full recognition at the UTIMCO level that the U. T. Board of Regents has a fiduciary responsibility that includes a review of the compensation, that they are the ultimate defender, if you might call it that, of any compensation plan that's installed at UTIMCO and they have to be fully knowledgeable and comfortable with that plan. So you also have my commitment that nothing will move forward as far as implementation without review, comfort, understanding, and approval at the U. T. Board of Regents' level.

Chairman Miller: Thank you, Regent Hunt.

Chancellor Yudof: Mr. Chairman, it's Mark Yudof. I just wanted to associate myself with Regent Hunt's remarks. I think it is important to look at those issues and to delay implementation of any compensation plan until there's been a thorough airing of the issue by the Board of Regents. I'm assuming in all of this that UTIMCO will continue to do the job that it's doing, but that until the review is finished in critical policy areas there won't be major renovations. Maybe I'm wrong in that, but that's the way I read it; maybe the underlying intent of Regent Huffines and, Regent Huffines, correct me if I'm wrong.

Regent Huffines: That's correct, Chancellor. You stated it very well.

VC Hunt: I would add one more thing. I think there's a clear understanding at the UTIMCO Board level that if we are going to hold our staff accountable for competitive returns, that we also need to be competitive in our compensation program and we are investing considerable Board and consultant time in trying to devise the best possible incentive compensation plan, which once the UTIMCO Board has acted upon that, as I said earlier, would be rendered to the U. T. Board for their approval.

I don't want to underestimate or to state that because we're delaying it it's not important. I do think time is of the essence to work our way through that, but the Board of Regents ultimately has to feel comfortable with whatever is done there and they will set the final timeline for implementation approval.

Regent Huffines: Regent Hunt, my feeling and the reason I made that statement is we're four to five months, almost six months into the fiscal year and with this review going on I just thought it would probably be better that we work on some type of plan that would be in effect for the end of this fiscal year.

VC Hunt: Right. I understand.

Chairman Miller: Any other comments?

Regent Barnhill: This is John Barnhill. I need to ask what part of this last paragraph are people objecting to? I'm not too sure I understand since there is some thought that the current compensation plan would just stay in force; at least that's what James said, I think.

Chairman Miller: I don't know either, John.

Regent Huffines: I think you could, John, read into this that when you say, "Take no significant action involving the UTIMCO budget, including revision of the current compensation plan," which we've already talked about, but reviewing the budget could be a broader term and, "Hiring or renewal of contracts involving legal counsel or consultants," and of course we have from time to time a number of consultants doing various items. I think it could be implied or you could read this in a sense that the UTIMCO Board is, in a sense, on notice not to do anything different and then you'd be getting into defining what have they been doing that they shouldn't be doing going forward. I think that would be my concern, that this is perhaps too broad.

Chairman Miller: Let me answer it then. Nobody else has had a comment about it. I do have a concern about certain of those costs, serious concerns. They are one of the reasons for the resolution. I think we do have to define the role of UTIMCO. I don't think it is defined. There are some various assumptions, but it wasn't defined originally. It's clear that in some of the operations in the last year, regardless of the current performance, that we've had difficulties in defining that and there have been problems because of it. I could go through a list of them. I don't think we need to, but it has to do with investment policy, disclosure, the costs particularly. So I think that was put there because of concern. My concern and others' was a significant amount of compensation, a significant amount of lawyers' fees and consulting fees, millions of dollars over multiple years, and investment expenditures and compensation consultants and their role and, I think, administrative costs, which are significantly higher than the average for fiduciary accounts, maybe twice and, in spite of asking questions about it, haven't received those answers.

So, yes, there are concerns with the role, with costs, disclosure, investment policy and recently, compensation issues. I think the oversight at the U. T. System is inadequate and we know that. We've worked on it. So we do need to resolve some of these things. That's the reason for the study. It doesn't mean they can't be done and it isn't a reflection particularly on anybody or anything, but the fact is I think there are some refinements that need to be made. I think the language pretty clearly does that. So my answer would be that that paragraph would have actually sent that message; there are limits to what should be spent for some of these purposes and I think that is something that's valuable to do.

I'm okay with a resolution without it just for the record, but I do think the resolution should include, I feel very strongly, the definition of the role of UTIMCO. It would be hard to say, after going through what we've done in the last four and a half years, that that's well defined and that there's an agreement about it. I think we do need to do that. I've asked the Attorney General for permission and he's granted it to retain Baker Botts again to help us go through some of those legal questions and I think a sound review of that would help define the role. It is one of the things we need to do as prudent fiduciaries. If we don't I think regardless of the performance in some ways it still could be unsound and it doesn't guarantee future performance. We just have to look back six months or a year and say that maybe it's improved, but that period of time might not have been very good. If we go through one more year and it's a bad year, I wouldn't want that to reach a conclusion that we've done it either right or wrong by itself because it might just be an accident. I'd like to have this sound structure in place and also get good performance. That's the purpose of the resolution.

Regent Huffines: Mr. Chairman, for clarification purposes, it's my understanding that after the review is done and all of the information is assimilated that it will come to the U. T. Board and then at that point in time all of the Board of Regents will have an opportunity to vote and help define the appropriate relationship with UTIMCO.

Chairman Miller: Yes. Well, informally what I'd say is the plan would be to have the attorneys at Baker Botts look particularly at legal and fiduciary types of structures, how we're doing it and what could be improved. They had some things in their previous report, which we addressed, although there were some other things that don't seem to have been resolved. For example, the level of independence of UTIMCO. In the previous report it said it was a captive entity and there are other things in the structure, which don't define that very well and what the role is. It should be defined more clearly. That would be one of the questions.

Obviously, everybody on the Board would have a chance to vote to address that and talk to the counsel in the right kind of legal structure and that this would be a committee of the whole … function, so we would have an open, fulsome discussion and debate about it in the next, say, two to three months. I would anticipate including other types of consultants. I've had one conversation with a senior faculty member that has an investment management skill and background. It wouldn't be unlikely to have others. I'm not looking to spend significant amounts of funds. We wouldn't want to, but we need some independence of that view and today we're heavily dependent on self-evaluation by UTIMCO and its advisors and that's part of what the intention of this process would be. I think it's constructed to do it.

Even if nothing had been happening and necessarily something was not wrong or anything like that, we still ought to be doing it because this was set up seven or eight years ago without much review or examination. It's obvious in retrospect that it wasn't done structurally with everything covered. The last Baker Botts report showed that and I think this is the next step to do it correctly. So I would like to see the resolution include what language it has about defining the role.

I think, unless somebody has any other comments, we're ready to see if there's a motion and a second.

Regent Huffines: I believe, Francie, Regent Hunt made an amendment to my resolution. What is on the table right now?

Chairman Miller: We don't have anything on the table. We're open for a motion. I'm asking you to make a motion and see if there's a second. There's no motion on the table.

VC Hunt: Okay. Let me just make the following comment. Maybe that will lead to a motion here for the resolution and that is the current structure, which includes four members on this phone call today, including our Chancellor, who serve on the UTIMCO Board along with a representative from A&M, so I think this Board should feel comfort that we do not need the detail that's in that last paragraph to make sure our fiduciary responsibilities and oversight function is in place while we go through the studies that are laid out here. So I would like to propose the resolution dropping the last sentence, but leaving, "defining and structural" in the next to last sentence and I'm prepared to make that motion.

Regent Huffines: Could you restate that?

VC Hunt: All right. The resolution that you read, Regent Huffines, earlier, I would delete the last sentence that says, "Be it further resolved," and that would be the only change that I would …

Regent Huffines: In other words, you're withdrawing or scratching, "defining and structural"?

VC Hunt: Yes.

VC Clements: This is Rita Clements. I agree that we ought to drop that last (paragraph) and I think this first part is a real positive step forward. I think we all agree we want to do this and we will do this … in that last sentence, that kind of is the whole intent of this resolution.

Chairman Miller: I haven't recognized anybody for a motion yet, so when I do I'll say that. Again, does anybody else want to comment on that?

Ms. Frederick: Mr. Chairman?

Chairman Miller: Yes?

Ms. Frederick: I apologize. I'm afraid in the confusion of the telephone meeting, I believe Mr. Hunt did just make a motion.

Chairman Miller: No. I haven't recognized anybody for a motion. I said that when we started this discussion. When I say it's recognized we'll make a motion. That's what I said at the start. I'm not trying to be argumentative. I just want to be careful about the process.

Any other comments about the resolution and the wording before we make a formal motion?

Chancellor Yudof: Chairman Miller, I don't have much to add. The Board will go whichever way it pleases on this. I do think we need to look at the structure of a legal representation. The consultants, leaving aside the budgetary significance, I think it's important that there sort of be a level playing field as the Board looks at some of these issues. I think there are various ways that that can be accomplished and I think we're going to have to look at them seriously.

Chairman Miller: Any other comments?

Regent Krier: I'm a little confused at the differences of opinion because I hear Regent Hunt saying, "Don't include the last paragraph." Yet I hear him trying to reassure us that the compensation plan won't be changed, that there won't be additional contracts during the time the review is occurring.

Chairman Miller: Frankly, I have the same question, although I'm trying to be agreeable. I think whatever we do we're going to do in "defining and structurally" improving it. I think that's a very critical part of this process. If we're saying we already know the definition I think we've just proved that we don't. We want to do that and I'll do it in other ways, but I can give you a list of things that indicate clearly we haven't defined that and we need some structural improvement. I listed some of the things just now.

So I feel very strongly those statements should be in the resolution. I think it would dilute the meaning of it, but in any case we're going to look into those. There's no way we can review this or do anything that a sound fiduciary would do without studying those things. We just must do that.

Regent Krier: And I thought that you had convinced Regent Hunt of that and that he was now willing to leave, "defining and structurally improving" in the resolution. Is that correct, Woody?

VC Hunt: That is correct.

Chairman Miller: Then I'll take whatever Regent Huffines would make as a motion, with or without the last paragraph as the motion, however you want to make that. I'll recognize you to make a motion.

Regent Huffines: Thank you, Mr. Chairman. Just for clarification, Regent Hunt, you are happy or content with the fact of leaving, "Defining and structurally improving the investment management function of U. T. System," in there; is that correct?

VC Hunt: That is correct.

Regent Huffines: Okay. With that said I will make a motion that we approve the resolution I read, Mr. Chairman.

Chairman Miller: Is there a second?

VC Hunt: Second.

VC Clements: Second.

Chairman Miller: Any discussion further on the motion? I'm going to reserve the right to make a comment. Anybody else?

Regent Krier: I guess then I would reraise the question I just raised of Regent Huffines. Why are we leaving out the last paragraph if we're being reassured that there won't be changes in the compensation plan or hiring of additional consultants during the pendancy of the review?

Regent Huffines: Regent Krier, I can't speak on behalf of any of the other Regents. I can say that for me and I think maybe for some others there's a general feeling that it sends the message that there is something wrong with UTIMCO and it also really ties their hands. We're going to watch very closely what they do. They have a budget. We have an agreement. I've gone on record saying that I would not like any changes to be made in compensation during this review process. I just feel it's as strong of a resolution without the last paragraph.

Chairman Miller: I guess here's what I would say. I understand that point of view and it's been moved and seconded, but I want the public record to show that I think that there have been expenditures for consultants and lawyers and other purposes that are very large and need examination and that we make the point that those expenditures are not unlimited. Those are our dollars, the Board of Regents' responsibility, and we have a fiduciary duty since they all come from the accounts of our beneficiaries and I'm not comfortable with the cost of their expenditures in the past and I wanted to have some ability for that to be sent to the UTIMCO Board. It doesn't mean that the conclusion of what I've just said is right or wrong, but it does mean there was a question about it and so it's on the record. One way or the other I think that that's fair.

The motion's been made and seconded. Any further (comment)?

Regent Barnhill: So as a result, Chairman Miller, you still feel strongly about retaining the last paragraph?

Chairman Miller: I'm okay. What I did is go on record saying the things that I think got that in there to begin with. I think the discussion has done that. I think the review will look at that. Part of the structural problem that we're dealing with, to be clear, is the Board of Regents, the Chancellor, the Chairman, even the Chairman of UTIMCO has very little direct control over what UTIMCO can do and the CEO isn't an employee and none of the other people are employees of The University of Texas System. We can't even discuss some of the things, like compensation of those employees, in an executive session or their performance because they're not the System's employees.

We have structural problems about how we can interface or deal with things when we see there is something that's not there. It's very cumbersome. We do set the contract. We're the only client. We pick the directors, but at times in the last few years the directors will pick without consultation. In times in the last few years people had opinions about what UTIMCO was or should have been and we didn't necessarily agree or, in fact, they were not necessarily correct, but the advisors hired by UTIMCO were all paid by UTIMCO and there was no oversight, no resources, no dedication of funds on the System side. It was very, very imbalanced.

It still is. So we have structural issues no matter what the performance is that we have to deal with and we need to have that on the record. That will come out in whatever discussion we have, so I'm not trying to preempt it. That is what we're trying to deal with here. We don't have almost any way, except to terminate the contract, which we have the right to do at any time, or we could take a director out, which we have the right to do, but they're very cumbersome sort of atomic-type steps where we should have some kind of oversight governance, structural things where we could deal with issues or opinions or changes or things like this without that kind of action and we don't have a structure that's allowed that.

