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Committee Meeting: 11/10/2010

*Paul Foster, Chairman
Printice L. Gary
Brenda Pejovich
Wm. Eugene Powell*

Board Meeting: 11/11/2010
Austin, Texas

| | Committee Meeting | Board Meeting | Page |
|--|---|----------------------|-------------|
| Convene | <i>5:00 p.m. Chairman Foster</i> | | |
| 1. U. T. System: Discussion and appropriate action related to approval of <i>Docket No. 144</i> | <i>5:00 p.m. Discussion Dr. Kelley</i> | Action | 108 |
| 2. U. T. System: Key Financial Indicators Report | <i>5:10 p.m. Report Dr. Kelley</i> | Not on Agenda | 108 |
| 3. U. T. System: Overview of U. T. System debt programs | <i>5:20 p.m. Report/Discussion Mr. Aldridge</i> | Not on Agenda | 117 |
| 4. U. T. System Board of Regents: The University of Texas Investment Management Company (UTIMCO) Performance Summary Report and Investment Reports for the fiscal year and quarter ended August 31, 2010 | <i>5:35 p.m. Report/Discussion Mr. Zimmerman</i> | Report | 138 |
| 5. U. T. System Board of Regents: Approval of Custodian Agreements for The University of Texas Investment Management Company (UTIMCO) | <i>5:40 p.m. Action Mr. Zimmerman</i> | Action | 144 |
| 6. U. T. System Board of Regents: Approval of the Annual Budget, including the capital expenditures budget, and Annual Fee and Allocation Schedule for The University of Texas Investment Management Company (UTIMCO) | <i>5:45 p.m. Action Mr. Zimmerman</i> | Action | 145 |
| 7. U. T. System Board of Regents: Approval of revisions to the amended and restated University of Texas Investment Management Company (UTIMCO) Compensation Program | <i>5:55 p.m. Action Dr. Kelley Mr. Aldridge</i> | Action | 159 |
| Adjourn | <i>6:00 p.m.</i> | | |

1. **U. T. System: Discussion and appropriate action related to approval of Docket No. 144**

RECOMMENDATION

It is recommended that *Docket No. 144* be approved. The Docket is behind the Docket tab.

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

2. **U. T. System: Key Financial Indicators Report**

REPORT

Dr. Scott C. Kelley, Executive Vice Chancellor for Business Affairs, will discuss the Key Financial Indicators Report, as set forth on Pages 109 - 116. The report represents the consolidated and individual operating results of the U. T. System institutions.

The Key Financial Indicators Report compares the Systemwide results of operations, key revenues and expenses, reserves, and key financial ratios in a graphical presentation from Fiscal Year 2006 through July 2010. Ratios requiring balance sheet data are provided for Fiscal Year 2005 through Fiscal Year 2009.


















THE UNIVERSITY OF TEXAS SYSTEM



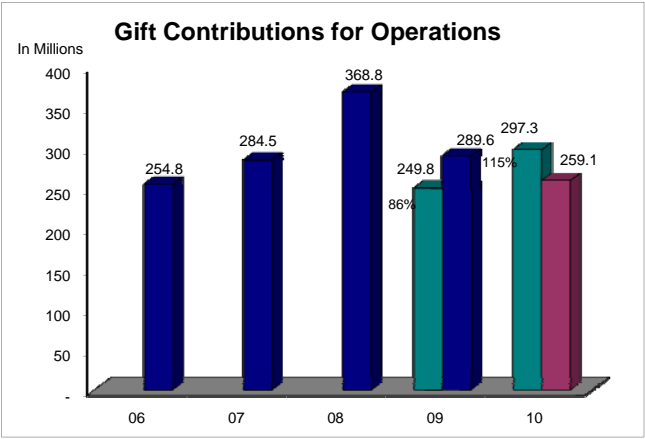
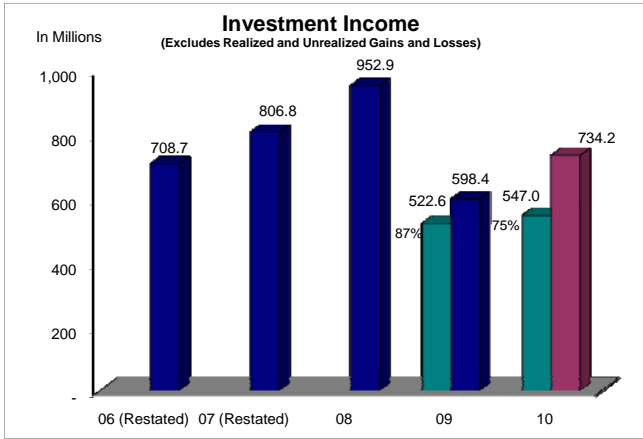
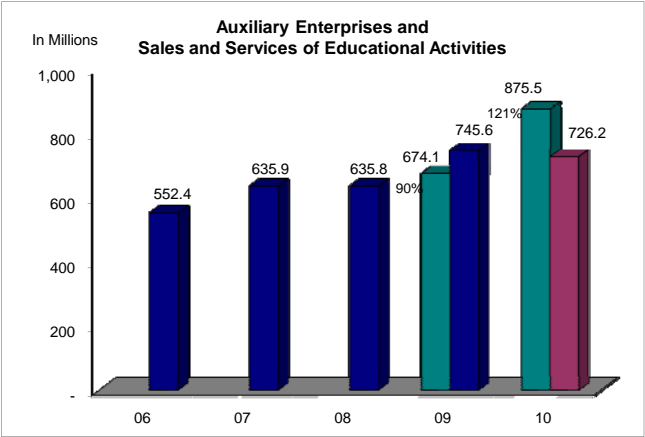
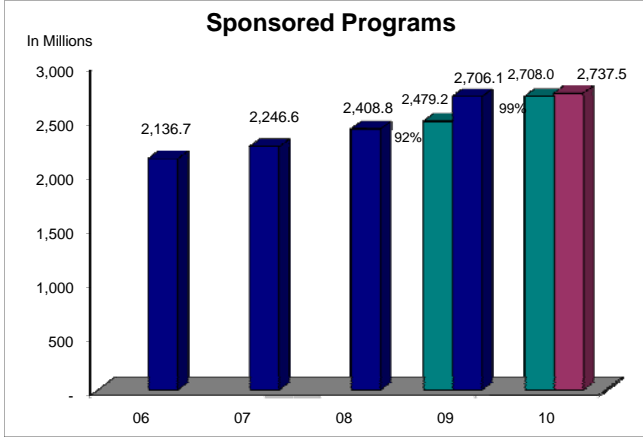
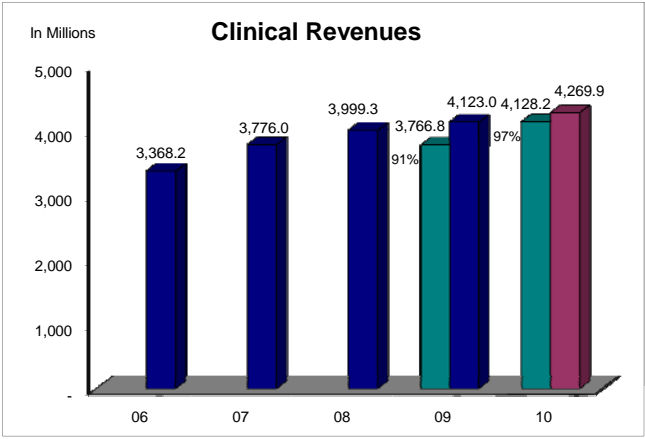
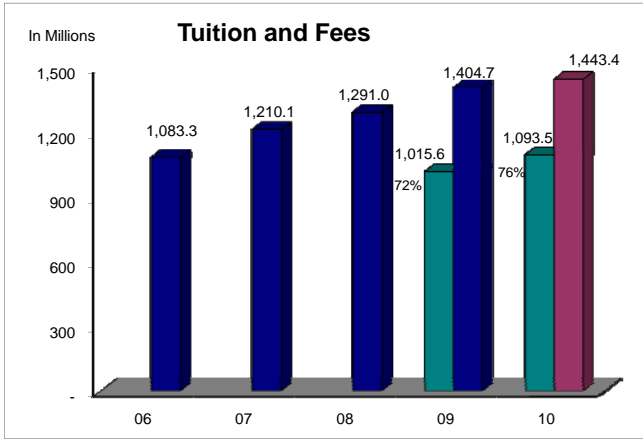
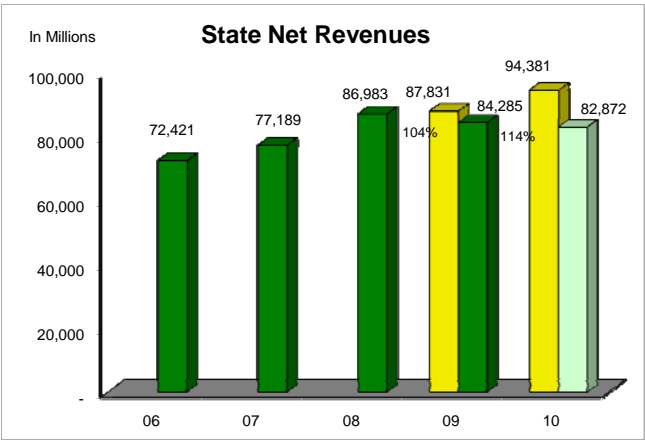
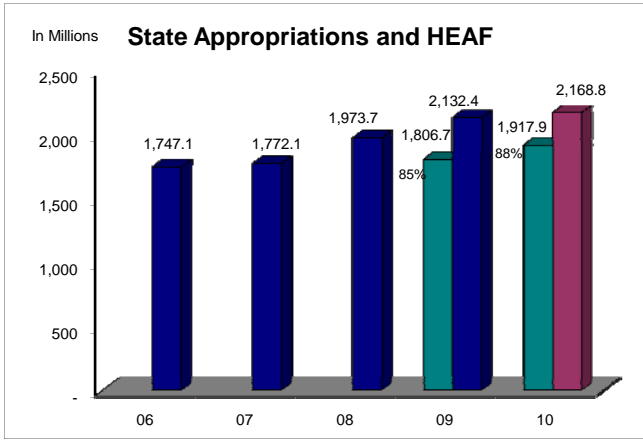
KEY FINANCIAL INDICATORS REPORT

JULY 2010

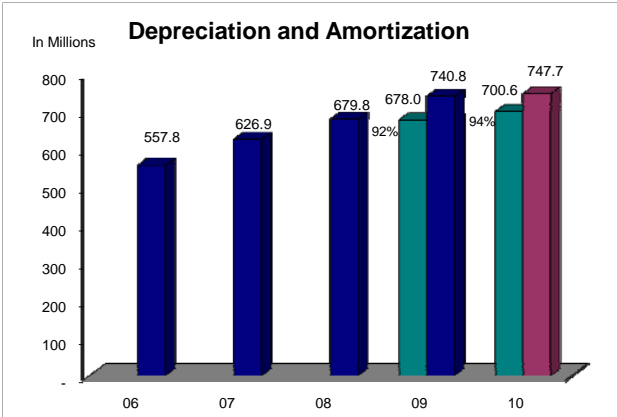
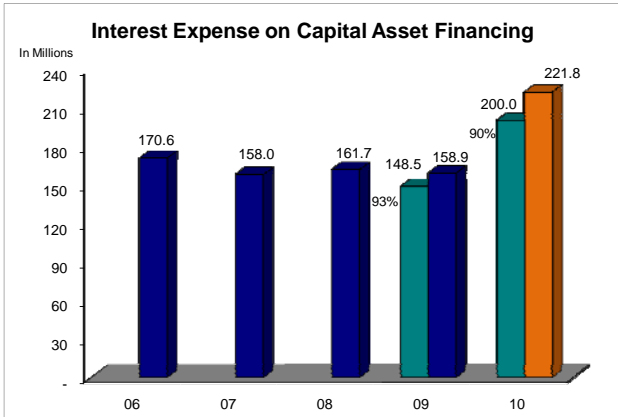
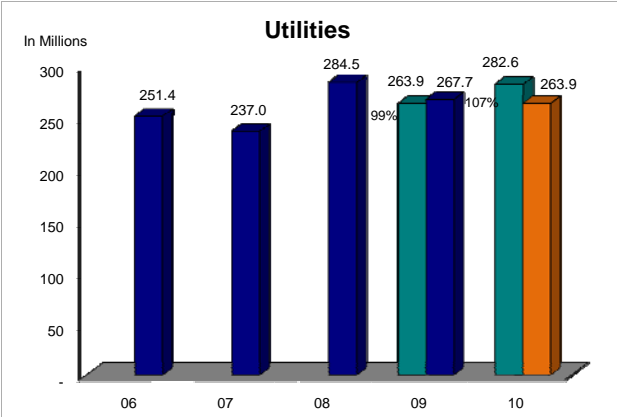
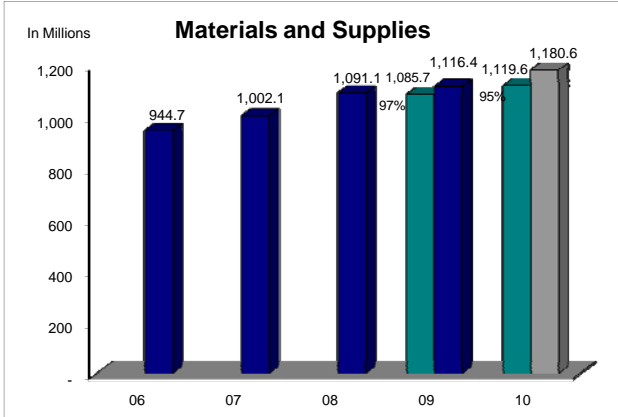
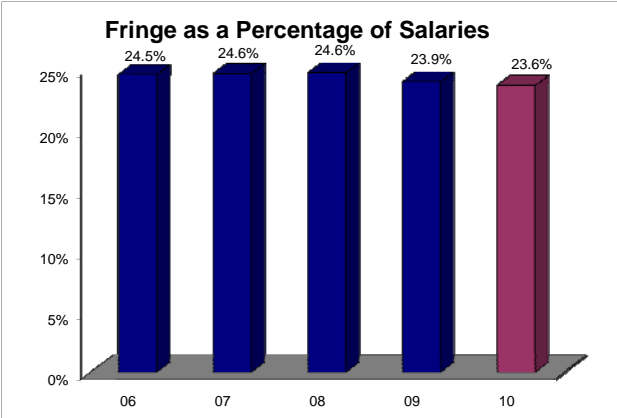
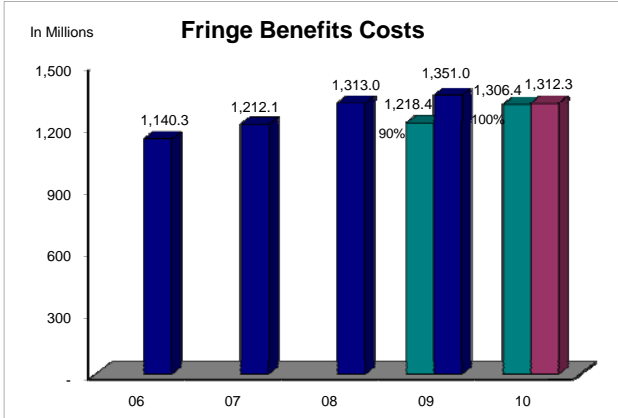
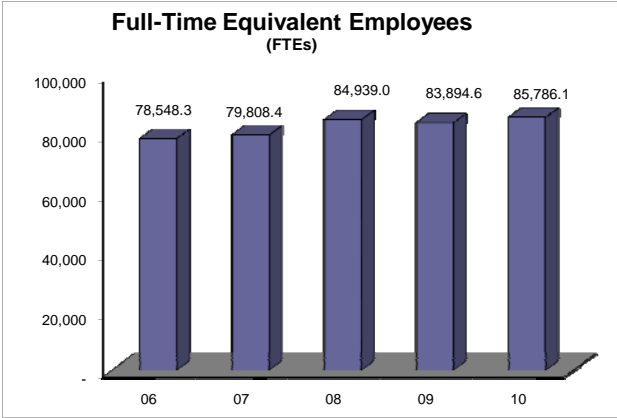
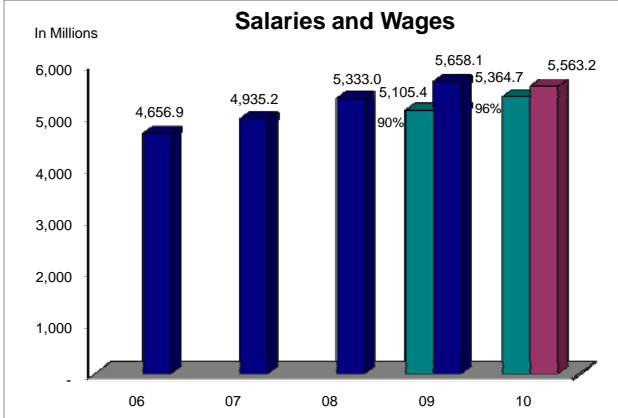
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| | |
|--|--|
|  | Actual Annual Amounts (SOURCE: Annual Financial Reports) |
|  | Adjustment to Actual Annual Amounts to exclude the Increase in Net OPEB Obligation (SOURCE: Annual Financial Reports) |
|  | Budget amounts (SOURCE: Operating Budget Summary) |
|  | Projected Amounts based on the average change of the previous three years of data |
|  | Monthly Financial Report Year-to-Date Amounts |
|  | Annual State Net Revenue Collections (SOURCE: Texas Revenue History by Source and Texas Net Revenue by Source, State Comptroller's Office) |
|  | Year-to-Date State Net Revenue Collections (SOURCE: State Comptroller's Office) |
|  | Estimated State Revenue Collections (SOURCE: Biennial Revenue Estimate, State Comptroller's Office) |
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|  | Year-to-Date Margin (SOURCE: Monthly Financial Report) |
|  | Projected Amounts based on Monthly Financial Report |
|  | Year-to-Date Margin (SOURCE: Monthly Financial Report) |
|  | Target Normalized Rates |
|  | Aaa/Aa1 Median (SOURCE: Moody's) |
|  | A2 Median (SOURCE: Moody's) |
|  | Good Facilities Condition Index (Below 5%) |
|  | Fair Facilities Condition Index (5% - 10%) |