It's very imbalanced and so the role of UTIMCO and its situation relative to the Board of Regents should be defined. The idea of that part of it was to cover the fact that we don't have a way to deal today interfacing with UTIMCO other than rely on the trust of the people and that's not enough in today's world. You need to have structural ways to do it.

VC Hunt: I'd follow that comment, so everybody clearly understands that UTIMCO was a creature of the U. T. System. We created that. We're responsible for that creation and we clearly are responsible for review, oversight. Any appropriate changes of the UTIMCO model should be adding value to our money management process, value over the cost, but we can't hold UTIMCO responsible for a structure that was created by the U. T. System. We can hold them responsible for their performance and their budgets and their expenditures, all of those expenses, by the way, are netted against the results that I mentioned earlier. So I think it's totally appropriate for us to review and to go through the process that's laid out in this resolution, but we need to remember who created the current method upon which we manage our funds. We created it and we're responsible for the review. We can't hold a director or the management of UTIMCO responsible for what we created.

Chairman Miller: I agree with all of that. In fact, the last paragraph would have just sent the message that we were concerned with the structure and the ability to deal with it, so we are going to address it. There's no blame there or bad signal that was intended, but it does point out that there is a structural issue about how to deal with it and we're doing it now.

Any other comments? Thank you all. All in favor say, "Aye."

Participants: "Aye."

Chairman Miller: I'll vote. Any opposed?   Motion carried unanimously.

A copy of the Resolution, as approved, is set out on Page 61.

THE UNIVERSITY OF TEXAS SYSTEM
PERMANENT UNIVERSITY FUND
INVESTMENT POLICY STATEMENT

Purpose

The Permanent University Fund (the "PUF") is a public endowment contributing to the support of institutions of The University of Texas System (other than The University of Texas - Pan American and The University of Texas at Brownsville) and institutions of The Texas A&M University System (other than Texas A&M University-Corpus Christi, Texas A&M International University, Texas A&M University-Kingsville, West Texas A&M University, Texas A&M University-Commerce, Texas A&M University-Texarkana, and Baylor College of Dentistry).

PUF Organization

The PUF was established in the Texas Constitution of 1876 through the appropriation of land grants previously given to The University of Texas at Austin plus one million acres. The land grants to the PUF were completed in 1883 with the contribution of an additional one million acres of land. Today, the PUF contains 2,109,190 acres of land (the "PUF Lands") located in 24 counties primarily in West Texas.

The 2.1 million acres comprising the PUF Lands produce two streams of income: a) mineral income, primarily in the form of oil and gas royalties and b) surface income, in the form of surface leases and easements. Under the Texas Constitution, mineral income, as a non-renewable source of income, remains a non-distributable part of PUF corpus, and is invested in securities. Surface income, as a renewable source of income, is distributed to the Available University Fund (the "AUF"), as received.

The Constitution prohibits the distribution and expenditure of mineral income contributed to the PUF. The Constitution also requires that all surface income and investment distributions paid to the AUF be expended for certain authorized purposes.

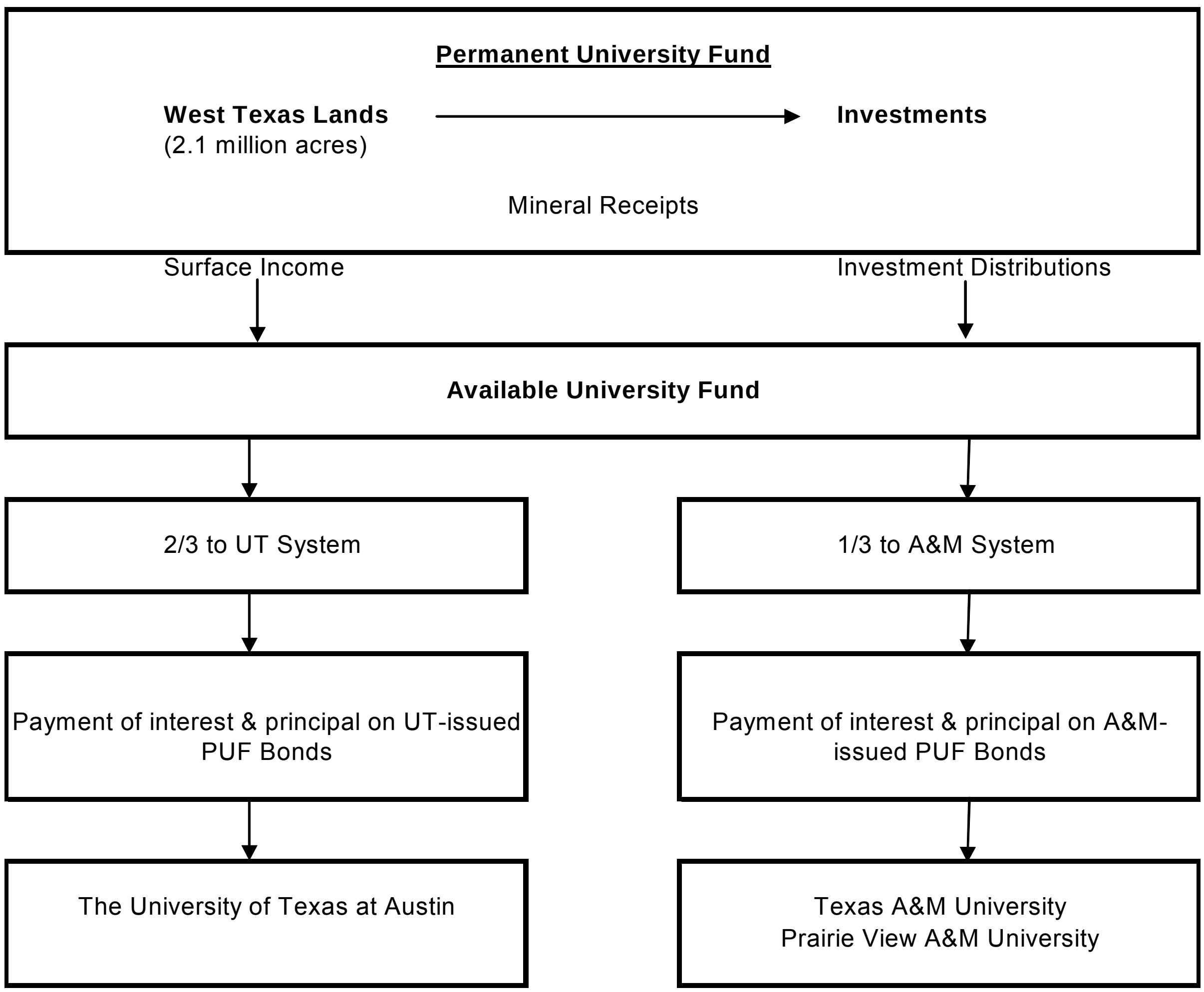
The expenditure of the AUF is subject to a prescribed order of priority:

First, following a 2/3rds and 1/3rd allocation of AUF receipts to the U. T. System and Texas A&M University System, respectively, expenditures for debt service on PUF bonds. Article VII of the Texas Constitution authorizes the Board of Regents and the Texas A&M University System Board (the "TAMUS Board") to issue bonds payable from their respective interests in AUF receipts to finance permanent improvements and to refinance outstanding PUF obligations. The Constitution limits the amount of bonds and notes secured by each System's interest in divisible PUF income to 20% and 10% of the book value of PUF investment securities, respectively. Bond resolutions adopted by both Boards also prohibit the issuance of additional PUF parity obligations unless the projected interest in AUF receipts for each System covers projected debt service at least 1.5 times.

Second, expenditures to fund a) excellence programs specifically at U. T. Austin, Texas A&M University and Prairie View A&M University and b) the administration of the university systems.

The payment of surface income and investment distributions from the PUF to the AUF and the associated expenditures is depicted below in Exhibit 1:

Exhibit 1



PUF Management

Article VII of the Texas Constitution assigns fiduciary responsibility for managing and investing the PUF to the Board of Regents. Article VII authorizes the Board of Regents, subject to procedures and restrictions it establishes, to invest the PUF in any kind of investments and in amounts it considers appropriate, provided that it adheres to the prudent investor standard. This standard provides that the Board of Regents, in making investments, may acquire, exchange sell, supervise, manage, or retain, through procedures and subject to restrictions it establishes and in amounts it considers appropriate, any kind of investment that prudent investors, exercising reasonable care, skill, and caution, would acquire or retain in light of the purposes, terms, distribution requirements, and other circumstances of the fund then prevailing, taking into consideration the investment of all the assets of the fund rather than a single investment.

Ultimate fiduciary responsibility for the PUF rests with the Board of Regents. Section 66.08 of the Texas Education Code authorizes the Board of Regents to delegate to its committees, officers or employees of the U. T. System and other agents the authority to act for the Board of Regents in investment of the PUF. The PUF shall be managed through The University of Texas Investment Management Company ("UTIMCO") which shall a) recommend investment policy for the PUF, b) determine specific asset allocation targets, ranges and performance benchmarks consistent with PUF objectives, and c) monitor PUF performance against PUF objectives. UTIMCO shall invest the PUF's assets in conformity with investment policy.

UTIMCO may select and terminate unaffiliated investment managers subject to the Delegation of Investment Approval Authority approved by the UTIMCO Board. These guidelines are intended to ensure that the appropriate managers are retained to pursue a defined investment strategy within the PUF's portfolio structure and to define the general conditions under which a portfolio manager may be placed on a watch list or terminated. Such managers shall have complete investment discretion unless restricted by the terms of their management contracts. Managers shall be monitored for performance and adherence to investment disciplines.

PUF Administration

UTIMCO shall employ an administrative staff to ensure that all transaction and accounting records are complete and prepared on a timely basis. Internal controls shall be emphasized so as to provide for responsible separation of duties and adequacy of an audit trail. Custody of PUF assets shall comply with applicable law and be structured so as to provide essential safekeeping and trading efficiency.

PUF Investment Objectives

The primary investment objective shall be to preserve the purchasing power of PUF assets and annual distributions by earning an average annual real return of 5.1% over rolling ten-year periods or longer. This 5.1% target was derived by adding the current target distribution rate of 4.75% plus an annual expected expense of .35%. The PUF's success in meeting its objectives depends upon its ability to generate high returns in periods of low inflation that will offset lower returns generated in years when the capital markets underperform the rate of inflation.

The secondary fund objective is to generate a fund return in excess of the Policy Portfolio benchmark over rolling five-year periods or longer. The Policy Portfolio benchmark will be established by UTIMCO and will be comprised of a blend of asset class indices weighted to reflect PUF asset allocation policy targets.

Asset Allocation and Policy

Asset allocation is the primary determinant of the volatility of investment return and, subject to the asset allocation ranges specified in Exhibit A, is the responsibility of UTIMCO. Specific asset allocation positions may be changed from time to time, within the ranges specified in Exhibit A, based on the economic and investment outlook.

PUF assets shall be allocated among the following broad asset classes based upon their individual return/risk characteristics and relationships to other asset classes:

A. U.S. Equities - U.S. equities represent ownership in U.S. companies that are traded in public markets. Equities include stocks that are further identified by size of the company and are classified as large capitalization, medium capitalization, and small capitalization. U.S. equities may further be delineated by style (growth or value). Warrants, rights, options, futures and hedge funds are also included if the underlying assets are equities. In addition, Derivative Applications approved by the UTIMCO Board that serve as a U.S. equity substitute will be classified as U.S. equities. Equities provide both current income and growth of income.

B. Global ex U.S. Equities – Global ex U.S. equities represent ownership in global companies that are traded in public markets. The global ex U.S. markets include established and emerging markets. Equities include stocks that are further identified by size of the company and are classified as large capitalization, medium capitalization, and small capitalization. Global ex U.S. equities may further be delineated by style (growth or value) or region (Latin America, Asia etc.) or state of economic development (Emerging Markets). Warrants, rights, options, futures and hedge funds are also included if the underlying assets are equities. In addition, Derivative Applications approved by the UTIMCO Board that serve as a Global ex U.S. equity substitute will be classified as Global ex U.S. equities. Equities provide both current income and growth of income.

C. Hedge Funds – Hedge funds are broadly defined to include nontraditional investment strategies whereby the majority of the underlying securities are traded on public exchanges or are otherwise readily marketable.

   Equity Hedge Funds – Equity hedge fund investments include U.S. and international long/short equity strategies. These strategies attempt to exploit profits from stock selection skills by taking long and short positions in various equity securities. These strategies may also include fund of hedge fund investments. Equity hedge fund investments are made through private placement agreements.

Absolute Return Hedge Funds – Absolute return hedge fund investments include arbitrage and event driven strategies. Arbitrage strategies attempt to exploit pricing discrepancies between closely related securities, utilizing a variety of different tactics primarily within equity, fixed income and convertible securities markets. Event driven strategies attempt to exploit discreet events such as bankruptcies, mergers, and takeovers. Absolute return hedge funds may include fund of hedge fund investments. Absolute return hedge fund investments are made through private placement agreements.

D. Private Capital - Private Capital investments include the illiquid debt and equity securities of private or publicly-traded companies. Private Capital investments consist of two sub-asset class categories: Venture Capital and Private Equity.

Venture Capital – Venture capital investments consist of investments in companies, both U.S. and non-U.S. that are in the early stages of development. Venture Capital investments are held either through limited partnership or as direct ownership interests.