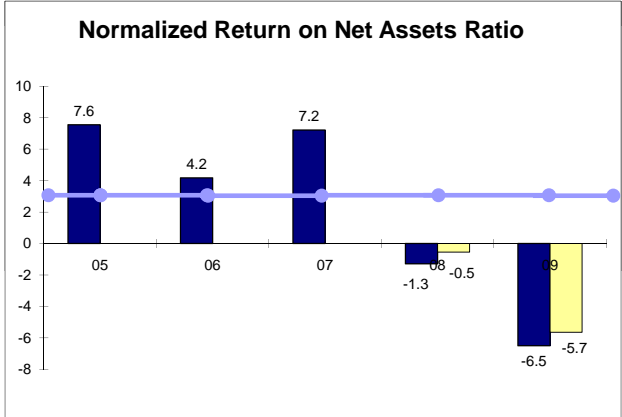
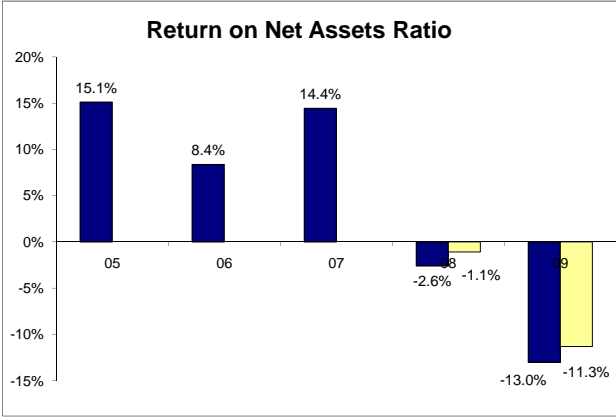
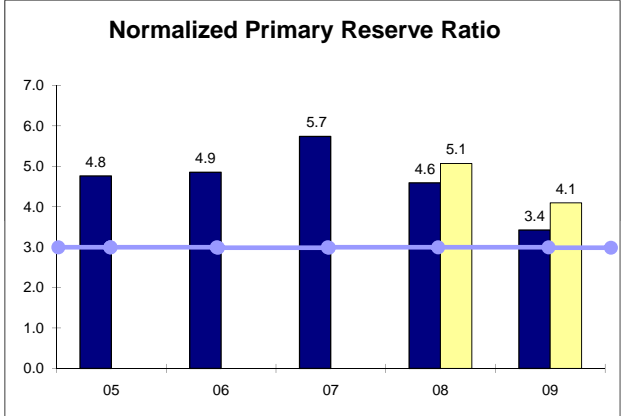
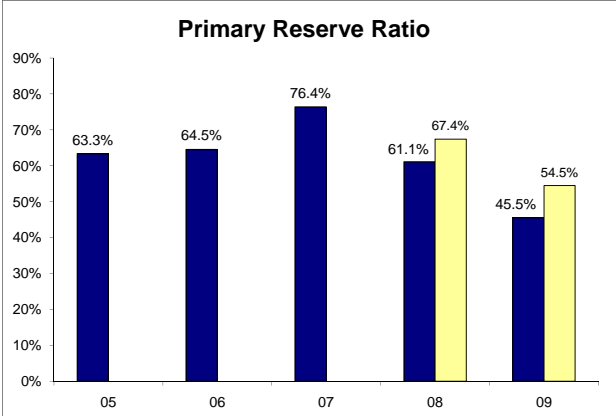
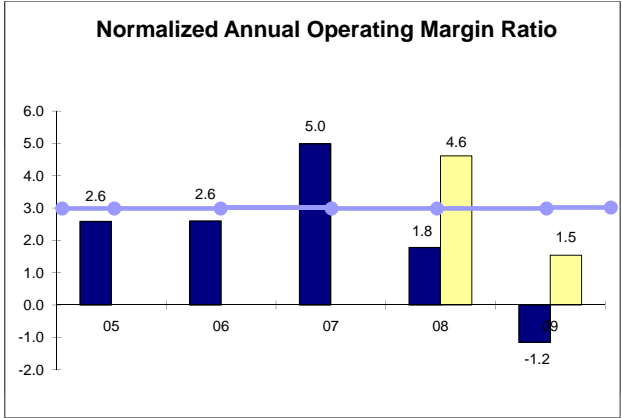
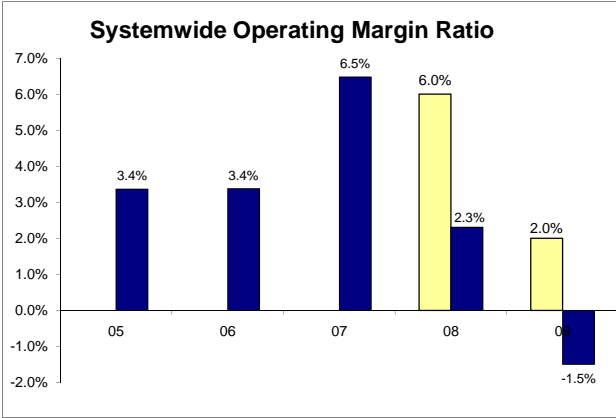
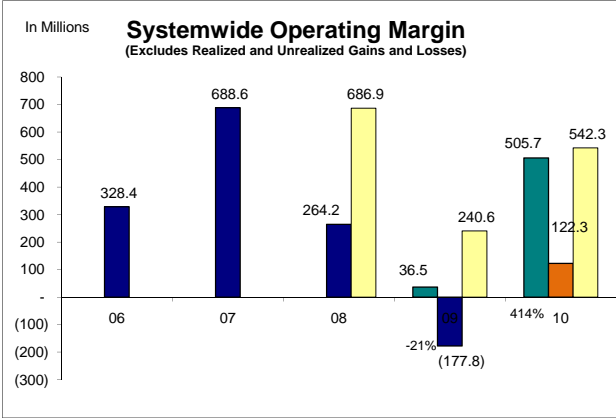
**KEY INDICATORS OF REVENUES
ACTUAL 2006 THROUGH 2009
PROJECTED 2010
YEAR-TO-DATE 2009 AND 2010 FROM JULY MONTHLY FINANCIAL REPORT**



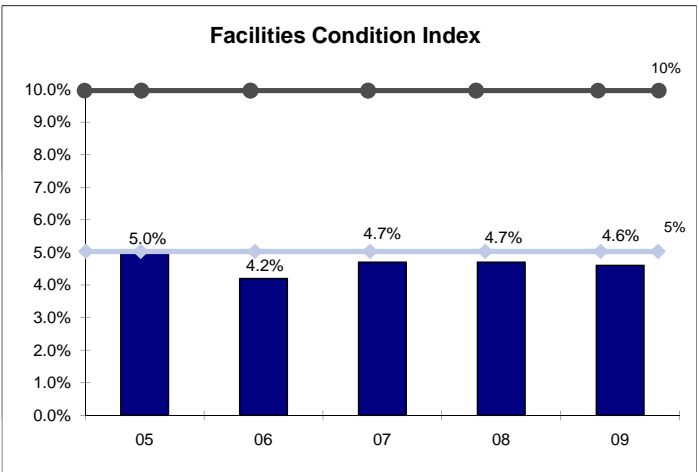
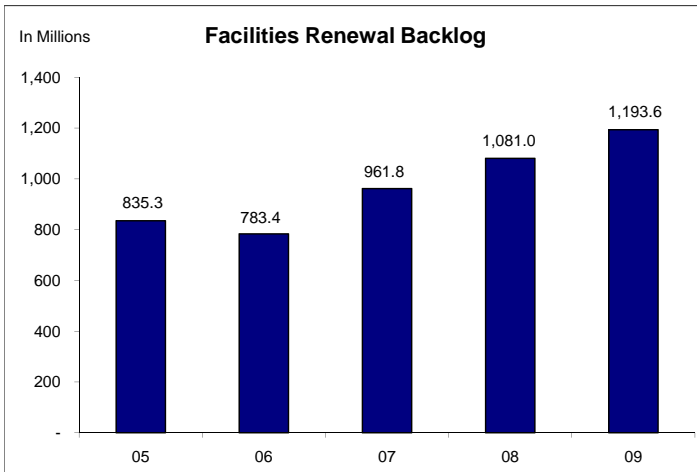
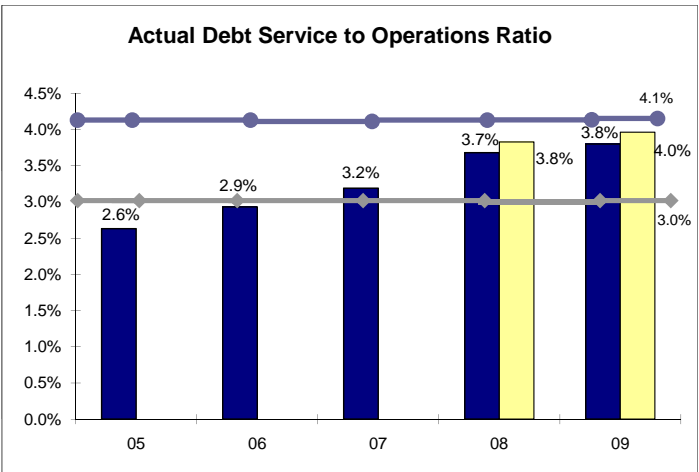
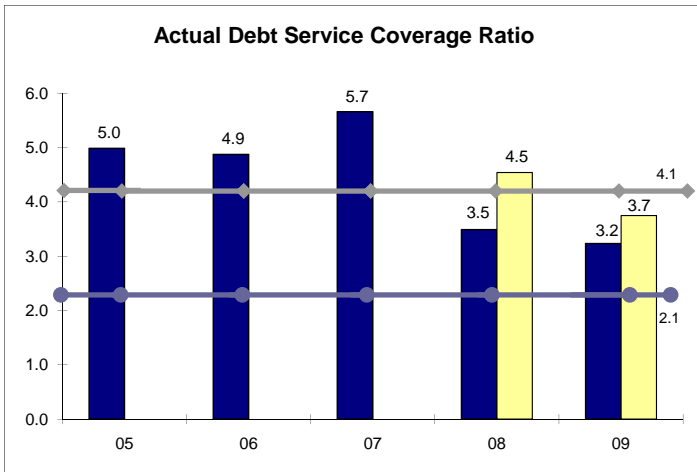
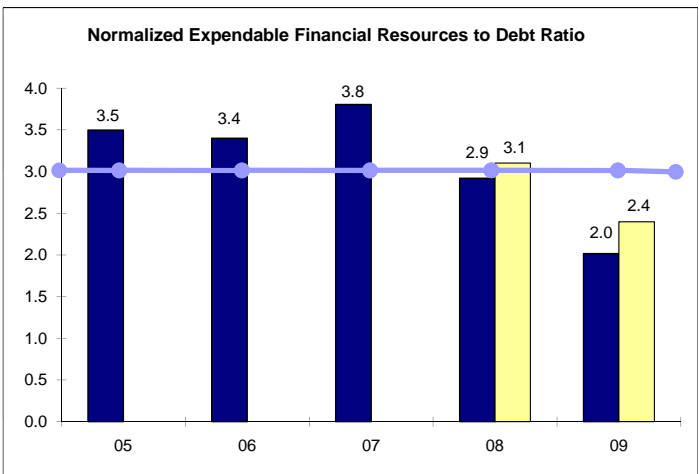
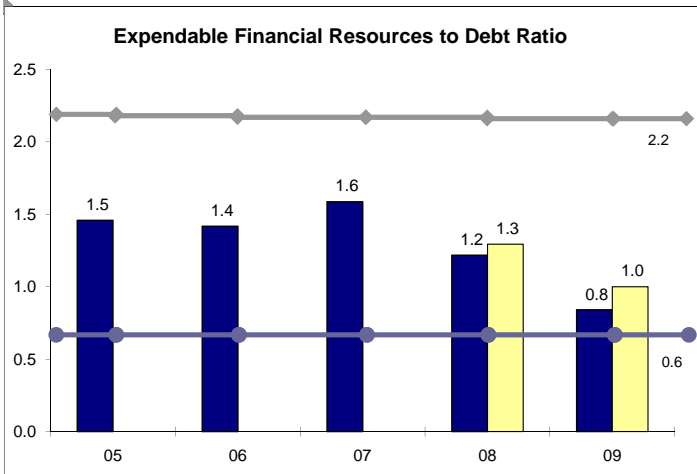
**KEY INDICATORS OF EXPENSES
ACTUAL 2006 THROUGH 2009
PROJECTED 2010
YEAR-TO-DATE 2009 AND 2010 FROM JULY MONTHLY FINANCIAL REPORT**