Private Equity – Private Equity investments consist of investments in the equity securities of private businesses, both U.S. and non-U.S., that are considered to be in the post-start-up phase and that are profitable and generating income. Private Equity investments are held either through limited partnerships or as direct ownership interests. The classification of private equity also includes mezzanine and opportunistic investments. Mezzanine consists of investments in funds that make subordinated debt or minority equity investments in private companies. Opportunistic investments are limited to illiquid assets and may include distressed debt or secondary private equity partnerships.

E. Commodities – Natural resource investments which include oil and gas interests, commodities, and other hard assets.

F. Fixed Income – Fixed income investments include debt issued by the U.S. Treasury, various government agencies and domestic and foreign corporations. The principal securities include bonds, notes, bills and mortgage and asset-backed securities. Fixed income investments also include hedge funds if the underlying assets are fixed income investments, and treasury inflation protected securities (TIPS) which are marketable securities with a return linked to the inflation rate. In addition, Derivative Applications approved by the UTIMCO Board that serve as a fixed income substitute will be classified as fixed income.

G. Cash & Equivalents – Cash & equivalents consist of money markets, deposit of the Texas State Treasury, foreign currencies and other overnight funds that have not been allocated to a specific asset class.

Performance Measurement

The investment performance of the PUF will be measured by the PUF's custodian, an unaffiliated organization, with recognized expertise in this field and reporting responsibility to the UTIMCO Board, and compared against the stated investment benchmarks of the PUF, as indicated in Exhibit A.

Investment Guidelines

The PUF must be invested at all times in strict compliance with applicable law.

Investment guidelines include the following:

<u>General</u>

- Investment guidelines for index and other commingled funds managed externally shall be governed by the terms and conditions of the Investment Management Contract.

- All investments will be U.S. dollar denominated assets unless held by an internal or external portfolio manager with discretion to invest in foreign currency denominated securities.

- Investment policies of any unaffiliated liquid investment fund must be reviewed and approved by the chief investment officer prior to investment of PUF assets in such liquid investment fund.

- No securities may be purchased or held which would jeopardize the PUF's tax-exempt status.

- No investment strategy or program may purchase securities on margin or use leverage unless specifically authorized by the UTIMCO Board.

- No investment strategy or program employing short sales may be made unless specifically authorized by the UTIMCO Board.

- The PUF's investments in warrants shall not exceed more than 5% of the PUF's net assets or 2% with respect to warrants not listed on the New York or American Stock Exchanges.

- The PUF may utilize Derivative Securities to: a) simulate the purchase or sale of an underlying market index while retaining a cash balance for fund management purposes; b) facilitate trading; c) reduce transaction costs; more

d) seek higher investment returns when a Derivative Security is priced attractively than the underlying security; e) index or to hedge risks associated with PUF investments; or f) adjust the market exposure of the asset allocation, including long and short strategies and other strategies provided that the PUF's use of derivatives complies with the Derivative Investment Policy approved by the UTIMCO Board. The Derivative Investment Policy shall serve the purpose of defining the permitted applications under which derivative securities can be used, which applications are prohibited, and the requirements for the reporting and oversight of their use. The objective of the Derivative Investment Policy is to facilitate risk management and provide efficiency in the implementation of the investment strategies using derivatives.

Cash and Cash Equivalents

Holdings of cash and cash equivalents may include the following:

- Internal short-term pooled investment funds managed by UTIMCO.
- Unaffiliated liquid investment funds as approved by the chief investment officer.
- Deposits of the Texas State Treasury.
- The PUF's custodian late deposit interest bearing liquid investment fund.
- Commercial paper must be rated in the two highest quality classes by Moody's Investors Service, Inc. (P1 or P2) or Standard & Poor's Corporation (A1 or A2).
- Negotiable certificates of deposit must be with a bank that is associated with a holding company meeting the commercial paper rating criteria specified above or that has a certificate of deposit rating of 1 or better by Duff & Phelps.
- Bankers' Acceptances must be guaranteed by an accepting bank with a minimum certificate of deposit rating of 1 by Duff & Phelps.
- Repurchase Agreements and Reverse Repurchase Agreements must be transacted with a dealer that is approved by UTIMCO and selected by the Federal Reserve Bank as a Primary Dealer in U.S. Treasury securities and rated A-1 or P-1 or the equivalent.
    - Each approved counterparty shall execute the Standard Public Securities Association (PSA) Master Repurchase Agreement with UTIMCO.

- Eligible Collateral Securities for Repurchase Agreements are limited to U.S. Treasury securities and U.S. Government Agency securities with a maturity of not more than 10 years.

- The maturity for a Repurchase Agreement may be from one day to two weeks.

- The value of all collateral shall be maintained at 102% of the notional value of the Repurchase Agreement, valued daily.

- All collateral shall be delivered to the PUF custodian bank. Tri-party collateral arrangements are not permitted.

• The aggregate amount of Repurchase Agreements with maturities greater than seven calendar days may not exceed 10% of the PUF's fixed income assets.

• Overnight Repurchase Agreements may not exceed 25% of the PUF's fixed income assets.

• Mortgage Backed Securities (MBS) Dollar Rolls shall be executed as matched book transactions in the same manner as Reverse Repurchase Agreements above. As above, the rules for trading MBS Dollar Rolls shall follow the Public Securities Association standard industry terms.

Fixed Income

Domestic Fixed Income

Holdings of domestic fixed income securities shall be limited to those securities a) issued by or fully guaranteed by the U.S. Treasury, U.S. Government-Sponsored Enterprises, or U.S. Government Agencies, and b) issued by corporations and municipalities. Within this overall limitation:

• Permissible securities for investment include the components of the Lehman Brothers Aggregate Bond Index (LBAGG): investment grade government and corporate securities, agency mortgage pass-through securities, and asset-backed securities. These sectors are divided into more specific subindices 1) Government: Treasury and Agency; 2) Corporate: Industrial, Finance, Utility, and Yankee; 3) Mortgage-backed securities: GNMA, FHLMC, and FNMA; 4) Asset-backed securities; 5) Taxable Municipal securities; and 6) Commercial Mortgage-backed securities. In addition to the permissible securities listed above, the following securities shall be permissible: a) floating rate securities with periodic coupon changes in market rates issued by the same entities that are included in the LBAGG as issuers of fixed rate securities; b) medium term notes issued by investment grade corporations; c) zero coupon bonds and stripped Treasury and Agency securities created from coupon securities; and d) structured notes issued by LBAGG qualified entities.

- U.S. Domestic Bonds must be rated investment grade, Baa3 or better by Moody's Investors Services, BBB- by Standard & Poor's Corporation, or an equivalent rating by a nationally recognized rating agency at the time of acquisition. This provision does not apply to an investment manager that is authorized by the terms of an investment advisory agreement to invest in below investment grade bonds.

- Not more than 5% of the market value of domestic fixed income securities may be invested in corporate and municipal bonds of a single issuer provided that such bonds, at the time of purchase, are rated, not less than Baa3 or BBB-, or the equivalent, by any two nationally-recognized rating services, such as Moody's Investors Service, Standard & Poor's Corporation, or Fitch Investors Service.

<u>Non-U.S. Fixed Income</u>

- Not more than 50% of the PUF's fixed income portfolio may be invested in non-U.S. dollar bonds. Not more than 15% of the PUF's fixed income portfolio may be invested in bonds denominated in any one currency.

- Non-dollar bond investments shall be restricted to bonds rated equivalent to the same credit standard as the U.S. Fixed Income Portfolio.

- Not more than 15% of the PUF's fixed income portfolio may be invested in Emerging Market debt.

- International currency exposure may be hedged or unhedged at UTIMCO's discretion or delegated by UTIMCO to an external investment manager.

<u>Equities</u>

The PUF shall:

A. hold no more than 25% of its equity securities in any one industry or industries (as defined by the standard industry classification code and supplemented by other reliable data sources) at market

B. hold no more than 5% of its equity securities in the securities of one corporation at cost unless authorized by the chief investment officer.

Members of UTIMCO management, with the approval of the UTIMCO Board, may serve as directors of companies in which UTIMCO has directly invested PUF assets. In such event, any and all compensation paid to UTIMCO management for their services as directors shall be endorsed over to UTIMCO and applied against

UTIMCO management fees. Furthermore, UTIMCO Board approval of UTIMCO management's service as a director of an investee company shall be conditioned upon the extension of UTIMCO's Directors and Officers Insurance Policy coverage to UTIMCO management's service as a director of an investee company.

PUF Distributions

The PUF shall balance the needs and interests of present beneficiaries with those of the future. PUF spending policy objectives shall be to:

A. provide a predictable, stable stream of distributions over time

B. ensure that the inflation adjusted value of distributions is maintained over the long term

C. ensure that the inflation adjusted value of PUF assets after distributions is maintained over the long term.

The goal is for the PUF's average spending rate over time not to exceed the PUF's average annual investment return after inflation and expenses in order to preserve the purchasing power of PUF distributions and underlying assets.

The Texas Constitution states that "The amount of any distributions to the available university fund shall be determined by the board of regents of The University of Texas System in a manner intended to provide the available university fund with a stable and predictable stream of annual distributions and to maintain over time the purchasing power of permanent university fund investments and annual distributions to the available university fund. The amount distributed to the available university fund in a fiscal year must be not less than the amount needed to pay the principal and interest due and owing in that fiscal year on bonds and notes issued under this section. If the purchasing power of permanent university fund investments for any rolling 10-year period is not preserved, the board may not increase annual distributions to the available university fund until the purchasing power of the permanent university fund investments is restored, except as necessary to pay the principal and interest due and owing on bonds and notes issued under this section. An annual distribution made by the board to the available university fund during any fiscal year may not exceed an amount equal to seven percent of the average net fair market value of permanent university fund investment assets as determined by the board, except as necessary to pay any principal and interest due and owing on bonds issued under this section. The expenses of managing permanent university fund land and investments shall be paid by the permanent university fund."

Annually, the Board of Regents will approve a distribution amount to the AUF.

In conjunction with the annual U. T. System budget process, UTIMCO shall recommend to the Board of Regents in May of each year an amount to be distributed to the AUF during the next fiscal year. UTIMCO's recommendation on the annual distribution shall be an amount equal to 4.75% of the trailing twelve quarter average of the net asset value of the PUF for the quarter ending February of each year.

Following approval of the distribution amount, distributions from the PUF to the AUF may be quarterly or annually at the discretion of UTIMCO Management.

PUF Accounting

The fiscal year of the PUF shall begin on September 1st and end on August 31st. Market value of the PUF shall be maintained on an accrual basis in compliance with Financial Accounting Standards Board Statements, Government Accounting Standards Board Statements, industry guidelines, and state statutes, whichever is applicable. Significant asset write-offs or write-downs shall be approved by the chief investment officer and reported to the UTIMCO Board of Directors. The PUF's financial statements shall be audited each year by an independent accounting firm selected by the Board of Regents.

Valuation of Assets

As of the close of business on the last business day of each month, UTIMCO shall determine the fair market value of all PUF net assets. Valuation of PUF assets shall be based on the books and records of the custodian for the valuation date. Valuation of alternative assets shall be determined in accordance with the UTIMCO Valuation Criteria for Alternative Assets.

The fair market value of the PUF's net assets shall include all related receivables and payables of the PUF on the valuation. Such valuation shall be final and conclusive.

Securities Lending

The PUF may participate in a securities lending contract with a bank or nonbank security lending agent for either short-term or long-term purposes of realizing additional income. Loans of securities by the PUF shall be collateralized by cash, letters of credit or securities issued or guaranteed by the U.S. Government or its agencies. The collateral will equal at least 100% of the current market value of the loaned securities. The contract shall state acceptable collateral for securities loaned, duties of the borrower, delivery of loaned securities and collateral, acceptable investment of collateral and indemnification provisions. The contract may include other provisions as appropriate.

The securities lending program will be evaluated from time to time as deemed necessary by the UTIMCO Board. Monthly reports issued by the agent shall be reviewed by UTIMCO to insure compliance with contract provisions.

Investor Responsibility

As a shareholder, the PUF has the right to a voice in corporate affairs consistent with those of any shareholder. These include the right and obligation to vote proxies in a manner consistent with the unique role and mission of higher education as well as for the economic benefit of the PUF. Notwithstanding the above, the UTIMCO Board shall discharge its fiduciary duties with respect to the PUF solely in the interest of PUF unitholders and shall not invest the PUF so as to achieve temporal benefits for any purpose including use of its economic power to advance social or political purposes.

Amendment of Policy Statement

The Board of Regents reserves the right to amend the Investment Policy Statement as it deems necessary or advisable.

Effective Date

The effective date of this policy shall be December 19, 2003.