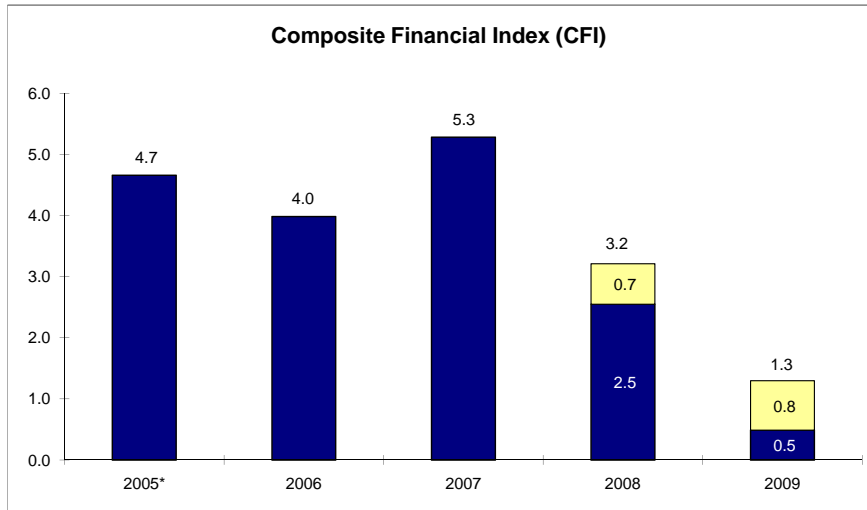
**KEY INDICATORS OF RESERVES
ACTUAL 2005 THROUGH 2009
PROJECTED 2010
YEAR-TO-DATE 2009 AND 2010 FROM JULY MONTHLY FINANCIAL REPORT**



KEY INDICATORS OF CAPITAL NEEDS AND CAPACITY 2005 THROUGH 2009

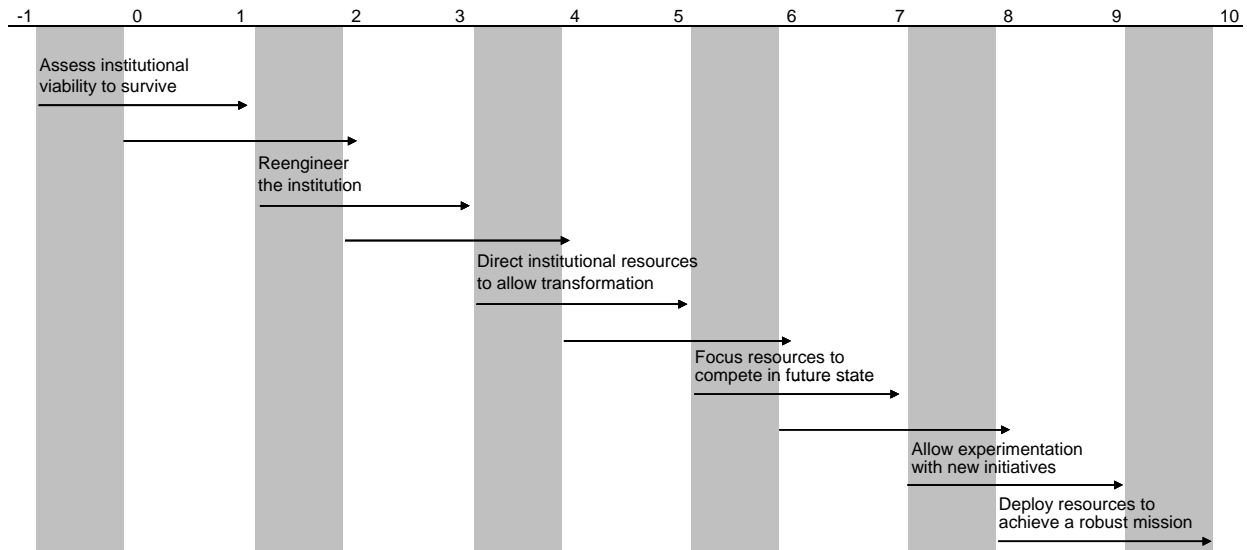


KEY INDICATORS OF FINANCIAL HEALTH 2005 THROUGH 2009



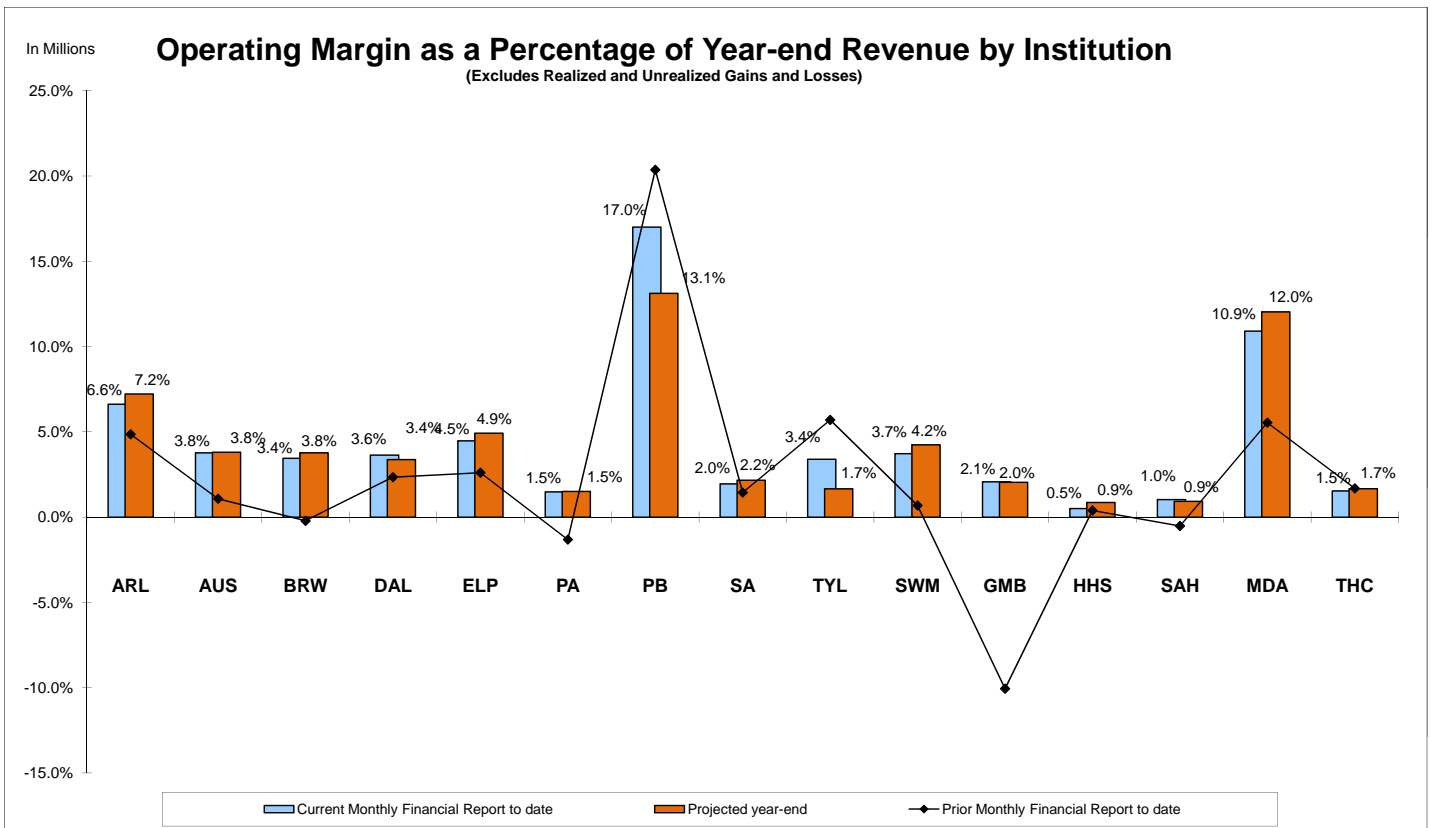
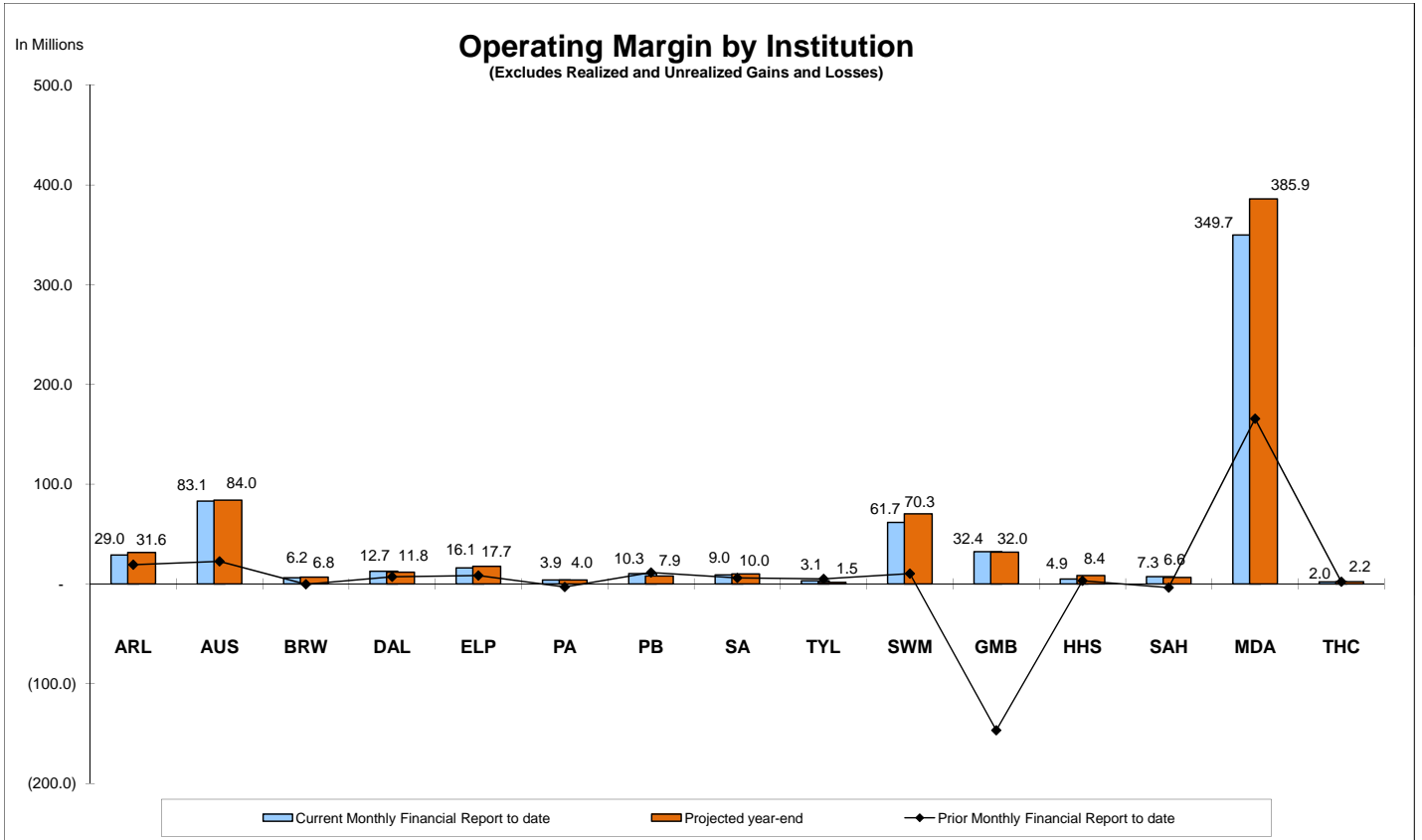
*Restated to reflect appreciation on endowments as restricted expendable net assets as a result of the 2006 external audit

Scale for Charting CFI Performance



KEY INDICATORS OF RESERVES

YEAR-TO-DATE 2009 AND 2010 FROM JULY MONTHLY FINANCIAL REPORT PROJECTED 2010 YEAR-END MARGIN



3. **U. T. System: Overview of U. T. System debt programs**

REPORT

Mr. Philip Aldridge, Vice Chancellor for Finance and Business Development, will provide an update on the status of the U. T. System debt programs using a PowerPoint presentation on Pages 118 - 137.

Overview of U. T. System Debt Programs

Philip Aldridge

Vice Chancellor for Finance and Business Development

U. T. System Board of Regents' Meeting

Finance and Planning Committee

November 2010



U. T. System Office of Finance

- The Office of Finance has eight professionals working in the following areas:
 - Debt Management
 - Technology Commercialization
 - Investment Oversight
 - Cash Management/Banking
 - Business Development



U. T. System Debt Team

- The Office of Finance staff works with various outside experts on each debt transaction:
 - External bond counsel
 - Investment banks (bond underwriters)
 - Underwriters' counsel
 - Credit rating agencies
 - Paying agent, escrow agent, verification agent, printer, etc.
- The Office of Finance does not utilize a financial advisor
- The Office of Finance does not utilize an arbitrage consultant



Summary of U. T. Debt Programs

- The U. T. System is authorized to issue debt under two primary programs:
 - The Revenue Financing System (RFS)
 - The Permanent University Fund (PUF)
- All debt is issued centrally by the Office of Finance in the name of the Board of Regents of the U. T. System, which approves:
 - All projects greater than \$4 million and any debt-financed project
 - Final Design and Development, including funding sources
 - The issuance of debt and underlying bond resolution
- Capital projects are approved by the Texas Higher Education Coordinating Board. The Bond Review Board and Attorney General review and approve bond issuances



Revenue Financing System

- The RFS is a cost-effective debt program secured by a systemwide pledge of all legally available revenues for debt issued on behalf of all 15 institutions and System Administration
 - Currently, the weighted average yield on the long-term RFS debt is 3.55%
 - As of October 19, 2010, the weighted average yield on the RFS Commercial Paper is 0.28%
- RFS debt has the highest possible credit ratings of Aaa, AAA, and AAA by Moody's, Standard & Poor's, and Fitch, respectively
- As of November 1, 2010, there was \$5.65 billion of RFS debt outstanding, including \$1.08 billion of Tuition Revenue Bonds (TRB).