EXHIBIT A

POLICY TARGETS, RANGES AND PERFORMANCE OBJECTIVES

	Percent of Portfolio (%)		
Asset Category	**Policy Targets**	**Policy Ranges**	**Benchmarks**
US Equities	25.0	15 to 45	Russell 3000 Index
Global ex US Equities:			MSCI All Country World Index ex US
Non-US Developed Equity	10.0	5 to 15	
Emerging Markets Equity	7.0	0 to 10	
Total Traditional Equity	**42.0**	**20 to 60**	
Equity Hedge Funds	10.0	5 to 15	90 Day T-Bills + 4%
Absolute Return Hedge Funds	15.0	10 to 20	90 Day T-Bills + 3%
Total Hedge Funds	**25.0**	**15 to 25**	
Venture Capital	6.0	0 to 10	Venture Economics Vintage Year Venture Capital Index
Private Equity	9.0	5 to 15	Venture Economics Vintage Year Private Equity Index
Total Private Capital	**15.0**	**5 to 15**	
Commodities	**3.0**	**0 to 5**	GSCI minus 1%
Fixed Income	**15.0**	**10 to 30**	Lehman Brothers Aggregate Bond Index
Cash	**0.0**	**0 to 5**	90 Day T-Bills

Expected Annual Return (%)	**8.36**
Downside Deviation (%)	**4.22**
Standard Deviation (%)	**10.30**

THE UNIVERSITY OF TEXAS SYSTEM
GENERAL ENDOWMENT FUND
INVESTMENT POLICY STATEMENT

Purpose

The General Endowment Fund (the "GEF"), established by the Board of Regents of The University of Texas System (the "Board of Regents") March 1, 2001, is a pooled fund for the collective investment of long-term funds under the control and management of the Board of Regents. The GEF provides for greater diversification of investments than would be possible if each account were managed separately.

GEF Organization

The GEF is organized as a mutual fund in which each eligible account purchases and redeems GEF units as provided herein. The ownership of GEF assets shall at all times be vested in the Board of Regents. Such assets shall be deemed to be held by the Board of Regents, as a fiduciary, regardless of the name in which the assets may be registered.

GEF Management

Ultimate fiduciary responsibility for the GEF rests with the Board of Regents. Section 66.08, Texas Education Code, as amended, authorizes the Board of Regents, subject to certain conditions, to enter into a contract with a nonprofit Corporation to invest funds under the control and management of the Board of Regents.

The GEF shall be governed through The University of Texas Investment Management Company ("UTIMCO"), a nonprofit Corporation organized for the express purpose of investing funds under the control and management of the Board of Regents. UTIMCO shall a) recommend investment policy for the GEF, b) determine specific asset allocation targets, ranges, and performance benchmarks consistent with GEF objectives, and c) monitor GEF performance against GEF objectives. UTIMCO shall invest the GEF assets in conformity with investment policy.

UTIMCO may select and terminate unaffiliated investment managers subject to the Delegation of Investment Approval Authority approved by the UTIMCO Board. These guidelines are intended to ensure that the appropriate managers are retained to pursue a defined investment strategy within the GEF's portfolio structure and to define the general conditions under which a portfolio manager may be placed on a watch list or terminated. Such managers shall have complete investment discretion unless restricted by the terms of their management contracts. Managers shall be monitored for performance and adherence to investment disciplines.

GEF Administration

UTIMCO shall employ an administrative staff to ensure that all transaction and accounting records are complete and prepared on a timely basis. Internal controls shall be emphasized so as to provide for responsible separation of duties and adequacy of an audit trail. Custody of GEF assets shall comply with applicable law and be structured so as to provide essential safekeeping and trading efficiency.

Funds Eligible to Purchase GEF Units

No fund shall be eligible to purchase units of the GEF unless it is under the sole control, with full discretion as to investments, by the Board of Regents and/or UTIMCO.

Any fund whose governing instrument contains provisions which conflict with this Policy Statement, whether initially or as a result of amendments to either document, shall not be eligible to purchase or hold units of the GEF.

GEF Investment Objectives

The primary investment objective shall be to preserve the purchasing power of GEF assets by earning an average annual real return of 5.1% over rolling ten-year periods or longer. This 5.1% target was derived by adding the current target distribution rate of 4.75% plus an annual expected expense of .35%. The GEF's success in meeting its objectives depends upon its ability to generate high returns in periods of low inflation that will offset lower returns generated in years when the capital markets underperform the rate of inflation.

The secondary fund objectives are to generate a fund return in excess of the Policy Portfolio benchmark and the average median return of the universe of the college and university endowments as reported annually by Cambridge Associates and NACUBO over rolling five-year periods or longer. The Policy Portfolio benchmark will be established by UTIMCO and will be comprised of a blend of asset class indices weighted to reflect GEF's asset allocation policy targets.

Asset Allocation and Policy

Asset allocation is the primary determinant of the volatility of investment return and, subject to the asset allocation ranges specified in Exhibit A, is the responsibility of UTIMCO. Specific asset allocation positions may be changed from time to time, within the ranges specified in Exhibit A, based on the economic and investment outlook.

GEF assets shall be allocated among the following broad asset classes based upon their individual return/risk characteristics and relationships to other asset classes:

A. U.S. Equities - U.S. equities represent ownership in U.S. companies that are traded in public markets. Equities include stocks that are further identified by size of the company and are classified as large capitalization, medium capitalization, and small capitalization. U.S. equities may further be delineated by style (growth or value). Warrants, rights, options, futures and hedge funds are also included if the underlying assets are equities. In addition, Derivative Applications approved by the UTIMCO Board that serve as a U.S. equity substitute will be classified as U.S. equities. Equities provide both current income and growth of income.

B. Global ex U.S. Equities – Global ex U.S. equities represent ownership in global companies that are traded in public markets. The global ex U.S. markets include established and emerging markets. Equities include stocks that are further identified by size of the company and are classified as large capitalization, medium capitalization, and small capitalization. Global ex U.S. equities may further be delineated by style (growth or value) or region (Latin America, Asia etc.) or state of economic development (Emerging Markets). Warrants, rights, options, futures and hedge funds are also included if the underlying assets are equities. In addition, Derivative Applications approved by the UTIMCO Board that serve as a Global ex U.S. equity substitute will be classified as Global ex U.S. equities. Equities provide both current income and growth of income.

C. Hedge Funds – Hedge funds are broadly defined to include nontraditional investment strategies whereby the majority of the underlying securities are traded on public exchanges or are otherwise readily marketable.

Equity Hedge Funds – Equity hedge fund investments include U.S. and international long/short equity strategies. These strategies attempt to exploit profits from stock selection skills by taking long and short positions in various equity securities. These strategies may also include fund of hedge fund investments. Equity hedge fund investments are made through private placement agreements.

Absolute Return Hedge Funds – Absolute return hedge fund investments include arbitrage and event driven strategies. Arbitrage strategies attempt to exploit pricing discrepancies between closely related securities, utilizing a variety of different tactics primarily within equity, fixed income and convertible securities markets. Event driven strategies attempt to exploit discreet events such as bankruptcies, mergers, and takeovers. Absolute return hedge funds may include fund of hedge fund investments. Absolute return hedge fund investments are made through private placement agreements.

D. Private Capital - Private Capital investments include the illiquid debt and equity securities of private or publicly-traded companies. Private Capital investments consist of two sub-asset class categories: Venture Capital and Private Equity.

Venture Capital – Venture Capital investments consist of investments in companies, both U.S. and non-U.S. that are in the early stages of development. Venture capital investments are held either through limited partnership or as direct ownership interests.

Private Equity – Private equity investments consist of investments in the equity securities of private businesses, both U.S. and non-U.S. that are considered to be in the post-start-up phase and that are profitable and generating income. Private Equity investments are held either through limited partnerships or as direct ownership interests. The classification of private equity also includes mezzanine and opportunistic investments. Mezzanine consists of investments in funds that make subordinated debt or minority equity investments in private companies. Opportunistic investments are limited to illiquid assets and may include distressed debt or secondary private equity partnerships.

E. Commodities – Natural resource investments which include oil and gas interests, commodities, and other hard assets.

F. Fixed Income – Fixed income investments include debt issued by the U.S. Treasury, various government agencies and domestic and foreign corporations. The principal securities include bonds, notes, bills and mortgage and asset-backed securities. Fixed income investments also include hedge funds if the underlying assets are fixed income investments, and treasury inflation protected securities (TIPS) which are marketable securities with a return linked to the inflation rate. In addition, Derivative Applications approved by the UTIMCO Board that serve as a fixed income substitute will be classified as fixed income.

G. Cash & Equivalents – Cash & equivalents consist of money markets, foreign currencies and other overnight funds that have not been allocated to a specific asset class.

Performance Measurement

The investment performance of the GEF will be measured by the GEF's custodian, an unaffiliated organization, with recognized expertise in this field and reporting responsibility to the UTIMCO Board, and compared against the stated investment benchmarks of the GEF, as indicated in Exhibit A.

Investment Guidelines

The GEF must be invested at all times in strict compliance with applicable law.

Investment guidelines include the following:

General

- Investment guidelines for index and other commingled funds managed externally shall be governed by the terms and conditions of the Investment Management Contract.

- All investments will be U.S. dollar denominated assets unless held by an internal or external portfolio manager with discretion to invest in foreign currency denominated securities.

- Investment policies of any unaffiliated liquid investment fund must be reviewed and approved by the chief investment officer prior to investment of GEF assets in such liquid investment fund.

- No securities may be purchased or held which jeopardize the GEF's tax exempt status.

- No investment strategy or program may purchase securities on margin or use leverage unless specifically authorized by the UTIMCO Board.

- No investment strategy or program employing short sales may be made unless specifically authorized by the UTIMCO Board.

- The GEF's investments in warrants shall not exceed more than 5% of the GEF's net assets or 2% with respect to warrants not listed on the New York or American Stock Exchanges.

- The GEF may utilize Derivative Securities to: a) simulate the purchase or sale of an underlying market index while retaining a cash balance for fund management purposes; b) facilitate trading; c) reduce transaction costs; d) seek higher investment returns when a Derivative Security is priced more attractively than the underlying security; e) index or to hedge risks associated with GEF investments; or f) adjust the market exposure of the asset allocation, including long and short strategies and other strategies provided that the GEF's use of derivatives complies with the Derivative Investment Policy approved by the UTIMCO Board. The Derivative Investment Policy shall serve the purpose of defining the permitted applications under which derivative securities can be used, which applications are prohibited, and the requirements for the reporting and oversight of their use. The objective of the Derivative Investment Policy is to facilitate risk management and provide efficiency in the implementation of the investment strategies using derivatives.

Cash and Cash Equivalents

Holdings of cash and cash equivalents may include the following:

- Internal short-term pooled investment funds managed by UTIMCO.

- Unaffiliated liquid investment funds as approved by the chief investment officer.

- The GEF's custodian late deposit interest bearing liquid investment fund.

- Commercial paper must be rated in the two highest quality classes by Moody's Investors Service, Inc. (P1 or P2) or Standard & Poor's Corporation (A1 or A2).

- Negotiable certificates of deposit must be with a bank that is associated with a holding company meeting the commercial paper rating criteria specified above or that has a certificate of deposit rating of 1 or better by Duff & Phelps.

- Bankers' Acceptances must be guaranteed by an accepting bank with a minimum certificate of deposit rating of 1 by Duff & Phelps.

- Repurchase Agreements and Reverse Repurchase Agreements must be transacted with a dealer that is approved by UTIMCO and selected by the Federal Reserve Bank as a Primary Dealer in U.S. Treasury securities and rated A-1 or P-1 or the equivalent.

    - Each approved counterparty shall execute the Standard Public Securities Association (PSA) Master Repurchase Agreement with UTIMCO.

    - Eligible Collateral Securities for Repurchase Agreements are limited to U.S. Treasury securities and U.S. Government Agency securities with a maturity of not more than 10 years.

    - The maturity for a Repurchase Agreement may be from one day to two weeks.

    - The value of all collateral shall be maintained at 102% of the notional value of the Repurchase Agreement, valued daily.

    - All collateral shall be delivered to the GEF custodian bank. Tri-party collateral arrangements are not permitted.

- The aggregate amount of repurchase agreements with maturities greater than seven calendar days may not exceed 10% of the GEF's fixed income assets.

- Overnight Repurchase Agreements may not exceed 25% of the GEF's fixed income assets.

- Mortgage Backed Securities (MBS) Dollar Rolls shall be executed as matched book transactions in the same manner as Reverse Repurchase Agreements above. As above, the rules for trading MBS Dollar Rolls shall follow the Public Securities Association standard industry terms.

Fixed Income

Domestic Fixed Income

Holdings of domestic fixed income securities shall be limited to those securities a) issued by or fully guaranteed by the U.S. Treasury, U.S. Government-Sponsored Enterprises, or U.S. Government Agencies, and b) issued by corporations and municipalities. Within this overall limitation:

- Permissible securities for investment include the components of the Lehman Brothers Aggregate Bond Index (LBAGG): investment grade government and corporate securities, agency mortgage pass-through securities, and asset-backed securities. These sectors are divided into more specific subindices 1) Government: Treasury and Agency; 2) Corporate: Industrial, Finance, Utility, and Yankee; 3) Mortgage-backed securities: GNMA, FHLMC, and FNMA; 4) Asset-backed securities; 5) Taxable Municipal securities; and 6) Commercial Mortgage-backed securities. In addition to the permissible securities listed above, the following securities shall be permissible: a) floating rate securities with periodic coupon changes in market rates issued by the same entities that are included in the LBAGG as issuers of fixed rate securities; b) medium term notes issued by investment grade corporations; c) zero coupon bonds and stripped Treasury and Agency securities created from coupon securities; and d) structured notes issued by LBAGG qualified entities.

- U.S. Domestic Bonds must be rated investment grade, Baa3 or better by Moody's Investors Services, BBB- by Standard & Poor's Corporation, or an equivalent rating by a nationally recognized rating agency at the time of acquisition. This provision does not apply to an investment manager that is authorized by the terms of an investment advisory agreement to invest in below investment grade bonds.

- Not more than 5% of the market value of domestic fixed income securities may be invested in corporate and municipal bonds of a single issuer provided that such bonds, at the time of purchase, are rated, not less than Baa3 or BBB-, or the equivalent, by any two nationally-recognized rating services, such as Moody's Investors Service, Standard & Poor's Corporation, or Fitch Investors Service.

<u>Non-U.S. Fixed Income</u>

- Not more than 50% of the GEF's fixed income portfolio may be invested in non-U.S. dollar bonds. Not more than 15% of the GEF's fixed income portfolio may be invested in bonds denominated in any one currency.

- Non-dollar bond investments shall be restricted to bonds rated equivalent to the same credit standard as the U.S. Fixed Income Portfolio.

- Not more than 15% of the GEF's fixed income portfolio may be invested in Emerging Market debt.

- International currency exposure may be hedged or unhedged at UTIMCO's discretion or delegated by UTIMCO to an external investment manager.

<u>Equities</u>

The GEF shall:

A. hold no more than 25% of its equity securities in any one industry or industries (as defined by the standard industry classification code and supplemented by other reliable data sources) at market

B. hold no more than 5% of its equity securities in the securities of one corporation at cost unless authorized by the chief investment officer.

Members of UTIMCO management, with the approval of the UTIMCO Board, may serve as directors of companies in which UTIMCO has directly invested GEF assets. In such event, any and all compensation paid to UTIMCO management for their services as directors shall be endorsed over to UTIMCO and applied against UTIMCO management fees. Furthermore, UTIMCO Board approval of UTIMCO management's service as a director of an investee company shall be conditioned upon the extension of UTIMCO's Directors and Officers Insurance Policy coverage to UTIMCO management's service as a director of an investee company.

GEF Accounting

The fiscal year of the GEF shall begin on September 1st and end on August 31st. Market value of the GEF shall be maintained on an accrual basis in compliance with Financial Accounting Standards Board Statements, Government Accounting

Standards Board Statements, or industry guidelines, whichever is applicable. Significant asset write-offs or write-downs shall be approved by the chief investment officer and reported to the UTIMCO Board of Directors. The GEF's financial statements shall be audited each year by an independent accounting firm selected by the Board of Regents.

Valuation of Assets

As of the close of business on the last business day of each month, UTIMCO shall determine the fair market value of all GEF net assets and the net asset value per unit of the GEF. Valuation of GEF assets shall be based on the books and records of the custodian for the valuation date. Valuation of alternative assets shall be determined in accordance with the UTIMCO Valuation Criteria for Alternative Assets.

The fair market value of the GEF's net assets shall include all related receivables and payables of the GEF on the valuation date and the value of each unit thereof shall be its proportionate part of such net value. Such valuation shall be final and conclusive.

Purchase of GEF Units

Purchase of GEF units may be made on any quarterly purchase date (September 1, December 1, March 1, and June 1 of each fiscal year or the first business day subsequent thereto) upon payment of cash to the GEF or contribution of assets approved by the chief investment officer, at the net asset value per unit of the GEF as of the most recent quarterly valuation date. Each fund whose monies are invested in the GEF shall own an undivided interest in the GEF in the proportion that the number of units invested therein bears to the total number of all units comprising the GEF.

Redemption of GEF Units

Redemption of GEF units shall be paid in cash as soon as practicable after the quarterly valuation date of the GEF. Withdrawals from the GEF shall be at the market value price per unit determined for the period of the withdrawal.

Securities Lending

The GEF may participate in a securities lending contract with a bank or nonbank security lending agent for either short-term or long-term purposes of realizing additional income. Loans of securities by the GEF shall be collateralized by cash, letters of credit, or securities issued or guaranteed by the U.S. Government or its agencies. The collateral will equal at least 100% of the current market value of the loaned securities. The contract shall state acceptable collateral for securities loaned, duties of the borrower, delivery of loaned securities and collateral, acceptable investment of collateral and indemnification provisions. The contract may include other provisions as appropriate.

The securities lending program will be evaluated from time-to-time as deemed necessary by the UTIMCO Board. Monthly reports issued by the agent shall be reviewed by UTIMCO to insure compliance with contract provisions.

Investor Responsibility

As a shareholder, the GEF has the right to a voice in corporate affairs consistent with those of any shareholder. These include the right and obligation to vote proxies in a manner consistent with the unique role and mission of higher education as well as for the economic benefit of the GEF. Notwithstanding the above, the UTIMCO Board shall discharge its fiduciary duties with respect to the GEF solely in the interest of GEF unitholders and shall not invest the GEF so as to achieve temporal benefits for any purpose including use of its economic power to advance social or political purposes.

Amendment of Policy Statement

The Board of Regents reserves the right to amend the Investment Policy Statement as it deems necessary or advisable.

Effective Date

The effective date of this policy shall be December 19, 2003.

EXHIBIT A

POLICY TARGETS, RANGES AND PERFORMANCE OBJECTIVES

	Percent of Portfolio (%)		
Asset Category	**Policy Targets**	**Policy Ranges**	**Benchmarks**
US Equities	25.0	15 to 45	Russell 3000 Index
Global ex US Equities:			MSCI All Country World Index ex US
Non-US Developed Equity	10.0	5 to 15	
Emerging Markets Equity	7.0	0 to 10	
Total Traditional Equity	**42.0**	**20 to 60**	
Equity Hedge Funds	10.0	5 to 15	90 Day T-Bills + 4%
Absolute Return Hedge Funds	15.0	10 to 20	90 Day T-Bills + 3%
Total Hedge Funds	**25.0**	**15 to 25**	
Venture Capital	6.0	0 to 10	Venture Economics Vintage Year Venture Capital Index
Private Equity	9.0	5 to 15	Venture Economics Vintage Year Private Equity Index
Total Private Capital	**15.0**	**5 to 15**	
Commodities	**3.0**	**0 to 5**	GSCI minus 1%
Fixed Income	**15.0**	**10 to 30**	Lehman Brothers Aggregate Bond Index
Cash	**0.0**	**0 to 5**	90 Day T-Bills

Expected Annual Return (%)	**8.36**
Downside Deviation (%)	**4.22**
Standard Deviation (%)	**10.30**

THE UNIVERSITY OF TEXAS SYSTEM
PERMANENT HEALTH FUND
INVESTMENT POLICY STATEMENT

Purpose

The Permanent Health Fund (the "PHF") is hereby established by the Board of Regents of The University of Texas System (the "Board of Regents"), as a pooled fund for the collective investment of certain permanent funds for health-related institutions of higher education created, effective August 30, 1999, by Chapter 63 of the Texas Education Code. The permanent health funds which have assets in the PHF are:

A. The Permanent Health Fund for Higher Education (PHFHE), the distributions from which are to fund programs that benefit medical research, health education, or treatment programs at 10 health-related institutions of higher education;

B. Eight of the thirteen separate Permanent Funds for Health Related Institutions (PFHRIs), the distributions from which are to fund research and other programs at health-related institutions of higher education that benefit public health. The PFHRIs invested in the PHF are:

U. T. Health Science Center - San Antonio
U. T. M. D. Anderson Cancer Center
U. T. Southwestern Medical Center - Dallas
U. T. Medical Branch - Galveston
U. T. Health Science Center - Houston
U. T. Health Center - Tyler
U. T. El Paso
Regional Academic Health Center

The PHF provides for greater diversification of investments than would be possible if each account were managed separately.

PHF Organization

The PHF is organized as a mutual fund in which each eligible account purchases and redeems PHF units as provided herein.

PHF Management

Chapter 63 of the Texas Education Code designates: a) the Board of Regents as the administrator for the PHFHE and b) the governing board of an institution for which a PFHRI fund is established as the administrator for its own PFHRI, or if the governing board so elects, the Comptroller of Public Accounts (State Comptroller). It permits the State Comptroller, in turn, to contract with the governing board of any institution that is eligible to receive a grant under Chapter 63. It further states that the Board of Regents may manage and invest the PHF in the same manner as the Board of Regents manages and invests other permanent endowments. It also requires that the administrator invest the funds in a manner that preserves the purchasing power of the funds' assets and distributions. It further requires that the administrator make distributions in a manner consistent with the administrator's policies and procedures for making distributions to the beneficiaries of its own endowments in the case of the PHFHE or the funds themselves in the case of the PFHRI funds.

Section 163 of the Texas Property Code provides the guidelines for the management, investment and expenditure of endowment funds. It also authorizes the Board of Regents to delegate to its committees, officers or employees of the U. T. System and other agents the authority to act for the Board of Regents in the investment of the PHF. The PHF shall be governed through The University of Texas Investment Management Company (UTIMCO) which shall: a) recommend investment policy for the PHF; b) determine specific asset allocation targets, ranges, and performance benchmarks consistent with PHF objectives; and c) monitor PHF performance against PHF objectives. UTIMCO shall invest the PHF assets in conformity with investment policy.

PHF Administration

UTIMCO shall employ an administrative staff to ensure that all transaction and accounting records are complete and prepared on a timely basis. Internal controls shall be emphasized so as to provide for responsible separation of duties and adequacy of an audit trail. Custody of PHF assets shall comply with applicable law and be structured so as to provide essential safekeeping and trading efficiency.

Funds Eligible to Purchase PHF Units

No fund shall be eligible to purchase units of the PHF unless it is a permanent health fund established pursuant to Chapter 63 of the Texas Education Code, under the control, with full discretion as to investments, by the Board of Regents and/or UTIMCO.

Any fund whose governing instrument contains provisions which conflict with this Policy Statement, whether initially or as a result of amendments to either document, shall not be eligible to purchase or hold units of the PHF.

PHF Investment Objectives

The primary investment objective shall be to preserve the purchasing power of PHF assets and annual distributions by earning an average annual real return of 5.1% over rolling ten-year periods or longer. This 5.1% target was derived by adding the current target distribution rate of 4.75% plus an annual expected expense of .35%. The PHF's success in meeting its objectives depends upon its ability to generate high returns in periods of low inflation that will offset lower returns generated in years when the capital markets underperform the rate of inflation.

The secondary fund objectives are to generate a fund return in excess of the Policy Portfolio benchmark and the average median return of the universe of the college and university endowments as reported annually by Cambridge Associates and NACUBO over rolling five-year periods or longer. The Policy Portfolio benchmark will be established by UTIMCO and will be comprised of a blend of asset class indices weighted to reflect PHF's asset allocation policy targets.

Asset Allocation and Policy

Asset allocation is the primary determinant of the volatility of investment return and, subject to the asset allocation ranges specified in Exhibit A and Exhibit B, is the responsibility of UTIMCO. PHF assets shall be allocated among the following investments:

A. Cash Equivalents - are highly reliable in protecting the purchasing power of current income streams but historically have not provided a reliable return in excess of inflation. Cash equivalents provide good liquidity under both deflation and inflation conditions.

B. U. T. System General Endowment Fund (GEF) (See Exhibit B)

Performance Measurement

The investment performance of the PHF will be measured by the PHF's custodian, an unaffiliated organization, with recognized expertise in this field and reporting responsibility to the UTIMCO Board. Such measurement will occur at least annually.

Investment Guidelines

The PHF must be invested at all times in strict compliance with applicable law.

Investment guidelines include the following:

General

- Investment guidelines for the U. T. System GEF shall be as stated in the GEF Investment Policy Statement.

- All investments will be reported in U.S. dollars.

- Investment policies of any unaffiliated liquid investment fund must be reviewed and approved by the chief investment officer prior to investment of PHF assets in such liquid investment fund.

- No securities may be purchased or held which jeopardize the PHF's tax exempt status.

- No investment strategy or program may purchase securities on margin or use leverage unless specifically authorized by the UTIMCO Board.

- No investment strategy or program employing short sales may be made unless specifically authorized by the UTIMCO Board.

<u>Cash and Cash Equivalents</u>

<u>Holdings of cash and cash equivalents may include the following:</u>

- Internal short-term pooled investment funds managed by UTIMCO.

- Unaffiliated liquid investment funds as approved by the chief investment officer.

- The PHF's custodian late deposit interest bearing liquid investment fund.

PHF Distributions

The PHF shall balance the needs and interests of present beneficiaries with those of the future. PHF spending policy objectives shall be to:

A. provide a predictable, stable stream of distributions over time

B. ensure that the inflation adjusted value of distributions is maintained over the long-term

C. ensure that the inflation adjusted value of PHF assets after distributions is maintained over the long-term.

The goal is for the PHF's average spending rate over time not to exceed the PHF's average annual investment return after inflation in order to preserve the purchasing power of PHF distributions and underlying assets.

UTIMCO shall be responsible for establishing the PHF's distribution percentage and determining the equivalent per unit rate for any given year. Unless otherwise established by UTIMCO and approved by the Board of Regents, fund distributions shall be based on the following criteria:

The annual unit distribution amount shall be adjusted annually based on the following formula:

A. Increase the prior year's per unit distribution amount (cents per unit) by the average inflation rate (C.P.I.) for the previous twelve quarters. This will be the per unit distribution amount for the next fiscal year. This amount may be rounded to the nearest $.0005 per unit.