Tuition Revenue Bonds

- TRBs are specifically authorized by the Legislature in Chapter 55 of the *Texas Education Code*
- TRBs are issued under the RFS program and are secured by the same pledge of legally available revenues of the U. T. System
- While not a legal obligation, the State of Texas has been reimbursing higher education institutions for TRB debt service since 1971
- Despite the name, TRB debt service is not directly related to tuition, and an institution need not have tuition revenue to receive TRBs
- Actual TRB debt service is \$115.5 million in fiscal year 2012 and 2013 (\$231 million for the biennium) excluding authorized but unissued TRBs



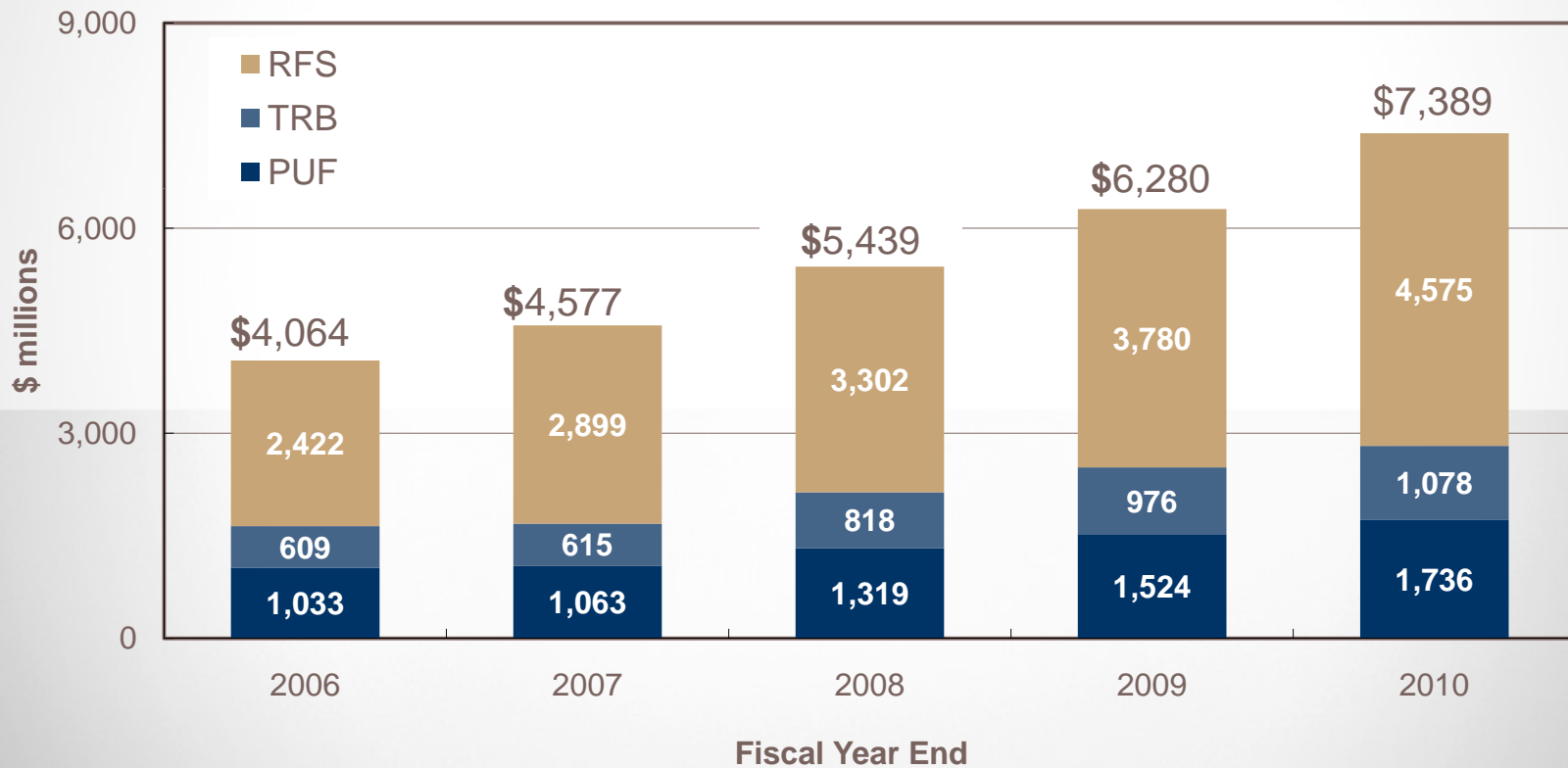
Permanent University Fund Financing Program

- The PUF debt program is used to fund projects at 13 of the 15 U. T. System institutions and System Administration. PUF debt is secured by distributions from the PUF to the Available University Fund (AUF)
- Per the Texas Constitution, PUF debt cannot be used for student housing, intercollegiate athletics, or auxiliary enterprises
- PUF debt has the highest possible credit ratings of Aaa, AAA, and AAA by Moody's, Standard and Poor's and Fitch, respectively
- As of November 1, 2010, \$1.74 billion of PUF debt was outstanding
 - Currently, the weighted averaged yield on long-term PUF debt is 3.94%
 - As of October 19, 2010, the weighted average yield on PUF Commercial Paper is 0.25%



U. T. System Debt Outstanding has Grown 82% in Four Years

U. T. System Debt Outstanding

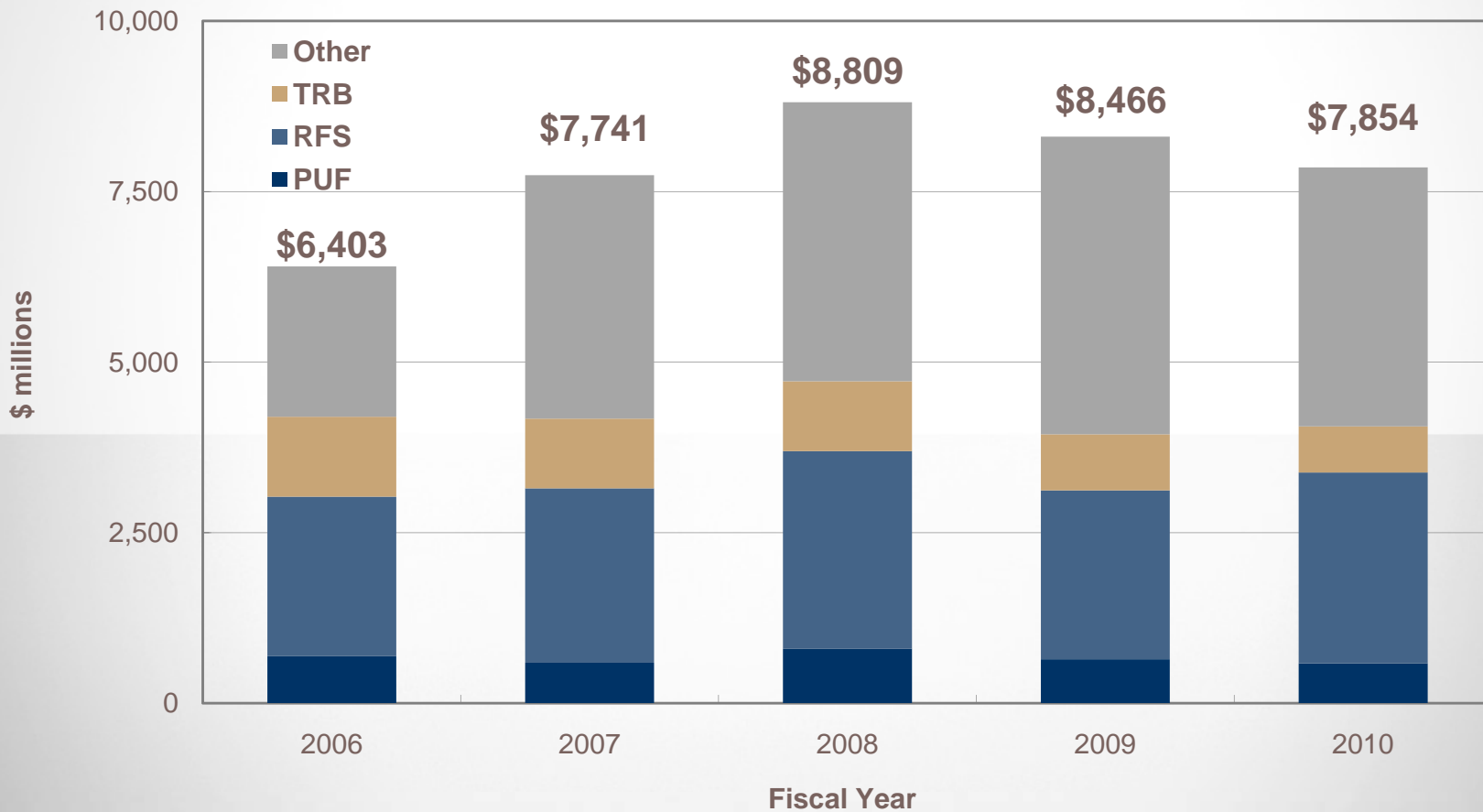


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Capital Improvement Program (CIP)

Six-Year CIP



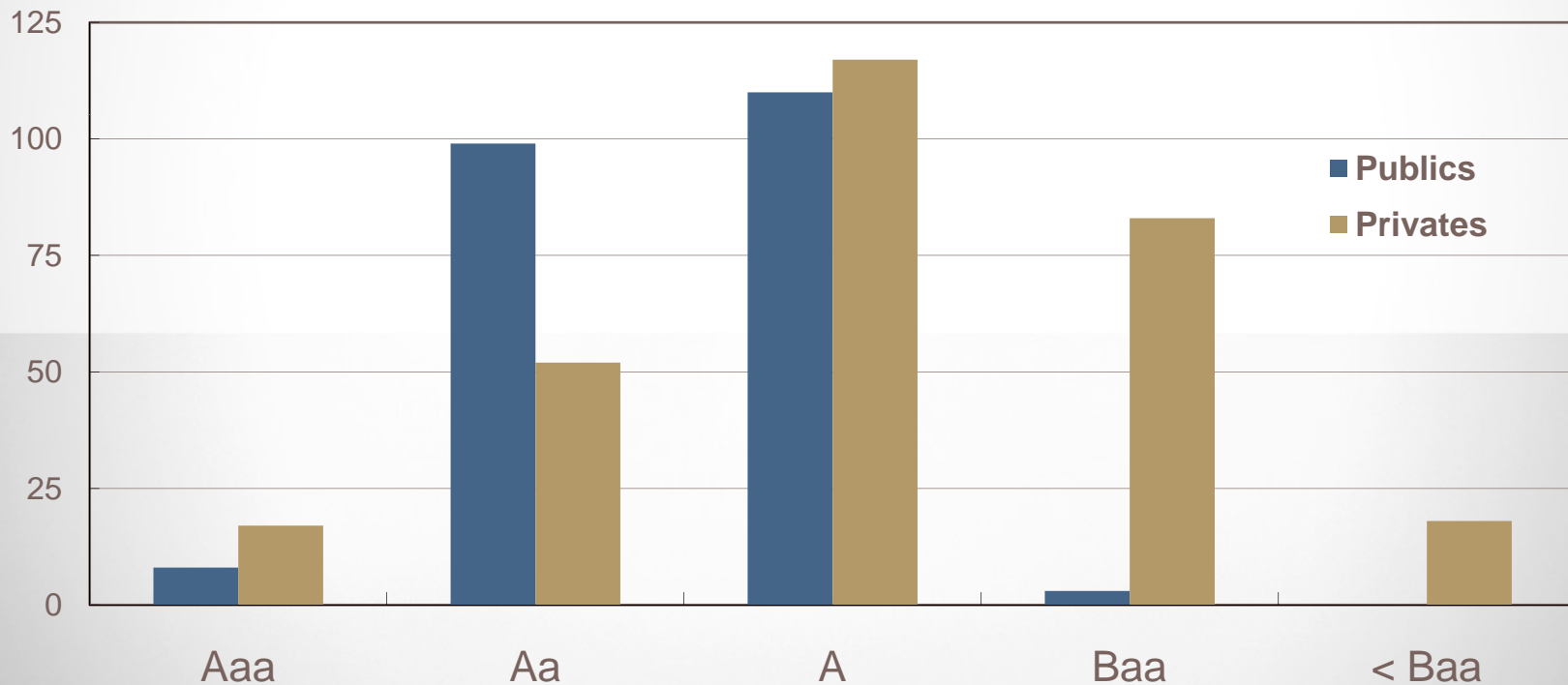
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Distribution of Moody's Higher Education Ratings

- Due to a ratings recalibration in 2010, eight public higher education issuers are now rated Aaa by Moody's Investors Service

Moody's Public Higher Education Ratings



SOURCE: Moody's FY09 Public College & University Medians (pub. Aug. 2010) and Moody's FY09 Private College & University Medians (pub. July 2010)



U. T. System Credit Strengths

- The U. T. System's credit rating is supported by a number of factors:
 - Strong cash flow generation
 - Strong balance sheet with more than \$36 billion of assets and \$24 billion of net assets (i.e., book equity)
 - Substantial liquidity to support variable rate debt programs
 - Conservative debt profile
 - Diversified revenue sources
 - Growing enrollment and research funding
 - Strong private sector support
 - Strong management team (per rating agencies)
 - Industry leading disclosure practices



Strong Operating Performance

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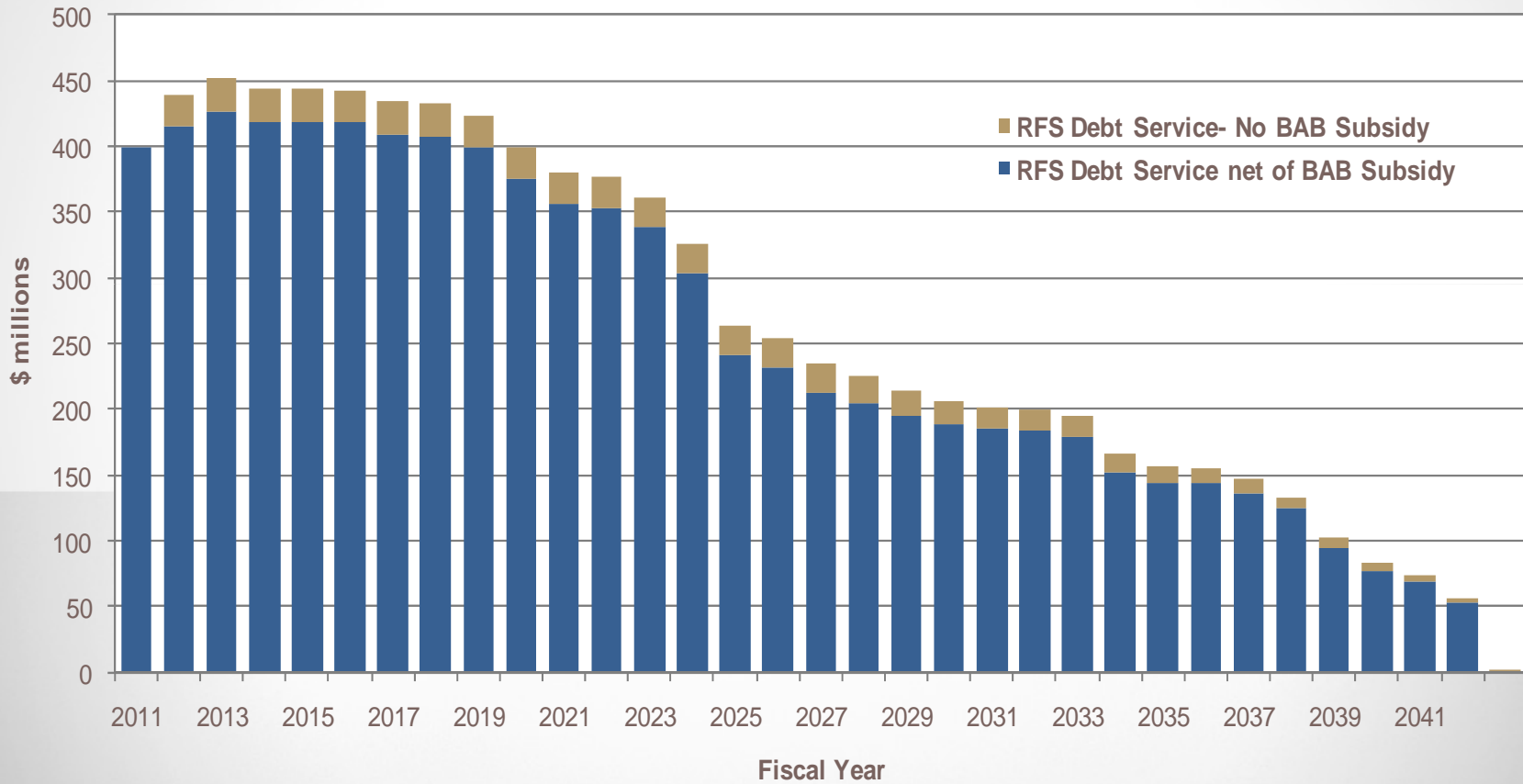
| \$ millions | FY 2010* | FY 2009 | FY 2008 | FY 2007 |
|---|------------|------------|------------|------------|
| Net operating results before depreciation/amortization and OPEB | \$ 1,206.3 | \$ 981.3 | \$ 1,366.7 | \$ 1,315.5 |
| Depreciation and amortization | (700.6) | (740.8) | (679.8) | (626.9) |
| Net OPEB expense ** | (454.7) | (418.3) | (422.7) | ----- |
| Net operating results | 50.7 | \$ (177.8) | \$ 264.2 | \$ 688.6 |

* As of July 31, 2010

** Other Post Employment Benefit Expense (OPEB) was first recorded in FY 2008 per GASB 45



RFS Debt Service Profile



NOTE: Includes all projected RFS debt service as of November 1st, except commercial paper notes.