B. If the inflationary increase in Step A. results in a distribution rate below 3.5%, (computed by taking the proposed distribution amount per unit divided by the previous twelve quarter average market value per unit) the UTIMCO Board, at its sole discretion, may grant an increase in the distribution amount as long such increase does not result in a distribution rate of more than 5.5%.

C. If the distribution rate exceeds 5.5%, (computed by taking the proposed distribution amount per unit divided by the previous twelve quarter average market value price per unit) the UTIMCO Board at its sole discretion, may reduce the per unit distribution amount.

Notwithstanding any of the foregoing provisions, the Board of Regents may approve a per unit distribution amount that, in their judgment, would be more appropriate than the rate calculated by the policy provisions.

Distributions from the PHF to the unitholders shall be made quarterly as soon as practicable on or after the last business day of November, February, May, and August of each fiscal year.

PHF Accounting

The fiscal year of the PHF shall begin on September 1st and end on August 31st. Market value of the PHF shall be maintained on an accrual basis in compliance with Financial Accounting Standards Board Statements, Government Accounting Standards Board Statements, or industry guidelines, whichever is applicable. Significant asset write-offs or write-downs shall be approved by the chief investment officer and reported to the UTIMCO Board of Directors. The PHF's financial statements shall be audited each year by an independent accounting firm selected by the Board of Regents.

Valuation of Assets

As of the close of business on the last business day of each month, UTIMCO shall determine the fair market value of all PHF net assets and the net asset value per unit of the PHF. Valuation of PHF assets shall be based on the books and records of the custodian for the valuation date. The fair market value of the PHF's net assets shall include all related receivables and payables of the PHF on the valuation date and the value of each unit thereof shall be its proportionate part of such net value. Such valuation shall be final and conclusive.

Purchase of PHF Units

Purchase of PHF units may be made on any quarterly purchase date (September 1, December 1, March 1, and June 1 of each fiscal year or the first business day subsequent thereto) upon payment of cash to the PHF or contribution of assets approved by the chief investment officer, at the net asset value per unit of the PHF as of the most recent quarterly valuation date.

Each fund whose monies are invested in the PHF shall own an undivided interest in the PHF in the proportion that the number of units invested therein bears to the total number of all units comprising the PHF.

Redemption of PHF Units

Redemption of PHF units shall be paid in cash as soon as practicable after the quarterly valuation date of the PHF. If the withdrawal is greater than $5 million, advance notice of 30 business days shall be required prior to the quarterly valuation date. If the withdrawal is for less than $5 million, advance notice of five business days shall be required prior to the quarterly valuation date. If the aggregate amount of redemptions requested on any redemption date is equal to or greater than 10% of the PHF's net asset value, the Board of Regents may redeem the requested units in installments and on a pro rata basis over a reasonable period of time that takes into consideration the best interests of all PHF unitholders. Withdrawals from the PHF shall be at the market value price per unit determined for the period of the withdrawal.

Investor Responsibility

The UTIMCO Board shall discharge its fiduciary duties with respect to the PHF solely in the interest of PHF unitholders and shall not invest the PHF so as to achieve temporal benefits for any purpose including use of its economic power to advance social or political purposes.

Amendment of Policy Statement

The Board of Regents reserves the right to amend the Investment Policy Statement as it deems necessary or advisable.

Effective Date

The effective date of this policy shall be December 19, 2003.

EXHIBIT A

PHF ASSET ALLOCATION

POLICY TARGETS, RANGES AND PERFORMANCE OBJECTIVES

	Neutral Allocation	Range	Benchmark Return
GEF Commingled Fund	**100.0%**	95%-100%	Endowment Policy Portfolio
Cash	**0.0%**	0%-5%	90 day T-Bills

Expected Annual Return (%)	**8.36**
Downside Deviation (%)	**4.22**
Standard Deviation (%)	**10.30**

The endowment policy portfolio is the sum of the neutrally weighted benchmark returns for the GEF.

EXHIBIT B

GEF ASSET ALLOCATION

POLICY TARGETS, RANGES AND PERFORMANCE OBJECTIVES

	Percent of Portfolio (%)		
Asset Category	**Policy Targets**	**Policy Ranges**	**Benchmarks**
US Equities	25.0	15 to 45	Russell 3000 Index
Global ex US Equities:			MSCI All Country World Index ex US
Non-US Developed Equity	10.0	5 to 15	
Emerging Markets Equity	7.0	0 to 10	
Total Traditional Equity	**42.0**	**20 to 60**	
Equity Hedge Funds	10.0	5 to 15	90 Day T-Bills + 4%
Absolute Return Hedge Funds	15.0	10 to 20	90 Day T-Bills + 3%
Total Hedge Funds	**25.0**	**15 to 25**	
Venture Capital	6.0	0 to 10	Venture Economics Vintage Year Venture Capital Index
Private Equity	9.0	5 to 15	Venture Economics Vintage Year Private Equity Index
Total Private Capital	**15.0**	**5 to 15**	
Commodities	**3.0**	**0 to 5**	GSCI minus 1%
Fixed Income	**15.0**	**10 to 30**	Lehman Brothers Aggregate Bond Index
Cash	**0.0**	**0 to 5**	90 Day T-Bills

Expected Annual Return (%)	**8.36**
Downside Deviation (%)	**4.22**
Standard Deviation (%)	**10.30**

THE UNIVERSITY OF TEXAS SYSTEM
LONG TERM FUND
INVESTMENT POLICY STATEMENT

Purpose

The Long Term Fund (the "LTF"), succeeded the Common Trust Fund in February, 1995, and was established by the Board of Regents of The University of Texas System (the "Board of Regents") as a pooled fund for the collective investment of private endowments and other long-term funds supporting various programs of The University of Texas System. The LTF provides for greater diversification of investments than would be possible if each account were managed separately.

LTF Organization

The LTF is organized as a mutual fund in which each eligible account purchases and redeems LTF units as provided herein. The ownership of LTF assets shall at all times be vested in the Board of Regents. Such assets shall be deemed to be held by the Board of Regents, as a fiduciary, regardless of the name in which the assets may be registered.

LTF Management

Ultimate fiduciary responsibility for the LTF rests with the Board of Regents. Section 163 of the Texas Property Code authorizes the Board of Regents to delegate to its committees, officers or employees of the U. T. System and other agents the authority to act for the Board of Regents in the investment of the LTF. The LTF shall be governed through The University of Texas Investment Management Company ("UTIMCO") which shall a) recommend investment policy for the LTF, b) determine specific asset allocation targets, ranges, and performance benchmarks consistent with LTF objectives, and c) monitor LTF performance against LTF objectives. UTIMCO shall invest the LTF assets in conformity with investment policy.

LTF Administration

UTIMCO shall employ an administrative staff to ensure that all transaction and accounting records are complete and prepared on a timely basis. Internal controls shall be emphasized so as to provide for responsible separation of duties and adequacy of an audit trail. Custody of LTF assets shall comply with applicable law and be structured so as to provide essential safekeeping and trading efficiency.

Funds Eligible to Purchase LTF Units

No fund shall be eligible to purchase units of the LTF unless it is under the sole control, with full discretion as to investments, by the Board of Regents and/or UTIMCO.

Any fund whose governing instrument contains provisions which conflict with this Policy Statement, whether initially or as a result of amendments to either document, shall not be eligible to purchase or hold units of the LTF.

LTF Investment Objectives

The primary investment objective shall be to preserve the purchasing power of LTF assets by earning an average annual real return of 5.1% over rolling ten year periods or longer. This 5.1% target was derived by adding the current target distribution rate of 4.75% plus an annual expected expense of .35%. The LTF's success in meeting its objectives depends upon its ability to generate high returns in periods of low inflation that will offset lower returns generated in years when the capital markets underperform the rate of inflation.

The secondary fund objectives are to generate a fund return in excess of the Policy Portfolio benchmark and the average median return of the universe of the college and university endowments as reported annually by Cambridge Associates and NACUBO over rolling five-year periods or longer. The Policy Portfolio benchmark will be established by UTIMCO and will be comprised of a blend of asset class indices weighted to reflect LTF's asset allocation policy targets.

Asset Allocation and Policy

Asset allocation is the primary determinant of the volatility of investment return and, subject to the asset allocation ranges specified in Exhibit A and Exhibit B, is the responsibility of UTIMCO. LTF assets shall be allocated among the following investments.

A. <u>Cash Equivalents</u> - are highly reliable in protecting the purchasing power of current income streams but historically have not provided a reliable return in excess of inflation. Cash equivalents provide good liquidity under both deflation and inflation conditions.

B. <u>U. T. System General Endowment Fund (GEF) (See Exhibit B)</u>

Performance Measurement

The investment performance of the LTF will be measured by the LTF's custodian, an unaffiliated organization, with recognized expertise in this field and reporting responsibility to the UTIMCO Board. Such measurement will occur at least annually.

Investment Guidelines

The LTF must be invested at all times in strict compliance with applicable law.

Investment guidelines include the following:

General

- Investment guidelines for the U. T. System GEF shall be as stated in the GEF Investment Policy Statement.

- All investments will be reported in U.S. dollars.

- Investment policies of any unaffiliated liquid investment fund must be reviewed and approved by the chief investment officer prior to investment of LTF assets in such liquid investment fund.

- No securities may be purchased or held which jeopardize the LTF's tax exempt status.

- No investment strategy or program may purchase securities on margin or use leverage unless specifically authorized by the UTIMCO Board.

- No investment strategy or program employing short sales may be made unless specifically authorized by the UTIMCO Board.

Cash and Cash Equivalents

Holdings of cash and cash equivalents may include the following:

- Include internal short-term pooled investment funds managed by UTIMCO.

- Unaffiliated liquid investment funds as approved by the chief investment officer.

- The LTF's custodian late deposit interest bearing liquid investment fund.

LTF Distributions

The LTF shall balance the needs and interests of present beneficiaries with those of the future. LTF spending policy objectives shall be to:

A. provide a predictable, stable stream of distributions over time

B. ensure that the inflation adjusted value of distributions is maintained over the long-term

C. ensure that the inflation adjusted value of LTF assets after distributions is maintained over the long-term.

The goal is for the LTF's average spending rate over time not to exceed the LTF's average annual investment return after inflation in order to preserve the purchasing power of LTF distributions and underlying assets.

Pursuant to the Uniform Management of Institutional Funds Act (“Act”), a governing board may distribute, for the uses and purposes for which the fund is established, the net appreciation, realized and unrealized, in the fair market value of the assets of an endowment fund over the historic dollar value of the fund to the extent prudent under the standard provided by the Act. In addition, income may be distributed for the purposes associated with the endowments/foundations.

UTIMCO shall be responsible for establishing the LTF’s distribution percentage and determining the equivalent per unit rate for any given year. Unless otherwise established by UTIMCO and approved by the Board of Regents or prohibited by the Act, fund distributions shall be based on the following criteria:

The annual unit distribution amount shall be adjusted annually based on the following formula:

A. Increase the prior year’s per unit distribution amount (cents per unit) by the average inflation rate (C.P.I.) for the previous twelve quarters. This will be the per unit distribution amount for the next fiscal year. This amount may be rounded to the nearest $.0005 per unit.

B. If the inflationary increase in Step A. results in a distribution rate below 3.5%, (computed by taking the proposed distribution amount per unit divided by the previous twelve quarter average market value price per unit) the UTIMCO Board, at its sole discretion, may grant an increase in the distribution amount as long as such increase does not result in a distribution rate of more than 5.5%.

C. If the distribution rate exceeds 5.5%, (computed by taking the proposed distribution amount per unit divided by the previous twelve quarter average market value per unit) the UTIMCO Board at its sole discretion, may reduce the per unit distribution amount.

Notwithstanding any of the foregoing provisions, the Board of Regents may approve a per unit distribution amount that, in their judgment, would be more appropriate than the rate calculated by the policy provisions.

Distributions from the LTF to the unitholders shall be made quarterly as soon as practicable on or after the last business day of November, February, May, and August of each fiscal year.

LTF Accounting

The fiscal year of the LTF shall begin on September 1st and end on August 31st. Market value of the LTF shall be maintained on an accrual basis in compliance with Financial Accounting Standards Board Statements, Government Accounting Standards Board Statements, or industry guidelines, whichever is applicable. Significant asset write-offs or write-downs shall be approved by the chief investment officer and reported to the UTIMCO Board. The LTF's financial statements shall be audited each year by an independent accounting firm selected by the Board of Regents.

Valuation of Assets

As of the close of business on the last business day of each month, UTIMCO shall determine the fair market value of all LTF net assets and the net asset value per unit of the LTF. Such valuation of LTF assets shall be based on the bank trust custody agreement in effect at the date of valuation. Valuation of LTF assets shall be based on the books and records of the custodian for the valuation date.

The fair market value of the LTF's net assets shall include all related receivables and payables of the LTF on the valuation date and the value of each unit thereof shall be its proportionate part of such net value. Such valuation shall be final and conclusive.

Purchase of LTF Units

Purchase of LTF units may be made on any quarterly purchase date (September 1, December 1, March 1, and June 1 of each fiscal year or the first business day subsequent thereto) upon payment of cash to the LTF or contribution of assets approved by the chief investment officer, at the net asset value per unit of the LTF as of the most recent quarterly valuation date.