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U. T. System Credit Challenges

- The U. T. System's credit profile is supported by variables that are unpredictable:
 - State support
 - Investment returns
 - Interest rates
 - Oil and gas prices
- The rating agencies cite more specific challenges for the System:
 - Large-scale capital program and associated future borrowing needs
 - Two years of investment losses (FY 2008 and FY 2009)
 - Concentration of operating revenues in volatile healthcare businesses
 - Relatively complex operations requiring skillful management, particularly in healthcare and research



Value of the AAA Ratings

- Lower cost of debt
 - Benefit of AAA rating relative to AA has historically averaged 0.10% to 0.20%, or several million dollars per year
- Value is maximized during periods of market distress
 - Inherent value in “natural” AAA vs. enhanced AAA
 - Continued market access and flight to quality
- Value of self-liquidity
 - Bank liquidity is expensive – recent indications in the 0.50%-0.75% range
 - Excluding trading advantage, self-liquidity saves over \$15 million annually
- Better terms on contracts
 - One-way swap collateral – U. T. System does not post collateral
 - Substantially similar documents among counterparties



RFS Debt Capacity

- The Master Resolution establishing the Revenue Financing System requires that before any RFS debt is issued, the Board make a determination (“Finding of Fact”) that:
 - The Board will have sufficient “Pledged Revenues” to meet all financial obligations relating to the Revenue Financing System, and;
 - The Members (i.e., institutions) on whose behalf the debt is issued possess the financial capacity to satisfy their direct obligations



RFS Institutional Debt Capacity

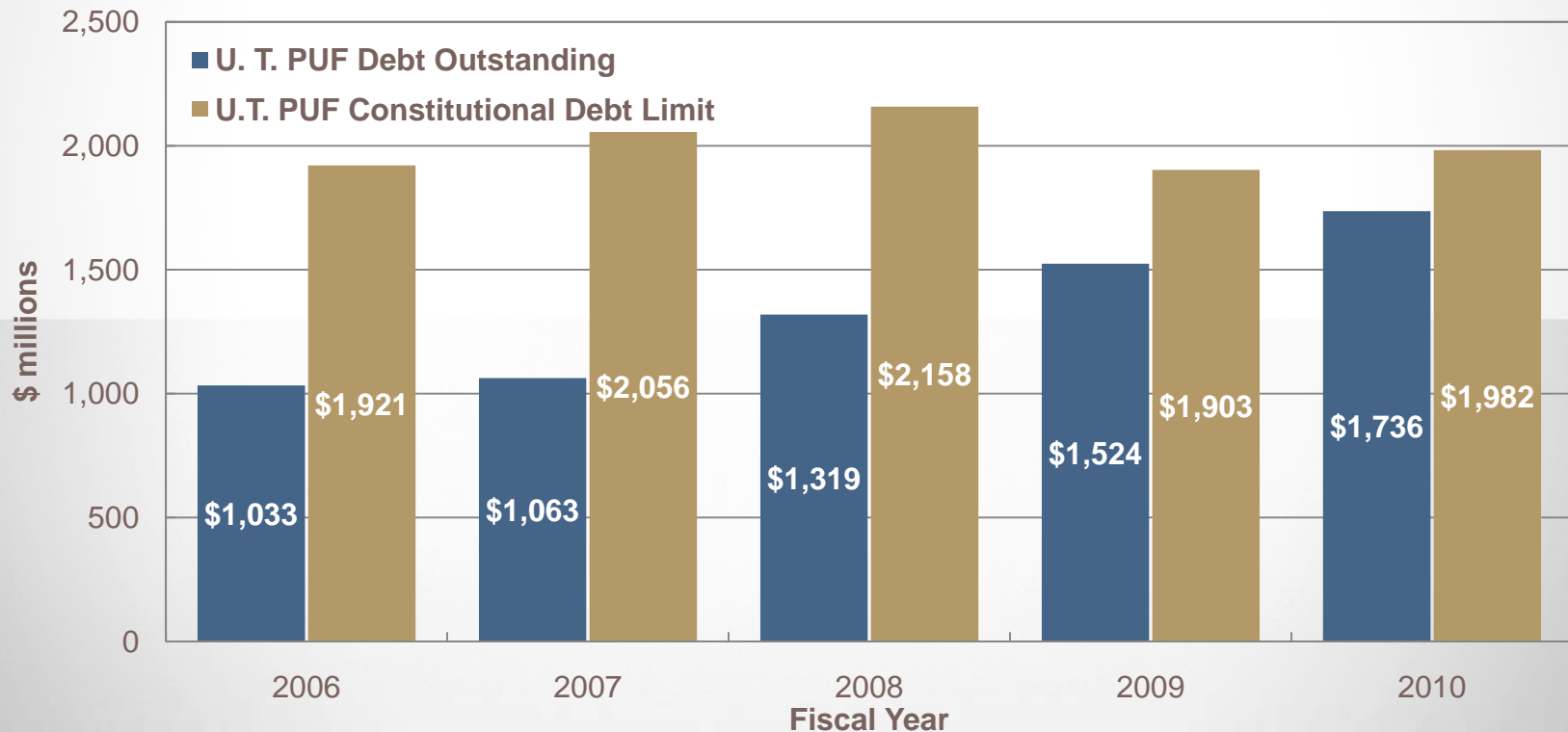
- Debt capacity is largely determined by an institution's ability to meet at least two of the following three standards:
 - Debt Service Coverage ratio of at least 1.8 times
 - Debt Service-to-Operations (Debt Burden) ratio less than 5.0%
 - Expendable Resources-to-Debt ratio of at least 0.8 times
- The minimum institutional standards approximate a low-investment grade credit rating consistent with Texas universities such as Midwestern State University, Stephen F. Austin State University, and Texas State Technical College System (rated A1 by Moody's)
- An institution with little debt capacity may be granted approval for debt on revenue-supporting projects



Constitutional Restriction on PUF Debt Issuance

- The Constitution limits the aggregate amount of PUF debt that may be issued by the U. T. Board of Regents to 20% of the cost value of PUF Investments

PUF Debt Outstanding and Constitutional Limit



U. T. System is a Low-Cost Issuer in Texas

| | The University of Texas System ¹ (\$/bond) | All Texas Bond Issuers ² (\$/bond) | All Texas Cities ³ (\$/bond) | All Texas Counties ³ (\$/bond) | All Texas School Districts ³ (\$/bond) | All Texas Community/ Jr. Coll. ³ (\$/bond) |
|-----------------------|--|--|--|--|--|--|
| Underwriter's Spread | \$4.85 | \$6.07 | \$10.29 | \$10.08 | \$9.04 | \$8.13 |
| Other Issuance Costs: | | | | | | |
| Bond Counsel | 0.41 | 0.93 | | | | |
| Financial Advisor | 0.00 | 0.61 | | | | |
| Rating Agencies | 0.33 | 0.64 | | | | |
| Printing | 0.01 | 0.04 | | | | |
| Other | 0.16 | 0.65 | | | | |
| Subtotal | 0.91 | 2.87 | 14.20 | 8.77 | 8.54 | 5.44 |
| Total Cost per Bond | \$5.76 | \$8.94 | \$24.49 | \$18.85 | \$17.58 | \$13.57 |
| Average Issue Size | \$258 million | \$190 million | \$20 million | \$36 million | \$30 million | \$35 million |

¹Represents U.T. System TRB 2008A and RFS 2009D, both traditional fixed-rate bond issues.
²Source: Texas Bond Review Board FY 2009 Annual Report.
³Source: Texas Bond Review Board FY 2008 Local Government Report.



Strategic Themes for Debt Programs

- Decline in funding availability
 - Temporary?
 - Limited funding available for TRBs and PUF debt
- Persistently low interest rates
 - Record low short-term interest rates
 - “Build America Bonds”
- Taking care of the fundamentals
 - Retain good people
 - Effectively manage large debt and swap portfolios consistent with Board policies and expectations
 - Continue to hold down debt costs



4. U. T. System Board of Regents: The University of Texas Investment Management Company (UTIMCO) Performance Summary Report and Investment Reports for the fiscal year and quarter ended August 31, 2010

REPORT

The August 31, 2010 UTIMCO Performance Summary Report is attached on Page 139.

The Investment Reports for the fiscal year and quarter ended August 31, 2010, are set forth on Pages 140 - 143.

Item I on Page 140 reports activity for the Permanent University Fund (PUF) investments. The PUF's net investment return for the fiscal year was 13.04% versus its composite benchmark return of 8.76%. The PUF's net asset value increased by \$1,051 million since the beginning of the fiscal year to \$10,725 million. This change in net asset value includes contributions from PUF Land receipts, increases due to net investment return, and the annual distribution to the Available University Fund (AUF) of \$516 million.

Item II on Page 141 reports activity for the General Endowment Fund (GEF) investments. The GEF's net investment return for the fiscal year was 13.02% versus its composite benchmark return of 8.76%. The GEF's net asset value increased by \$676 million during the fiscal year to \$6,035 million.

Item III on Page 142 reports activity for the Intermediate Term Fund (ITF). The ITF's net investment return for the fiscal year was 11.04% versus its composite benchmark return of 6.05%. The net asset value increased during the fiscal year to \$4,156 million due to net investment return of \$406 million, net contributions of \$297 million, less distributions of \$119 million.

For all funds, all exposures were within their asset class and investment type ranges and liquidity were within policy.

Item IV on Page 143 presents book and market values of cash, debt, equity, and other securities held in funds outside of internal investment pools. Total cash and equivalents, consisting primarily of institutional operating funds held in the Dreyfus money market fund, increased by \$116 million to \$1,990 million during the three months since the last reporting period. Market values for the remaining asset types were debt securities: \$24 million versus \$24 million at the beginning of the period; equities: \$43 million versus \$43 million at the beginning of the period; and other investments: \$7 million versus \$2 million at the beginning of the period.

UTIMCO Performance Summary

August 31, 2010

| | Net Asset Value 8/31/2010 (in Millions) | Periods Ended August 31, 2010 (Returns for Periods Longer Than One Year are Annualized) | | | | | | | |
|-------------------------------------|--|--|--------------|---------------------|---------------|-------------------------|-----------------|-----------------|-----------------|
| | | <u>Short Term</u> | | <u>Year to Date</u> | | <u>Historic Returns</u> | | | |
| | | 1 Mo | 3 Mos | Fiscal | Calendar | 1 Yr | 3 Yrs | 5 Yrs | 10 Yrs |
| ENDOWMENT FUNDS | | | | | | | | | |
| Permanent University Fund | \$ 10,725 | 0.21% | 2.47% | 13.04% | 3.97% | 13.04% | (1.66%) | 4.04% | 4.65% |
| General Endowment Fund | | 0.20 | 2.48 | 13.02 | 3.96 | 13.02 | (1.68) | 4.12 | N/A |
| Permanent Health Fund | 906 | 0.18 | 2.44 | 12.91 | 3.94 | 12.91 | (1.74) | 4.05 | N/A |
| Long Term Fund | 5,130 | 0.18 | 2.45 | 12.90 | 3.95 | 12.90 | (1.74) | 4.05 | 4.73 |
| Separately Invested Funds | 396 | N/A | N/A | N/A | N/A | N/A | N/A | N/A | N/A |
| Total Endowment Funds | 17,157 | | | | | | | | |
| OPERATING FUNDS | | | | | | | | | |
| Short Term Fund | 1,667 | 0.03 | 0.08 | 0.22 | 0.15 | 0.22 | 1.79 | 3.06 | 2.80 |
| Intermediate Term Fund | 4,156 | 0.72 | 3.79 | 11.04 | 3.65 | 11.04 | 0.82 | N/A | N/A |
| Total Operating Funds | 5,823 | | | | | | | | |
| Total Investments | \$ 22,980 | | | | | | | | |
| VALUE ADDED (Percent) | | | | | | | | | |
| Permanent University Fund | | 0.94% | (0.18%) | 4.28% | 2.51% | 4.28% | 2.80% | 1.89% | 1.95% |
| General Endowment Fund | | 0.93 | (0.17) | 4.26 | 2.50 | 4.26 | 2.78 | 1.97 | N/A |
| Short Term Fund | | 0.02 | 0.04 | 0.08 | 0.07 | 0.08 | 0.53 | 0.39 | 0.20 |
| Intermediate Term Fund | | 1.00 | 0.50 | 4.99 | 3.22 | 4.99 | 2.87 | N/A | N/A |
| VALUE ADDED (\$ IN MILLIONS) | | | | | | | | | |
| Permanent University Fund | | \$101 | \$(19) | \$410 | \$261 | \$410 | \$908 | \$959 | \$1,961 |
| General Endowment Fund | | 57 | (10) | 230 | 146 | 230 | 508 | 561 | N/A |
| Intermediate Term Fund | | 41 | 20 | 186 | 129 | 186 | 334 | N/A | N/A |
| Total Value Added | | \$ 199 | \$(9) | \$ 826 | \$ 536 | \$ 826 | \$ 1,750 | \$ 1,520 | \$ 1,961 |

Footnotes available upon request.

I. PERMANENT UNIVERSITY FUND

Investment Reports for Periods Ended August 31, 2010

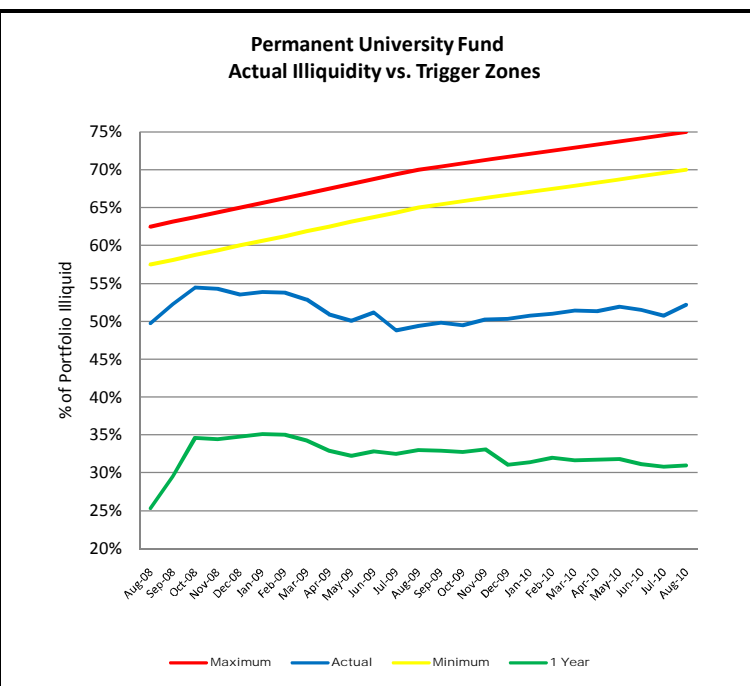
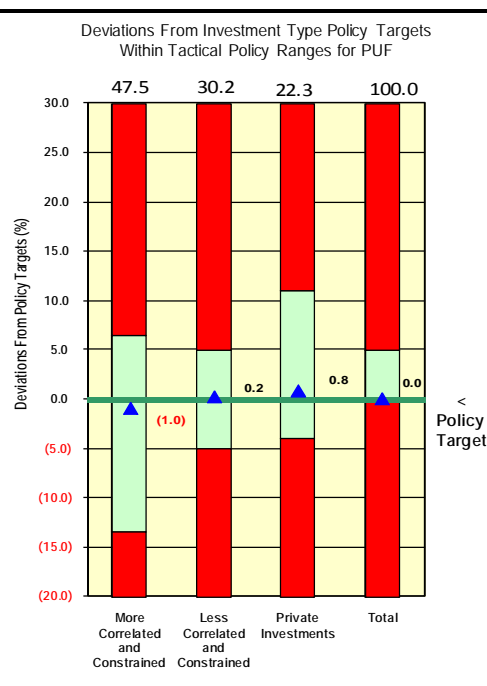
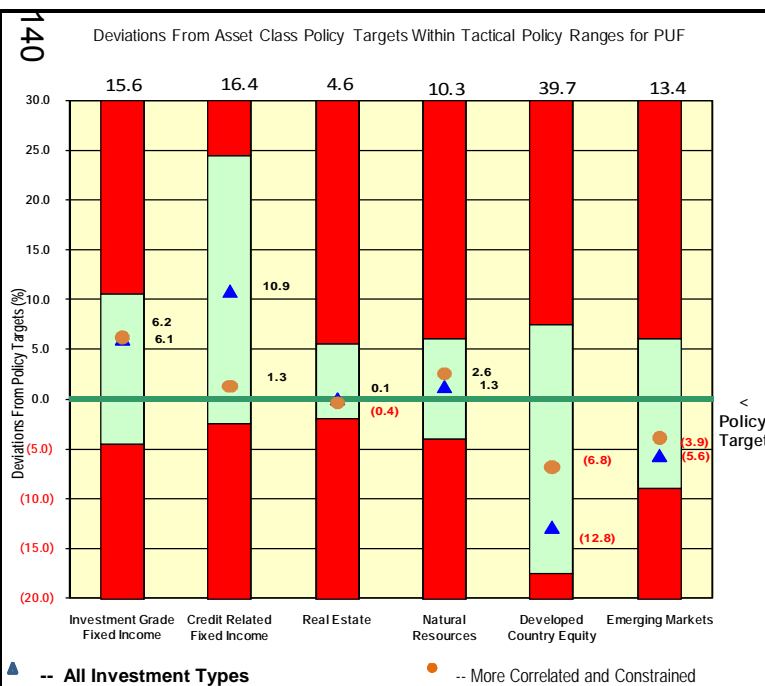
Prepared in accordance with Texas Education Code Sec. 51.0032