Each fund whose monies are invested in the LTF shall own an undivided interest in the LTF in the proportion that the number of units invested therein bears to the total number of all units comprising the LTF.

Redemption of LTF Units

Redemption of LTF units shall be paid in cash as soon as practicable after the quarterly valuation date of the LTF. If the withdrawal is greater than $10 million, advance notice of 30 business days shall be required prior to the quarterly valuation date. If the withdrawal is for less than $10 million, advance notice of five business days shall be required prior to the quarterly valuation date. If the aggregate amount of redemptions requested on any redemption date is equal to or greater than 10% of the LTF's net asset value, the Board of Regents may redeem the requested units in installments and on a pro rata basis over a reasonable period of time that takes into consideration the best interests of all LTF unitholders. Withdrawals from the LTF shall be at the market value price per unit determined for the period of the withdrawal except as follows: withdrawals to correct administrative errors shall be calculated at the per unit value at the time the error occurred. To be considered an administrative error, the contribution shall have been invested in the LTF for a period less than or equal to one year determined from the date of the contribution to the LTF. Transfer of units between endowment unitholders shall not be considered redemption of units subject to this provision.

Investor Responsibility

The UTIMCO Board shall discharge its fiduciary duties with respect to the LTF solely in the interest of LTF unitholders and shall not invest the LTF so as to achieve temporal benefits for any purpose including use of its economic power to advance social or political purposes.

Amendment of Policy Statement

The Board of Regents reserves the right to amend the Investment Policy Statement as it deems necessary or advisable.

Effective Date

The effective date of this policy shall be December 19, 2003.

EXHIBIT A

LTF ASSET ALLOCATION

POLICY TARGETS, RANGES AND PERFORMANCE OBJECTIVES

	Neutral Allocation	Range	Benchmark Return
GEF Commingled Fund	**100.0%**	95%-100%	Endowment Policy Portfolio
Cash	**0.0%**	0%-5%	90 day T-Bills

Expected Annual Return (%)	**8.36**
Downside Deviation (%)	**4.22**
Standard Deviation (%)	**10.30**

The endowment policy portfolio is the sum of the neutrally weighted benchmark returns for the GEF.

EXHIBIT B

GEF ASSET ALLOCATION

POLICY TARGETS, RANGES AND PERFORMANCE OBJECTIVES

	Percent of Portfolio (%)		
Asset Category	**Policy Targets**	**Policy Ranges**	**Benchmarks**
US Equities	25.0	15 to 45	Russell 3000 Index
Global ex US Equities:			MSCI All Country World Index ex US
Non-US Developed Equity	10.0	5 to 15	
Emerging Markets Equity	7.0	0 to 10	
Total Traditional Equity	**42.0**	**20 to 60**	
Equity Hedge Funds	10.0	5 to 15	90 Day T-Bills + 4%
Absolute Return Hedge Funds	15.0	10 to 20	90 Day T-Bills + 3%
Total Hedge Funds	**25.0**	**15 to 25**	
Venture Capital	6.0	0 to 10	Venture Economics Vintage Year Venture Capital Index
Private Equity	9.0	5 to 15	Venture Economics Vintage Year Private Equity Index
Total Private Capital	**15.0**	**5 to 15**	
Commodities	**3.0**	**0 to 5**	GSCI minus 1%
Fixed Income	**15.0**	**10 to 30**	Lehman Brothers Aggregate Bond Index
Cash	**0.0**	**0 to 5**	90 Day T-Bills

Expected Annual Return (%)	**8.36**
Downside Deviation (%)	**4.22**
Standard Deviation (%)	**10.30**

The University of Texas Investment Management Company
Liquidity Policy

Effective Date of Policy: December 19, 2003
Date Approved by UTIMCO Board: December 4, 2003

Purpose:

The purpose of the Liquidity Policy is to establish limits on the overall liquidity profile of investments in the Permanent University Fund (PUF) and the General Endowment Fund (GEF), hereinafter referred to as the Funds. For the purposes of this policy, "liquidity" is defined as a measure of the ability of an investment position to be converted into a cash position. The established liquidity profile limits will act in conjunction with, but do not supercede, the Investment Policies established by The University of Texas Investment Management Company (UTIMCO) Board and approved by the U. T. Board of Regents.

Objective:

The objective of the Liquidity Policy is to control the element of total risk exposure of the Funds stemming from the uncertainties associated with the ability to convert longer term investments to cash to meet immediate needs or to change investment strategy, and to the potential cost of that conversion. This element of total risk is referred to as "Liquidity Risk" in this Policy.

Scope:

This Policy applies to all PUF and GEF investments made by UTIMCO, both by internal and by external managers. Policy implementation will be managed at the aggregate UTIMCO level and will not be a responsibility of individual internal or external managers managing a portion of the aggregate assets.

Definition of Liquidity Risk:

Liquidity Risk is defined as that element of total risk resulting from the uncertainty associated with both the cost and time period necessary to convert existing investment positions to cash (or cash equivalents). Liquidity risk can result in lower than expected returns and reduced opportunity to make changes in investment positions to respond to changes in capital market conditions. Modern finance theory asserts that liquidity risk is a systematic risk factor that is incorporated into asset prices such that future longer-term returns will be higher for assets with higher liquidity risk, although that may not be the case in the short term.

Liquidity Risk Measurement-The Liquidity Profile:

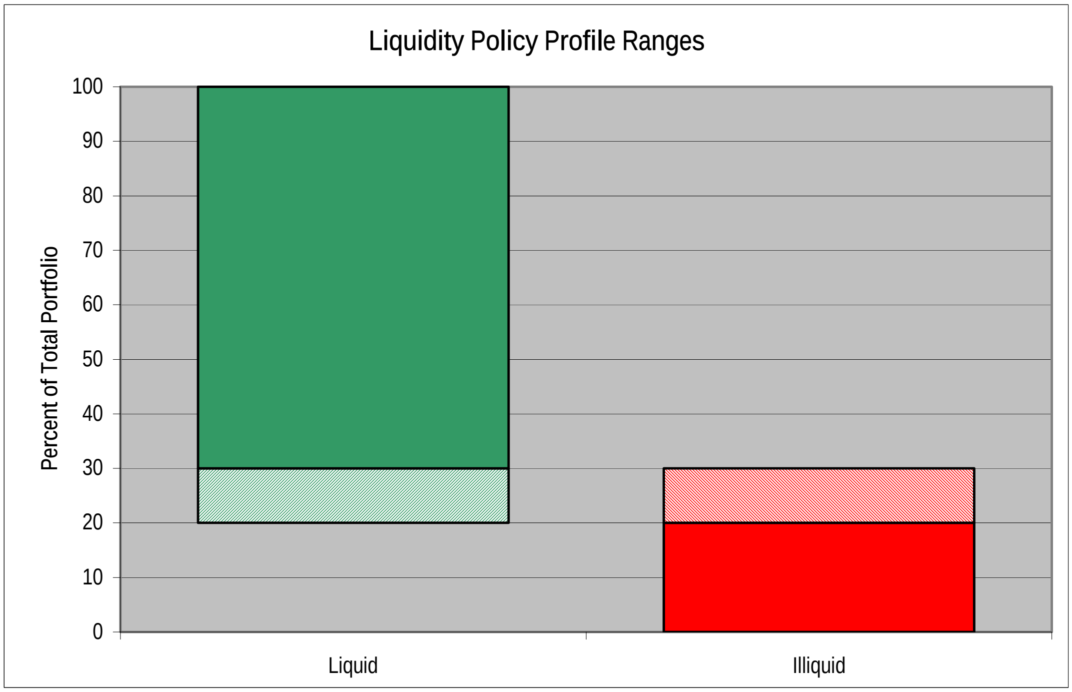
Capital market theory does not provide a precise technique to measure liquidity risk. For the purposes of this Liquidity Policy, potential liquidity risk will be defined and monitored by measuring the aggregate liquidity profile of the Funds. All individual investments within the Funds will be segregated into two categories:

- **Liquid:** Investments that could be converted to cash within a period of one day to three months in an orderly market at a discount of 10% or less.
- **Illiquid:** Investments that could be converted to cash in an orderly market over a period of more than three months or in a shorter period of time by accepting a discount of more than 10%.

The measurements necessary to segregate all investments into one of the two categories assume normally functioning capital markets and cash market transactions. In addition, swaps, derivatives, or other third party arrangements to create liquidity may be considered in determining the appropriate liquidity category for each investment upon approval of the UTIMCO Board or Board designated subcommittee.

The result of this liquidity risk measurement process will be a liquidity profile for the Funds which indicates the percentage of the total portfolio assets within each liquidity category. This Liquidity Policy defines the acceptable range of percentage of total assets within each liquidity category, specifies "trigger zones" requiring special review by UTIMCO staff and Board, and specifies the method of monitoring and presenting actual versus policy liquidity profiles.

Liquidity Policy Profile:
The current Liquidity Policy Profile ranges and trigger zones are defined by the chart below:



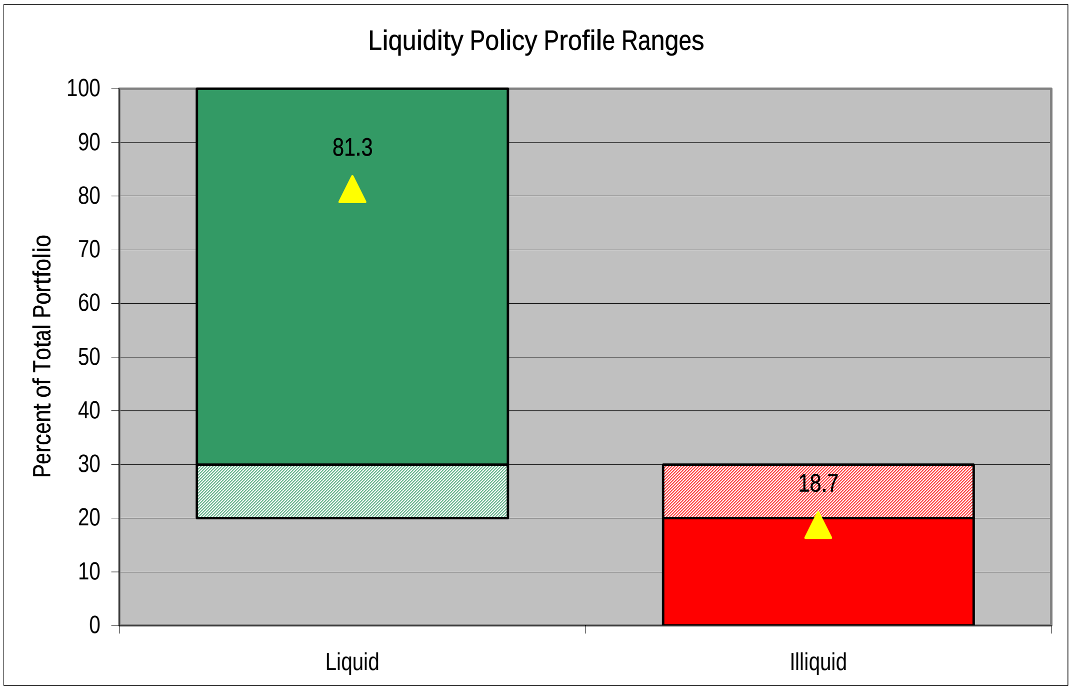
The green bar indicates the Policy range for investments categorized as "Liquid" by the definition presented earlier. The red bar indicates the Policy range for investments categorized as "Illiquid" by earlier definition. The shaded sections of the green and red bars indicate trigger zones requiring special action by the UTIMCO Board or a Board designated subcommittee. For example, the allowable range for "Illiquid" investments is 0% to 30% of the total portfolio, however, any investments made in the 20% to 30% range of total portfolio assets require special prior approval by the UTIMCO Board or subcommittee.

Documentation and Controls:
Managing Directors responsible for each asset class are responsible for determining the liquidity category for each investment in that class. These classifications will be reviewed by the Risk Manager and must receive final approval from the Chief Investment Officer. Classifications and weights within each liquidity category will be updated and reported on a monthly basis. All new investments considered will be categorized by liquidity category and a statement regarding the effect on overall liquidity of the addition of the new investment must be an element of the due diligence process and will be a part of all recommendation reports to the UTIMCO Board.

As additional safeguards, trigger zones have been established as indicated above to trigger required review and action by the UTIMCO Board in the event any investment action would cause any liquidity measure to enter any of the designated trigger zones, or in the event market actions caused measures to move into trigger zones. In addition, any proposed investment actions which would change any single liquidity category percentage by 10% or more would also require UTIMCO Board review and action prior to the change. Any actual positions in any trigger zones or outside the policy ranges will be communicated to the Chief Investment Officer immediately. The Chief Investment Officer will then determine the process to be used to eliminate the exception and report promptly to the UTIMCO Board the circumstances of the deviation from Policy and the remedy to the situation.

Reporting:

The actual Liquidity Profile of the Funds and compliance with the Liquidity Policy will be reported to the UTIMCO Board on at least a quarterly basis. Any exception to the Policy and actions taken to remedy the exception will be reported promptly. An example of the method of reporting is shown below where the yellow points and number labels indicate current actual exposure levels within each Liquidity Policy Range (numbers shown are examples only). For example, in this illustration the current exposure to "Liquid" investments is 81.3%, while exposure to "Illiquid" investments is 18.7% and both are within their respective allowable policy ranges and not in defined trigger zones.