Summary of Capital Flows

| (\$ millions) | Fiscal Year Ended August 31, 2009 | Quarter Ended August 31, 2010 | Fiscal Year Ended August 31, 2010 |
|-------------------------------------|--------------------------------------|----------------------------------|--------------------------------------|
| Beginning Net Assets | \$ 11,360 | \$ 10,524 | \$ 9,674 |
| PUF Lands Receipts | 340 | 75 | 338 |
| Investment Return (Net of Expenses) | (1,495) | 255 | 1,229 |
| Distributions to AUF | (531) | (129) | (516) |
| Ending Net Assets | <u>\$ 9,674</u> | <u>\$ 10,725</u> | <u>\$ 10,725</u> |

Fiscal Year to Date

| | Returns | | Value Added | | |
|--|---------------|------------------|-----------------------|-------------------------|---------------|
| | Portfolio | Policy Benchmark | From Asset Allocation | From Security Selection | Total |
| More Correlated and Constrained: | | | | | |
| Investment Grade | 6.39% | 5.84% | -0.10% | 0.05% | -0.05% |
| Credit-Related | 44.36% | 20.86% | 0.47% | 0.07% | 0.54% |
| Real Estate | 16.66% | 15.11% | -0.09% | 0.08% | -0.01% |
| Natural Resources | 12.87% | 2.78% | 0.01% | 0.56% | 0.57% |
| Developed Country | 7.13% | 1.54% | 0.07% | 1.07% | 1.14% |
| Emerging Markets | 19.39% | 18.02% | -0.24% | 0.15% | -0.09% |
| Total More Correlated and Constrained | 12.18% | 7.87% | 0.12% | 1.98% | 2.10% |
| Less Correlated and Constrained | 11.89% | 2.89% | 0.32% | 2.44% | 2.76% |
| Private Investments | 16.37% | 19.19% | 0.29% | -0.87% | -0.58% |
| Total | 13.04% | 8.76% | 0.73% | 3.55% | 4.28% |



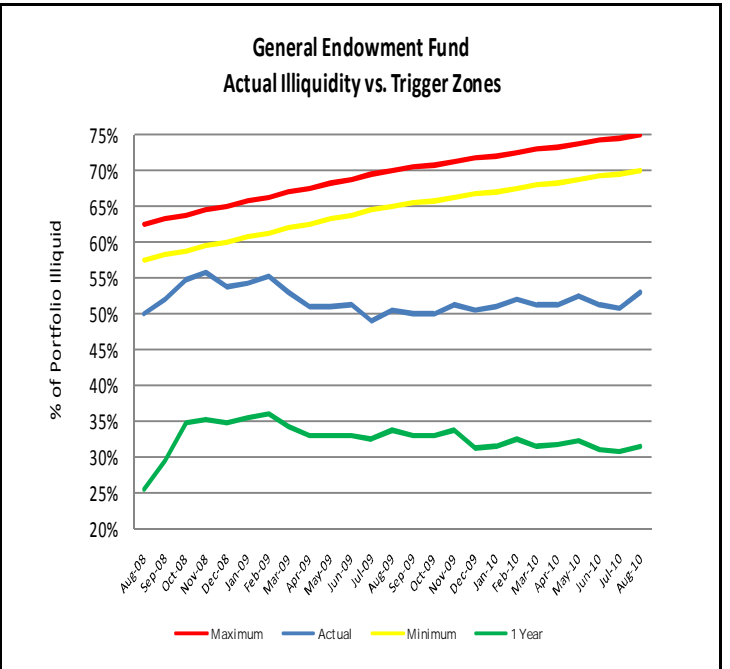
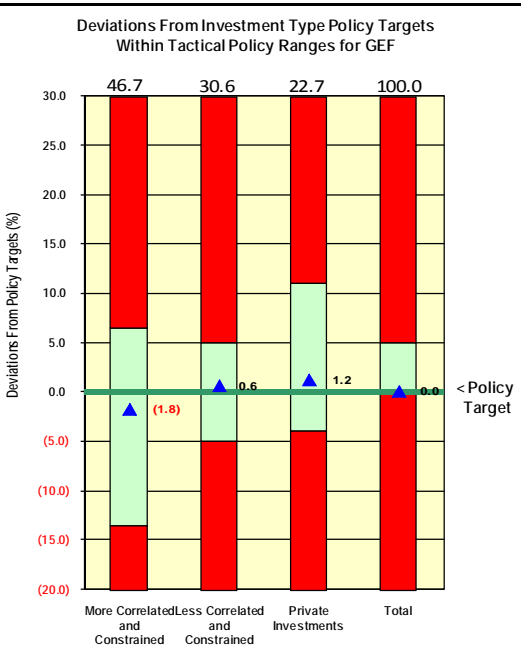
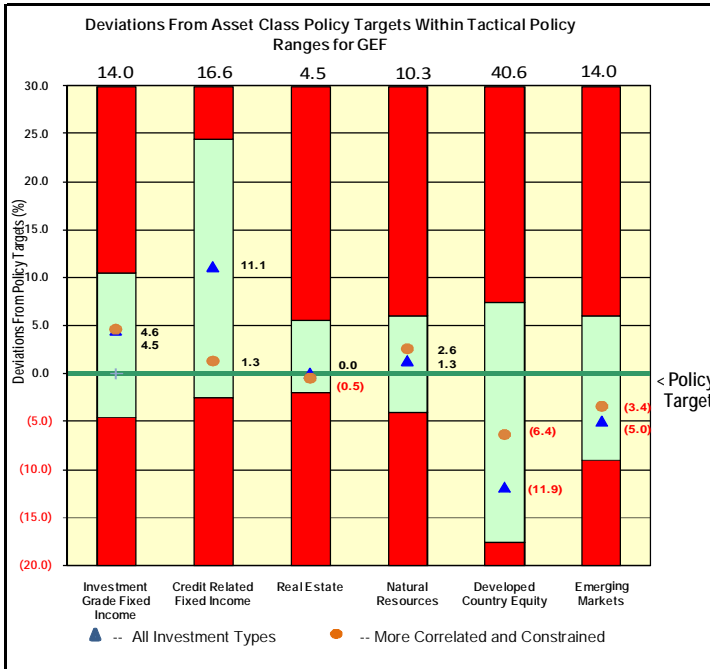
II. GENERAL ENDOWMENT FUND Investment Reports for Periods Ended August 31, 2010

Prepared in accordance with *Texas Education Code Sec. 51.0032*

| Summary of Capital Flows | | | |
|-------------------------------------|--------------------------------------|----------------------------------|--------------------------------------|
| (\$ millions) | Fiscal Year Ended August 31, 2009 | Quarter Ended August 31, 2010 | Fiscal Year Ended August 31, 2010 |
| Beginning Net Assets | \$ 6,310 | \$ 5,873 | \$ 5,359 |
| Contributions | 185 | 98 | 285 |
| Withdrawals | (11) | (7) | (11) |
| Distributions | (279) | (76) | (298) |
| Investment Return (Net of Expenses) | (846) | 147 | 700 |
| Ending Net Assets | <u>\$ 5,359</u> | <u>\$ 6,035</u> | <u>\$ 6,035</u> |

| | Returns | | Fiscal Year to Date | | |
|--|---------------|------------------|-----------------------|-------------------------|----------------------|
| | Portfolio | Policy Benchmark | From Asset Allocation | From Security Selection | Value Added Total |
| More Correlated and Constrained: | | | | | |
| Investment Grade | 6.29% | 5.84% | -0.14% | 0.04% | -0.10% |
| Credit-Related | 44.34% | 20.86% | 0.45% | 0.07% | 0.52% |
| Real Estate | 16.71% | 15.11% | -0.09% | 0.08% | -0.01% |
| Natural Resources | 12.82% | 2.78% | 0.00% | 0.55% | 0.55% |
| Developed Country | 7.08% | 1.54% | 0.10% | 1.07% | 1.17% |
| Emerging Markets | 19.11% | 18.02% | -0.26% | 0.15% | -0.11% |
| Total More Correlated and Constrained | 12.05% | 7.87% | 0.06% | 1.96% | 2.02% |
| Less Correlated and Constrained | 11.89% | 2.89% | 0.35% | 2.47% | 2.82% |
| Private Investments | 16.40% | 19.19% | 0.29% | -0.87% | -0.58% |
| Total | 13.02% | 8.76% | 0.70% | 3.56% | 4.26% |

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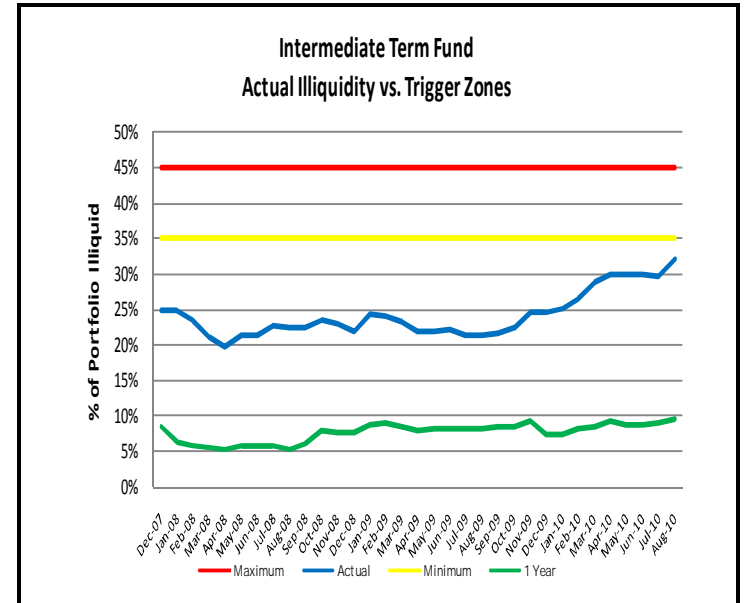
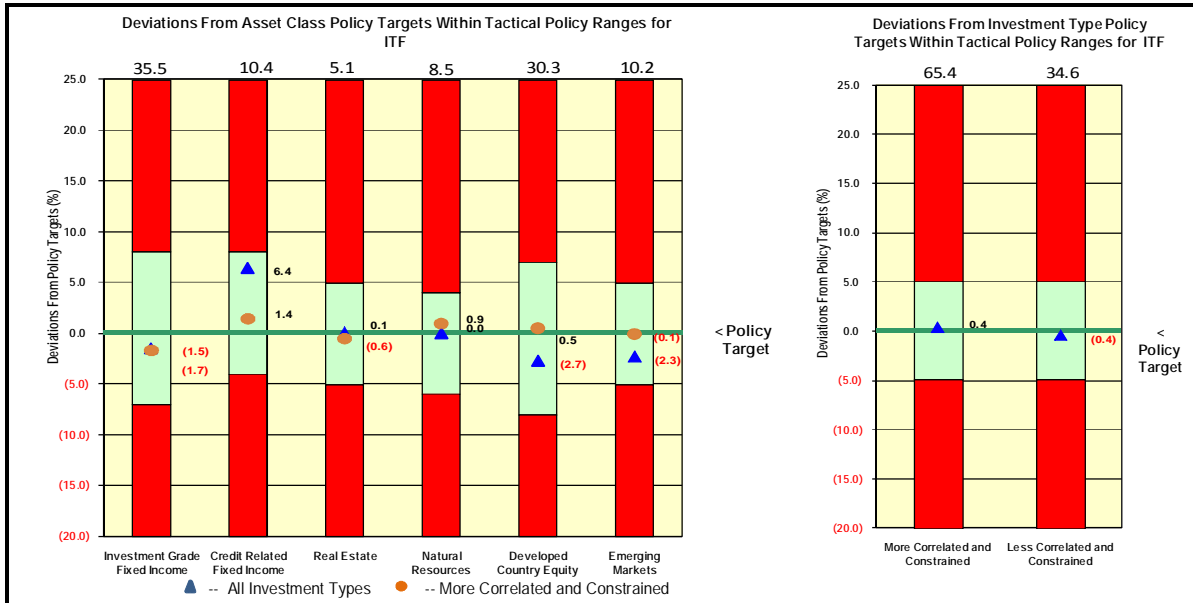


III. INTERMEDIATE TERM FUND Investment Reports for Periods Ended August 31, 2010

Prepared in accordance with Texas Education Code Sec. 51.0032

| Summary of Capital Flows | | | |
|-------------------------------------|--------------------------------------|----------------------------------|--------------------------------------|
| (\$ millions) | Fiscal Year Ended August 31, 2009 | Quarter Ended August 31, 2010 | Fiscal Year Ended August 31, 2010 |
| Beginning Net Assets | \$ 3,875 | \$ 4,035 | \$ 3,572 |
| Contributions | 251 | 35 | 409 |
| Withdrawals | (178) | (36) | (112) |
| Distributions | (98) | (31) | (119) |
| Investment Return (Net of Expenses) | (278) | 153 | 406 |
| Ending Net Assets | \$ 3,572 | \$ 4,156 | \$ 4,156 |

| | Returns | | Fiscal Year to Date | | |
|--|---------------|------------------|-----------------------|-------------------------|--------------|
| | Portfolio | Policy Benchmark | From Asset Allocation | From Security Selection | Total |
| More Correlated and Constrained: | | | | | |
| Investment Grade | 8.10% | 5.84% | -0.21% | 0.77% | 0.56% |
| Credit-Related | 43.13% | 20.86% | 0.33% | 0.18% | 0.51% |
| Real Estate | 17.27% | 15.11% | -0.34% | 0.18% | -0.16% |
| Natural Resources | 11.82% | 2.78% | 0.12% | 0.61% | 0.73% |
| Developed Country | 7.53% | 1.54% | -0.19% | 0.81% | 0.62% |
| Emerging Markets | 19.58% | 18.02% | 0.00% | 0.10% | 0.10% |
| Total More Correlated and Constrained | 10.81% | 7.42% | -0.29% | 2.65% | 2.36% |
| Less Correlated and Constrained | 11.89% | 2.89% | 0.25% | 2.38% | 2.63% |
| Private Investments | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Total | 11.04% | 6.05% | -0.04% | 5.03% | 4.99% |



IV. SEPARATELY INVESTED ASSETS
Summary Investment Report at August 31, 2010
 Report prepared in accordance with *Texas Education Code Sec. 51.0032*

| ASSET TYPES | (\$ thousands) | | | | | | | | | | | | | | | |
|--------------------------------|-------------------------------|--------|------------|--------|------------------------------|----------|--------------------------------|--------|--------------|---------|------------------------------------|---------|--------------------------------------|-----------|-----------|-----------|
| | FUND TYPE | | | | | | | | | | | | | | | |
| | CURRENT PURPOSE DESIGNATED | | RESTRICTED | | ENDOWMENT & SIMILAR FUNDS | | ANNUITY & LIFE INCOME FUNDS | | AGENCY FUNDS | | TOTAL EXCLUDING OPERATING FUNDS | | OPERATING FUNDS (SHORT TERM FUND) | | TOTAL | |
| | BOOK | MARKET | BOOK | MARKET | BOOK | MARKET | BOOK | MARKET | BOOK | MARKET | BOOK | MARKET | BOOK | MARKET | BOOK | MARKET |
| Cash & Equivalents: | | | | | | | | | | | | | | | | |
| Beginning value 05/31/10 | - | - | 1,658 | 1,658 | 95,463 | 95,463 | 1,311 | 1,311 | 4,787 | 4,787 | 103,219 | 103,219 | 1,770,640 | 1,770,640 | 1,873,859 | 1,873,859 |
| Increase/(Decrease) | - | - | 120 | 120 | (52,551) | (52,551) | (191) | (191) | 271,814 | 271,814 | 219,192 | 219,192 | (103,258) | (103,258) | 115,934 | 115,934 |
| Ending value 08/31/10 | - | - | 1,778 | 1,778 | 42,912 | 42,912 | 1,120 | 1,120 | 276,601 | 276,601 | 322,411 | 322,411 | 1,667,382 | 1,667,382 | 1,989,793 | 1,989,793 |
| Debt Securities: | | | | | | | | | | | | | | | | |
| Beginning value 05/31/10 | - | - | 301 | 300 | 11,716 | 12,831 | 10,555 | 11,116 | - | - | 22,572 | 24,247 | - | - | 22,572 | 24,247 |
| Increase/(Decrease) | - | - | 5 | 6 | (784) | (756) | (225) | 157 | - | - | (1,004) | (593) | - | - | (1,004) | (593) |
| Ending value 08/31/10 | - | - | 306 | 306 | 10,932 | 12,075 | 10,330 | 11,273 | - | - | 21,568 | 23,654 | - | - | 21,568 | 23,654 |
| Equity Securities: | | | | | | | | | | | | | | | | |
| Beginning value 05/31/10 | 17 | 3,952 | 387 | 345 | 29,344 | 27,729 | 12,908 | 10,881 | - | - | 42,656 | 42,907 | - | - | 42,656 | 42,907 |
| Increase/(Decrease) | 130 | (178) | 101 | 107 | 774 | 327 | (94) | 263 | - | - | 911 | 519 | - | - | 911 | 519 |
| Ending value 08/31/10 | 147 | 3,774 | 488 | 452 | 30,118 | 28,056 | 12,814 | 11,144 | - | - | 43,567 | 43,426 | - | - | 43,567 | 43,426 |
| Other: | | | | | | | | | | | | | | | | |
| Beginning value 05/31/10 | - | - | 393 | 393 | 2 | 2 | 370 | 137 | 1,640 | 1,640 | 2,405 | 2,172 | - | - | 2,405 | 2,172 |
| Increase/(Decrease) | - | - | 4,450 | 4,450 | (2) | (2) | 16 | - | 206 | 206 | 4,670 | 4,654 | - | - | 4,670 | 4,654 |
| Ending value 08/31/10 | - | - | 4,843 | 4,843 | - | - | 386 | 137 | 1,846 | 1,846 | 7,075 | 6,826 | - | - | 7,075 | 6,826 |
| Total Assets: | | | | | | | | | | | | | | | | |
| Beginning value 05/31/10 | 17 | 3,952 | 2,739 | 2,696 | 136,525 | 136,025 | 25,144 | 23,445 | 6,427 | 6,427 | 170,852 | 172,545 | 1,770,640 | 1,770,640 | 1,941,492 | 1,943,185 |
| Increase/(Decrease) | 130 | (178) | 4,676 | 4,683 | (52,563) | (52,982) | (494) | 229 | 272,020 | 272,020 | 223,769 | 223,772 | (103,258) | (103,258) | 120,511 | 120,514 |
| Ending value 08/31/10 | 147 | 3,774 | 7,415 | 7,379 | 83,962 | 83,043 | 24,650 | 23,674 | 278,447 | 278,447 | 394,621 | 396,317 | 1,667,382 | 1,667,382 | 2,062,003 | 2,063,699 |

Details of individual assets by account furnished upon request.

5. **U. T. System Board of Regents: Approval of Custodian Agreements for The University of Texas Investment Management Company (UTIMCO)**

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Business Affairs and the Vice Chancellor for Finance and Business Development that the U. T. System Board of Regents authorize Mr. Bruce Zimmerman, Chief Executive Officer and Chief Investment Officer of The University of Texas Investment Management Company (UTIMCO), to conclude negotiations with the HSBC Bank USA and/or The Bank of Nova Scotia, acting through its ScotiaMocatta division, for custodian bank services as deemed necessary by UTIMCO to perform investment management services for The University of Texas System.

BACKGROUND INFORMATION

The Master Investment Management Services Agreement (IMSA) between the U. T. System Board of Regents and the UTIMCO Board of Directors requires U. T. System Board approval of custodian banks and related custodian agreements. UTIMCO is in discussions with the HSBC Bank USA and The Bank of Nova Scotia to determine if these banks can provide UTIMCO with additional custodian services. Should these discussions result in new agreements, such agreements will be included in the Docket for U. T. System Board approval.

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

RECOMMENDATION

The University of Texas Investment Management Company (UTIMCO) Board of Directors recommends that the U. T. System Board of Regents approve the proposed Annual Budget as set forth on Page 146, which includes the capital expenditures budget and the Annual Fee and Allocation Schedule for the fiscal year ending August 31, 2011, as set forth on Page 147.

BACKGROUND INFORMATION

The proposed Total Budgeted Costs of \$66.3 million for Fiscal Year 2011 were approved by the UTIMCO Board on August 6, 2010.

The proposed Total Budgeted Costs consist of \$16.6 million for UTIMCO services, \$5.5 million for non-investment manager services such as custodial, legal, audit and consulting services, and \$44.2 million for invoiced external investment manager and performance fees charged directly to the UTIMCO Managed Funds.

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

The proposed capital expenditures budget totaling \$215 thousand is included in the total Annual Budget.

UTIMCO staff projects UTIMCO's available cash reserves to be approximately \$800 thousand and recommends that no cash reserves be distributed back to the U. T. System funds per the Master Investment Management Services Agreement (IMSA) between the U. T. System Board of Regents and UTIMCO.

The U. T. System Office of Finance has prepared a memorandum for the purpose of reviewing budgeted expenses, which is included as a part of this agenda item on Pages 148 - 158.

| UTIMCO (in thousands) | FY 2010 Budget | FY 2010 Forecast | FY 2011 Budget | FY11 Budget v FY10 Forecast | |
|---|-------------------|---------------------|-------------------|--------------------------------|-------------|
| | | | | \$ | % |
| SUMMARY | | | | | |
| UTIMCO Personnel | \$11,908 | \$11,911 | \$12,539 | \$628 | 5% |
| UTIMCO Other | <u>4,069</u> | <u>3,979</u> | <u>4,092</u> | <u>113</u> | <u>3%</u> |
| Total UTIMCO | 15,977 | 15,890 | 16,631 | 741 | 5% |
| Other, Non-Investment Manager | <u>5,437</u> | <u>5,652</u> | <u>5,505</u> | <u>(147)</u> | <u>-3%</u> |
| Total Non-Investment Manager | \$21,414 | \$21,542 | \$22,136 | \$594 | 3% |
| Investment Manager - Invoiced | <u>28,747</u> | <u>41,195</u> | <u>44,158</u> | <u>2,963</u> | <u>7%</u> |
| Total | \$50,161 | \$62,737 | \$66,294 | \$3,557 | 6% |
| DETAIL | | | | | |
| UTIMCO Personnel | | | | | |
| Salaries & Accrued Vacation | \$6,723 | \$6,518 | \$6,724 | \$206 | 3% |
| Performance Compensation | 3,482 | 3,727 | 4,081 | 354 | 9% |
| Benefits | 1,166 | 1,145 | 1,196 | 51 | 4% |
| Taxes | 470 | 472 | 479 | 7 | 1% |
| Hiring | 20 | 1 | 8 | 7 | 700% |
| Education, Dues, Memberships | 47 | 48 | 51 | 3 | 6% |
| Total | \$11,908 | \$11,911 | \$12,539 | \$628 | 5% |
| UTIMCO Other | | | | | |
| Travel & Meetings | \$622 | \$545 | \$705 | 160 | 29% |
| Online, Data, Contract Services & Subscriptions | 1,010 | 986 | 993 | 7 | 1% |
| Lease | 979 | 999 | 1,019 | 20 | 2% |
| Depreciation | 574 | 582 | 531 | (51) | -9% |
| Insurance | 250 | 248 | 248 | 0 | 0% |
| Office Expenses | 334 | 333 | 314 | (19) | -6% |
| Professional Services | 300 | 286 | 282 | (4) | -1% |
| Total | \$4,069 | \$3,979 | \$4,092 | \$113 | 3% |
| Other, Non-Investment Manager | | | | | |
| Custodian | \$2,009 | \$2,187 | \$2,445 | 258 | 12% |
| Measurement & Analytics | 1,210 | 1,175 | 1,058 | (117) | -10% |
| Consultants | 745 | 517 | 490 | (27) | -5% |
| Investment-related Legal | 725 | 1,044 | 811 | (233) | -22% |
| Audit | 735 | 719 | 691 | (28) | -4% |
| Other | 13 | 10 | 10 | 0 | 0% |
| Total | \$5,437 | \$5,652 | \$5,505 | (\$147) | -3% |
| Investment Manager - Invoiced | | | | | |
| Management Fees | \$18,695 | \$24,331 | \$35,861 | 11,530 | 47% |
| Performance Fees | <u>10,052</u> | <u>16,864</u> | <u>8,297</u> | <u>(8,567)</u> | <u>-51%</u> |
| Total | \$28,747 | \$41,195 | \$44,158 | \$2,963 | 7% |

Prepared by: UTIMCO
Date: July 2010

UTIMCO Management Fee and Direct Budgeted Investment Expenses
 Annual Fee and Allocation Schedule
 For the fiscal year ending August 31, 2011

| Proposed Budget | Fund Name | | | | | | Separate Funds | Total |
|---|-----------|-----|-------|-----------|-------|-------|----------------|--------|
| | PUF | PHF | LTF | GEF | ITF | STF | | |
| Market Value 2/28/10 (\$ millions) | 10,470 | 900 | 4,894 | 5,794 (2) | 4,028 | 1,703 | 200 | 22,195 |

| UTIMCO Management Fee | | | | | | | | |
|------------------------------|-------|-----|-------|---|-------|--|---|--------|
| Dollars (thousands) | 8,153 | 846 | 4,668 | | 2,964 | | | 16,631 |
| Basis Points | 7.8 | 9.4 | 9.5 | 0 | 7.4 | | 0 | 7.5 |

Direct Expenses to the Fund, excluding UT System Direct Expenses to the Fund

| Dollars (thousands) | | | | | | | | |
|--|---------------|-----------|-----------|---------------|---------------|---------|----------|---------------|
| Other Direct Costs | 2,488 | 30 | 36 | 1,677 | 1,274 | | 0 | 5,505 |
| External Management Fees - AUM | 17,239 | 0 | 0 | 9,631 | 8,991 | N/A (1) | 0 | 35,861 |
| External Management Fees - Performance | 4,128 | 0 | 0 | 2,283 | 1,886 | | 0 | 8,297 |
| Total Dollars | 23,855 | 30 | 36 | 13,591 | 12,151 | | 0 | 49,663 |

| Basis Points | | | | | | | | |
|--|-------------|------------|------------|-------------|-------------|---------|----------|-------------|
| Other Direct Costs | 2.4 | 0.3 | 0.1 | 2.9 | 3.2 | | 0 | 2.5 |
| External Management Fees - AUM | 16.5 | 0 | 0 | 16.6 | 22.3 | N/A (1) | 0 | 16.2 |
| External Management Fees - Performance | 3.9 | 0 | 0 | 3.9 | 4.7 | | 0 | 3.7 |
| Total Basis Points | 22.8 | 0.3 | 0.1 | 23.4 | 30.2 | | 0 | 22.4 |

UT System Direct Expenses to the Fund

| Dollars (thousands) | | | | | | | | |
|--|--------------|------------|---------------|----------|------------|----------|----------|---------------|
| UT System Compliance & Administration Fees | 0 | 0 | 12,242 | 0 | 0 | 0 | 0 | 12,242 |
| UT System Oversight Fees | 262 | 23 | 122 | 0 | 93 | 0 | 0 | 500 |
| UT System PUF Lands | 9,014 | 0 | 0 | 0 | 0 | 0 | 0 | 9,014 |
| Total Dollars | 9,276 | 23 | 12,364 | 0 | 93 | 0 | 0 | 21,756 |
| Total Basis Points | 8.9 | 0.3 | 25.3 | 0 | 0.0 | 0 | 0 | 9.8 |

(1) Income is net of fees

(2) Pooled Fund for the collective investment of the PHF and LTF

Prepared by: UTIMCO
 Date: July 2010

Fiscal Year 2011

**Review of UTIMCO Services Budget and
Other Budgeted Investment Management Expenses**

**The University of Texas System
Office of Finance**

Prepared by:

**Philip Aldridge – Vice Chancellor for Finance and Business Development
William Huang – Treasury Manager**

October 15, 2010

Based on information provided by UTIMCO staff through September 20, 2010.

Fiscal Year 2011 Review of UTIMCO Services Budget and Other Budgeted Investment Management Expenses

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Fiscal Year 2011 Review of UTIMCO Services Budget and Other Budgeted Investment Management Expenses

I. Executive Summary

This report reviews the UTIMCO Services budget and other budgeted investment management expenses (“Direct Costs to Funds”) for fiscal year 2011 that the UTIMCO Board has approved and the U. T. System Board of Regents are being asked to approve. The UTIMCO Services budget includes corporate expenses paid directly by UTIMCO. The Direct Costs to Funds budget includes external investment manager fees paid directly by UTIMCO and other costs related to custody, consulting, corporate legal, audit, and risk measurement. The proposed budget for FY11 is:

| | FY11 <u>(\$ millions)</u> |
|---|--|
| • Direct Costs to Funds: External Investment Manager Fees | \$ 44.2 |
| • UTIMCO Services Budget | 16.6 |
| • Direct Costs to Funds: Other Costs | <u>5.5</u> |
| Total Budgeted Costs | <u>\$ 66.3</u> |

The Total Budgeted Costs do not include all investment costs and exclude external manager fees that are paid by the funds and netted from asset values. The total investment costs for UTIMCO managed funds are reviewed in a separate report.