RESOLUTION

WHEREAS, The University of Texas System has been extensively engaged in the review of its organizational oversight and responsibility functions for the purpose of improving governance structures in the course of the Board's ongoing accountability activities; and

WHEREAS, The University of Texas Investment Management Company was formed in 1995 and has operated, under contract with the Board of Regents since 1996, through multiple market cycles and several changes in the management team.

THEREFORE, BE IT RESOLVED, That over the next several months, the U. T. Board of Regents will examine and evaluate The University of Texas Investment Management Company (UTIMCO) as to structure and services, including the following:

Investment services;
Administrative services;
Cost effectiveness;
Policy setting procedures;
Consulting services utilized;
Legal services utilized;
Budgeting procedures;
Oversight and reporting functions;
Contract form and legal structure; and
Other relevant and structural issues

with the goal of defining and structurally improving the investment management function of the U. T. System.

4. U. T. System: Correction of oversight of tuition approval for U. T. Austin School of Law for Academic Year 2005-2006

The action of the Board of Regents on November 18, 2003, approving tuition and fees to be effective January 23, 2004, was clarified to specifically approve tuition increases for Academic Year 2005-2006 at The University of Texas at Austin School of Law, as recommended by Chancellor Yudof.

5. U. T. Austin: Approval for the Geology Foundation, with the assistance of the Bureau of Economic Geology, to manage the royalties received from the Estate of John A. Jackson, Deceased (Waiver of Regents' Rules and Regulations, Part Two, Chapter IX, Section 1, Subsection 1.3)

The Board waived Subsection 1.3 of Section 1, Chapter IX, Part Two of the Regents' Rules and Regulations to authorize the Geology Foundation of The University of Texas at Austin, with assistance from the Bureau of Economic Geology, to manage the royalties received from the Estate of John A. Jackson, Deceased, as part of the bequest of 95% of the residuary estate.

Further, approval of the waiver is conditioned upon the development of procedures that assure appropriate oversight by the Board and the Chancellor of the expenditure by the Foundation of income from this bequest and other sources.

The Geology Foundation is an internal foundation of The University of Texas System created in October 1953 by a Board of Regents' resolution as set forth in Section 7, Subsection 7.3, Subdivision 7.31 of Part One, Chapter VII of the Regents' Rules and Regulations. The Foundation supports the Bureau of Economic Geology and the Institute of Geophysics, as well as the Department of Geological Sciences.

Mr. John A. Jackson died on March 21, 2003, and his Will included an express bequest of 95% of his residuary estate to the Geology Foundation to be used as a part of the John A. and Katherine G. Jackson Endowed Fund in Geosciences (Endowed Fund), which was created on June 15, 2001. The Endowed Fund is a permanent endowment for the Geology Foundation of U. T. Austin, which supports the John A. and Katherine G. Jackson School of Geosciences (School of Geosciences). This approximately $232 million bequest includes mineral interests valued in the probate inventory at $80,185,436.85. The University of Texas Investment Management Company (UTIMCO) will manage the nonmineral interest portion of the bequest.

Part Two, Chapter IX, Section 1, Subsection 1.3 of the Regents' Rules provides that all assets received by the Board through a bequest shall be accepted and processed by the Office of External Relations and, after acceptance and processing, shall be delivered to the appropriate office for management. Part Two, Chapter IX, Section 6, Subsection 6.8 of the Regents' Rules, provides that University Lands - West Texas Operations is to manage gifts of mineral interests received through bequests. In order for the Geology Foundation to manage the royalties, the Board of Regents must waive Subsection 6.8 "by a majority of all of the members of the Board" pursuant to Part One, Chapter I, Section 1, Subsection 1.3 of the Regents' Rules.

The Geology Foundation has developed Financial Management Procedures that provide instructions for management of the mineral interests and royalty payments to be received as a result of the addition of the mineral estates to the Endowed Fund. The Financial Management Procedures establish systems to manage the legal documents concerning ownership and royalty rights and to account for receipt and deposit of payments as well as provide an audit trail for distributions from the Endowed Fund to support the activities of the School of Geosciences. The Audit Office of the U. T. System will periodically audit the records of the Geology Foundation to ensure compliance with developed procedures. Findings of the U. T. System Audit Office will be reported to the Board of Regents, the Chancellor, and the President of U. T. Austin.

6. U. T. Dallas: Authorization to negotiate and enter into an economic development agreement with the State of Texas for expansion of the Erik Jonsson School of Engineering and Computer Science

The Board authorized the Chancellor to negotiate the terms of and execute any and all documents necessary to enter into an economic development agreement with the State of Texas, acting by and through the Office of the Governor, Economic Development and Tourism (State) to expand and enhance the Erik Jonsson School of Engineering and Computer Science at The University of Texas at Dallas.

The State of Texas is negotiating an agreement with Texas Instruments for construction of a $3 billion research, development, and manufacturing facility to be located in Richardson, Texas. This facility will be designed to manufacture advanced semiconductor devices. As part of that agreement, the State has offered to significantly enhance the academic and research programs at the Erik Jonsson School of Engineering and Computer Science at U. T. Dallas (the Jonsson School) as an incentive for Texas Instruments to locate the facility in the state.

To satisfy the State's commitment to Texas Instruments, the State and The University of Texas System have proposed a $300 million, five-year program aimed at elevating the Jonsson School to a Top-50 ranking among U.S. engineering schools.

7. U. T. Dallas: Campus Housing Phase IX - Approve design development; approve alternative energy economic feasibility; approve total project cost; appropriate funds and authorize expenditure; and parity debt

The Board approved the recommendations listed below for The University of Texas at Dallas Campus Housing Phase IX project:

Project Number:	301-173	
Architecturally or Historically Significant:	Yes ☐ No ☒	
Project Delivery Method:	Competitive Sealed Proposals	
Substantial Completion Date:	July 2005	
Total Project Cost:	Source Revenue Financing System Bond Proceeds	Current $4,000,000

Debt Service: The debt will be repaid from net student housing revenues at U. T. Dallas. Annual debt service on $4,000,000 of Revenue Financing System debt is projected to be $1,171,511. Debt service coverage for the project is expected to be at least 1.77 times.

Recommendations:

a. approve design development plans;

b. approve the evaluation of alternative energy economic feasibility;

c. approve the total project cost;

d. appropriate funds and authorize expenditure of funds; and

e. make the "finding of fact" determinations required by Section 5 of the Master Resolution regarding the ability to repay debt prior to the issuance of additional Revenue Financing System parity debt.

Previous Board Actions: In November 2003, the project was authorized for inclusion in the Capital Improvement Program (CIP).

Project Description: Approval of the Campus Housing Phase IX project at U. T. Dallas was needed at this time to help meet the anticipated growth in enrollment and the heavy demand for housing. Current facilities are operating at close to 100% occupancy. Approximately 200 beds will be made available in garden-style apartments with a completion date of August 2004.

Texas Government Code Section 2166.403 requires the governing body of a State agency to verify in an open meeting the economic feasibility of incorporating alternative energy devices into a new State building. Therefore, the Project Architect prepared an evaluation for this project in accordance with the Energy Conservation Design Standards for New State Buildings. This evaluation determined that alternative energy devices such as solar, wind, biomass, or photovoltaic energy are not economically feasible for the project.

8. <u>U. T. Southwestern Medical Center - Dallas: Authorization to purchase approximately 12.709 acres of land and improvements and a leasehold interest in 0.348 acres of land located at 2232 Inwood Road, Dallas, Dallas County, Texas, and authorization for the Executive Director of Real Estate to execute all documents related thereto</u>

On behalf of The University of Texas Southwestern Medical Center at Dallas, the Board:

a. authorized the purchase of approximately 12.709 acres of land and improvements and a leasehold interest in 0.348 acres of land located at 2232 Inwood Road, Dallas, Dallas County, Texas, from the City of Dallas; and

b. authorized the Executive Director of Real Estate to execute all documents, instruments, and other agreements, and to take all further actions deemed necessary or advisable to carry out the purpose and intent of the foregoing action.

The subject property is a 13.057-acre tract of land and improvements consisting of 12.709 acres owned by the City of Dallas and the City's leasehold interest in 0.348 acres of land. The buildings are industrial warehouse structures used by the City of Dallas for vehicle repair and maintenance, and have a combined area of approximately 64,618 square feet. The property is located near the Inwood entrance to the north campus, and is identified within the campus development zones in the Campus Master Plan 2002 Update as well as the acquisition area established by the 60th Texas Legislature, Regular Session (House Bill 287, Chapter 73), which authorizes acquisition of properties to be used for campus expansion and university purposes.

The institution will purchase the property to develop the site as a biomedical technology center or as an asset to support other medical missions. It is anticipated that U. T. Southwestern Medical Center - Dallas will seek a private entity to develop the property as a Biomedical Technology Research Center under a ground lease.

The purchase price of $4.1 million is supported by three appraisals ranging from $4.15 million to $6.73 million that were prepared in 2001 and 2002 for the City of Dallas and the General Land Office. Significant increases in value in the immediate area over recent months have been documented by the Real Estate Office. The source of funding for the acquisition will be Local Fund cash balances.

As partial consideration to the City of Dallas for making the land available, U. T. Southwestern Medical Center - Dallas will share 25% of any equity received, if any, in lieu of rent from tenants of the biotechnology facility on the premises. In the unlikely event the property is sold within 10 years, the City of Dallas will receive 50% of any net profits associated with the value of the land. The environmental assessment of the property indicated the need to remediate contamination on the site. As conditions prior to closing, the City will apply to the Texas Commission on Environmental Quality to participate in the Voluntary Cleanup Program and to obtain an Innocent Owner Certificate and will pay all costs required to remediate the site.

9. U. T. Southwestern Medical Center - Dallas: Authorization to sell real property and improvements located at 5140 Seneca Drive (Bashour House), Dallas, Dallas County, Texas, and authorization for the Executive Director of Real Estate to execute all documents related thereto

On behalf of The University of Texas Southwestern Medical Center at Dallas, the Board:

a. authorized the sale of real property and improvements located at 5140 Seneca Drive (Bashour House), Dallas, Dallas County, Texas, to Ms. Laurel Payne Smith for $1.3 million. If the contract with Ms. Smith is terminated, the property will be sold to the purchaser offering the highest amount equaling or exceeding the appraised value of $1.1 million.

b. authorized the Executive Director of Real Estate to execute all documents, instruments, and other agreements, and to take all further actions deemed necessary or advisable to carry out the purpose and intent of the foregoing transaction.

In December 1992, the Board accepted a gift of the subject property, known as "Bashour House", from the Cardiology Fund, Inc., of Dallas, Texas, for use as a residence for the President of U. T. Southwestern Medical Center - Dallas or other senior staff as designated by the President. The property was leased to Dr. Fouad A. Bashour. Dr. Bashour died on January 1, 2003, and the institution now wishes to sell the property, which is consistent with the original gift. The net proceeds from the sale will be added to the Fouad A. Bashour Cardiology Fund Endowment at U. T. Southwestern Medical Center - Dallas.

10. U. T. Southwestern Medical Center - Dallas: Ambulatory Surgical Center - Amendment of the FY 2004-2009 Capital Improvement Program and FY 2004-2005 Capital Budget to include project

The Board amended the FY 2004-2009 Capital Improvement Program (CIP) and the FY 2004-2005 Capital Budget to include the Ambulatory Surgical Center project at The University of Texas Southwestern Medical Center at Dallas and determined the project was not to be designated as architecturally or historically significant.

Project Delivery Method:	To be determined		
Architecturally or Historically Significant:	Yes ☐ No ☒		
Substantial Completion Date:	January 2006		
Total Project Cost:	Source	Current	Proposed
	Revenue Financing System Bond Proceeds	–	$62,400,000

Project Description:

The Ambulatory Surgical Center project consists of an approximately 250,000 gross square foot, 10-story building and an approximately 625 car parking garage. The building will initially include five finished floors totaling approximately 125,000 gross square feet and five shelled floors.

The Ambulatory Surgical Center will include ambulatory surgical and procedure suites and diagnostic and treatment rooms including imaging, clinics, and physician offices. The building will be located on the west side of St. Paul University Hospital adjacent to Medical Center Drive, in conformance with the current Campus Master Plan.

This is the first project to move forward as part of the work envisioned in the Clinical Services Building that is currently on the Future Projects list at $146,000,000. Working with the faculty and hospital partners, the immediate need has been identified to provide new space to conduct outpatient surgery. Presently, these procedures, including orthopedics, plastics, and gastrointestinal day procedures, are conducted primarily in the hospitals. With limited operating rooms, the outpatient surgery naturally competes for space, causing delays in conducting the less acute procedures. The conclusion of the combined hospital and practice management team, along with both University and private physicians, is that this new facility is vital to the combined operations.

This off-cycle project has been approved by U. T. System staff and meets the criteria for inclusion in the Capital Improvement Program.

ADJOURNMENT.--Chairman Miller announced that the purpose for which this meeting was called had been completed, and the meeting was duly adjourned at 1:34 p.m.

/s/ Francie A. Frederick
Counsel and Secretary to the Board

January 27, 2004