Highlights:

- **Total Budgeted Costs for FY11:** The FY11 budget is \$66.3 million, a 6% increase from the current projection for FY10 and a 32% increase from the FY10 budget.
- **The Direct Costs to Funds budget consists primarily of external investment manager fees.** The FY 11 budget of \$44.2 million is up 6% from the current FY10 projection and 37% from the FY10 budget. The increase is largely due to higher performance fees related to better than expected performance.
- **The UTIMCO Services Budget: The FY11 budget is \$16.6 million,** a 5% increase from the current projection for FY10 and a 4% increase from the FY10 budget.
- **Compensation: Compensation-related expenses represent more than 70% of the UTIMCO Services Budget.** Salaries for FY11 are budgeted to be flat from the FY10 budget. Budgeted salaries for FY11 include a 4.9% increase for existing staff (including promotions) and one open position. Incentive compensation for FY11 are budgeted to increase \$354k (10%) from FY10 projections. Over half of the increase is attributable to vesting of previously deferred incentive compensation.
- **UTIMCO Reserves:** UTIMCO staff projects UTIMCO’s available cash reserves to be \$789k at fiscal year-end 2010. We concur with UTIMCO staff in recommending that no distribution of reserves be made at this time.

II. Budget Analysis and Trends

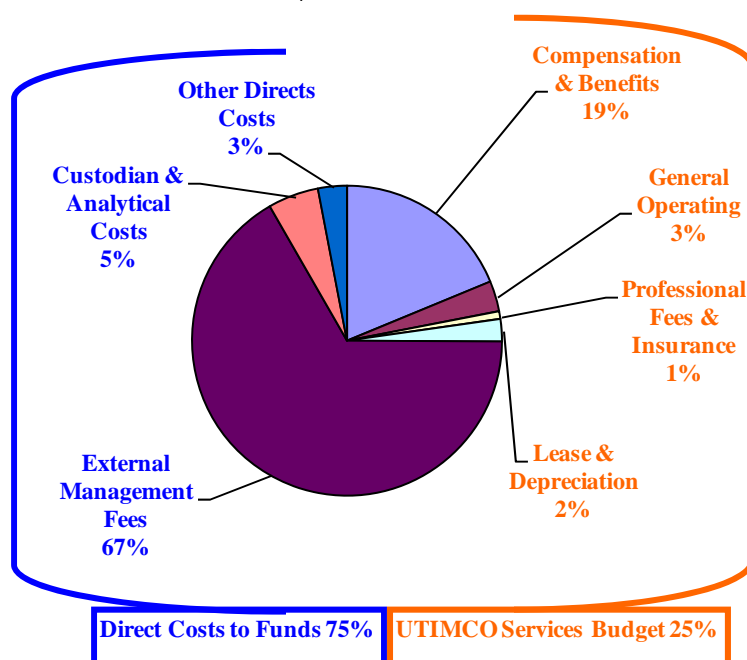
UTIMCO proposes Total Budgeted Costs for FY11 of \$66.3 million. Table 1 shows the Total Budgeted Costs (Direct Costs to Funds and UTIMCO Services Budget) as a percent of average Assets Under Management (AUM) since FY06.

Table 1
Total Budgeted Costs Trend FY06-FY11 (\$ millions)

| | FY06 | FY07 | FY08 | FY09 | Projected FY10 | Budget FY11 |
|---|--------|--------|--------|--------|----------------|-------------|
| Average Total Assets Under Management (AUM) * | 19,372 | 21,965 | 23,359 | 21,864 | 21,448 | 21,448 |
| % Change in AUM | 12% | 13% | 6% | -6% | -2% | 0% |
| Direct Costs to Funds | 52.3 | 40.1 | 35.1 | 37.8 | 46.8 | 49.7 |
| % Change in Direct Costs to Funds | 55% | -23% | -12% | 8% | 24% | 6% |
| Direct Costs to Funds % of AUM | 0.27% | 0.18% | 0.15% | 0.17% | 0.22% | 0.23% |
| UTIMCO Services Budget | 11.3 | 12.1 | 13.9 | 15.1 | 15.9 | 16.6 |
| % Change in UTIMCO Services Budget | 11% | 7% | 15% | 9% | 5% | 5% |
| UTIMCO Services Budget % of AUM | 0.06% | 0.05% | 0.06% | 0.07% | 0.07% | 0.08% |
| Total Budgeted Costs | 63.6 | 52.1 | 49.0 | 52.9 | 62.7 | 66.3 |
| % Change in Total Budgeted Costs | 44% | -18% | -6% | 8% | 18% | 6% |
| Total Budgeted Costs % of AUM | 0.33% | 0.24% | 0.21% | 0.24% | 0.29% | 0.31% |

* The FY10 and FY11 values are based on average AUM at fiscal year-end 2009 and May 2010.

FY 2011 Total Budgeted Costs
\$66.3 million



The pie chart to the left shows the breakdown of Total Budgeted Costs. The UTIMCO Services Budget represents 25% of the total budget, with Compensation & Benefits being the largest component. Direct Costs to Funds include External Management Fees (including performance fees) paid directly, Custodian & Analytical Costs and Other Direct Costs. External Management Fees represents the largest component of the total budget at 67%. UTIMCO retains external managers for 86% of the \$22.4 billion in operating and endowment funds (as of May 31, 2010). UTIMCO staff manages the remaining 14% of assets and an internal derivatives portfolio.

Table 2 compares the Total Budgeted Costs for FY10 and FY11. Refer to Exhibits A and B for a detailed budget comparison for FY10-FY11 and budget trend for FY06-FY11.

**Table 2
FY10 Forecast and FY11 Budget Overview**

| | FY10 | | | | FY11 | | | |
|-------------------------------|------------|--------------|--------------------------|-------------------------|------------|-----------------------------|----------------------------|-------------------------|
| | \$ Budget | \$ Projected | \$ Change vs FY10 Budget | % Change vs FY10 Budget | \$ Budget | \$ Change vs FY10 Projected | % Change vs FY10 Projected | % Change vs FY10 Budget |
| UTIMCO Services Budget | 15,977,125 | 15,889,516 | (87,609) | -0.5% | 16,631,305 | 741,789 | 4.7% | 4.1% |
| Direct Costs to Funds | 34,184,173 | 46,847,010 | 12,662,837 | 37.0% | 49,662,822 | 2,815,812 | 6.0% | 45.3% |
| Total Budgeted Costs | 50,161,298 | 62,736,526 | 12,575,228 | 25.1% | 66,294,127 | 3,557,601 | 5.7% | 32.2% |

FY10 Forecast versus FY10 Budget: UTIMCO staff projects FY10 Total Budgeted Costs will be \$62.7 million, \$12.6 million (25%) over the FY10 budget of \$50.2 million.

- UTIMCO Services corporate expenses are projected to be slightly under budget by \$88k (1%)
 - Salaries, largely driven by unfilled open positions, are expected to be \$205k under budget.
 - Travel expenses are projected to be \$70k (12%) under budget.
 - Corporate legal expenses are expected to be \$33k (22%) over budget.
- Direct Costs to Funds overall are projected to be over budget by \$12.7 million (37%).
 - External management fees are estimated to be \$5.6 million (30%) over budget and performance fees are anticipated to be \$6.8 million (68%) over budget in FY10, primarily due to the positive investment performance experienced during the fiscal year.
 - Consultant Fees are projected to be \$227k (31%) below budget.
 - Legal fees are projected to be \$232k (34%) over budget due to more investments being made.
- Capital Expenditures are forecasted at \$141k, mainly for ongoing technology and software upgrades.

FY11 Proposed Budget: The proposed \$66.3 million Total Budgeted Costs for FY11 is 6% higher than FY10 projected expenses (32% higher than the original FY10 budget).

- Direct Costs to Funds at \$49.7 million are budgeted to increase 6% over projected costs for FY10, mainly due to increases in external management fees.
- UTIMCO Services for FY11 at \$16.6 million is an increase of 5% over FY10 projected costs, primarily due to increases in personnel-related costs and travel expenses.
- Capital Expenditures are budgeted at \$215k, primarily for ongoing technology and software upgrades.

III. Direct Costs to Funds

Direct Costs to Funds for FY10 are projected at \$46.8 million or 37% above a budgeted \$34.2 million. The FY11 budget increases 6% to \$49.7 million from projected FY10 costs.

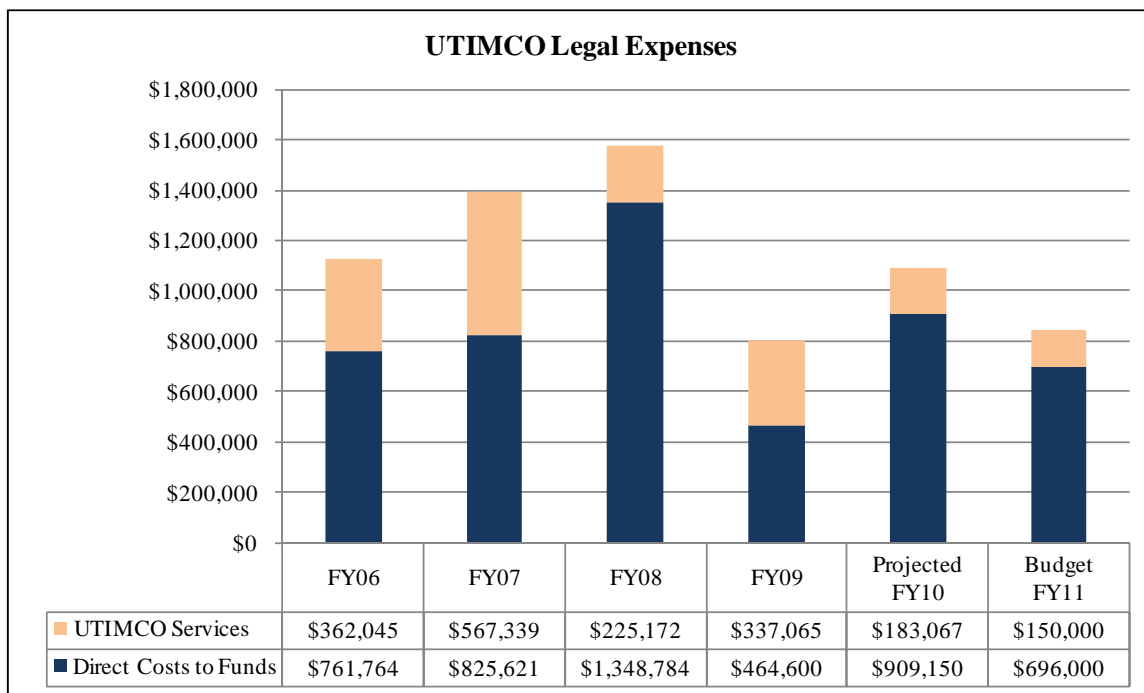
External Management and Performance Fees paid to external managers are the largest component of the overall budget. These fees, projected at \$41.2 million in FY10 (43% over the FY10 budget) and budgeted at \$44.2 million for FY11, represent 89% of Direct Costs to Funds budget and 67% of Total Budgeted Costs for FY11. Although UTIMCO staff estimates external management and performance fees using each manager's fee structure and current asset base, these fees are very difficult to forecast and budget due to the uncertainty of individual manager performance. The higher fees in FY10 represent investment performance greater than what was budgeted and projected. The budget for management fees includes an 8.6% investment return assumption. For FY11, the \$35.9 million in budgeted external management fees can be attributed as: \$20.2 million (56%) for existing managers, \$13.4 million (37%) for new managers and \$2.3 million (6%) for investment return assumptions.

Custodian and Analytical Costs: Custodian fees for FY10 are projected at \$2.2 million, 9% over budget. The FY11 budgeted amount for these expenses will increase 12% over FY10 levels. Performance measurement expenses paid in FY10 are projected to be 1% over budget at \$434k and are budgeted to decrease 6% to \$407k in FY11.

Risk Measurement: Risk measurement expenses charged to the funds are expected to be 9% under budget at \$392k for FY10 and budgeted to decrease 20% to \$316k in FY11.

Auditing expenses in FY10 of \$719k funded external auditors and U. T. System Audit Office fees. Audit expenses are budgeted at \$691k for FY11, a 4% decrease from FY10. Audit expenses have increased overall since FY08 due to a change in external auditors and additional time required to audit valuations of alternative investments.

Legal: The chart below shows the trend in UTIMCO Services (corporate) legal fees and direct legal expenses charged to the funds since FY06. Legal fees paid directly by the funds in FY10 are projected to be \$909k (34% over budget). Direct legal fees are budgeted for FY11 at \$696k, a 23% decrease.



IV. UTIMCO Services Budget

For FY11, total personnel-related expenses including employee benefits account for 75% of the UTIMCO Services budget (19% of Total Budgeted Costs). Trends in staffing and total compensation in relation to assets are shown in Table 3 on the next page. Highlights from Table 3 include:

- Staffing has grown 6% (annualized) from FY06 to FY10.
- Average AUM per employee decreased 3% (annualized) from FY06 to FY10.
- Staffing is projected at 57 employees for FY10 and budgeted at 58 employees for FY11.
- Salaries are budgeted to increase 3% in FY11; budgeted incentive compensation increase 10%; and total compensation is budgeted to increase 5%.
- Total compensation has increased 11% (annualized) since FY06.
- Total compensation per employee has increased 6% (annualized) since FY06 to \$180k in FY10.

**Table 3
UTIMCO Compensation and Headcount FY06-FY11**

| | FY06 | FY07 | FY08 | FY09 | Projected FY10 | % Change Since FY06 (annualized) | Budget FY11 | % Change From FY10 |
|--------------------------------------|-----------|-----------|-----------|-----------|-------------------|---|----------------|--------------------------|
| Employees (as of year end) | 46 | 47 | 58 | 57 | 57 | 6% | 58 | 2% |
| Average Total AUM(\$ millions) | 19,372 | 21,965 | 23,359 | 21,864 | 21,448 | 3% | 21,448 | 0% |
| Average AUM/Employee (\$ millions) | 421 | 467 | 403 | 384 | 376 | -3% | 370 | -2% |
| Salaries and Wages (\$) | 4,492,078 | 4,908,821 | 5,377,233 | 6,443,360 | 6,517,808 | 10% | 6,724,143 | 3% |
| Bonus Compensation (\$) | 2,164,963 | 2,082,700 | 3,016,393 | 3,245,765 | 3,726,719 | 15% | 4,081,154 | 10% |
| Total Compensation (\$) | 6,657,040 | 6,991,521 | 8,393,626 | 9,689,126 | 10,244,527 | 11% | 10,805,297 | 5% |
| Total Compensation per Employee (\$) | 144,718 | 148,756 | 144,718 | 169,985 | 179,729 | 6% | 186,298 | 4% |
| Bonus as % of Salaries and Wages | 48% | 42% | 56% | 50% | 57% | | 61% | |
| Bonus as % of Total Compensation | 33% | 30% | 36% | 33% | 36% | | 38% | |

Staffing: The FY10 budget was based on staffing of 60 employees; actual staffing is projected to be 57 employees at fiscal year-end 2010. The FY11 budget is based on filling one open position to bring staffing to 58 employees by fiscal year-end.

Personnel-related Expenses:

- **Salaries and Wages** are projected to be \$6.5 million, \$205k (3%) under budget, in FY10 because of unfilled positions and will remain budgeted at \$6.7 million in FY11. Budgeted salaries for FY11 include a 4.9% increase for existing staff (including promotions) and one open position.
- **Bonus Compensation** for FY10 based on performance year-to-date (including deferred incentive compensation earned in prior years and related income) is forecast at \$3.7 million, 7% over budget, due to better than projected investment performance. The FY11 budget of \$4.0 million in bonus compensation is 10% higher than projected FY10 incentive compensation. The proposed FY11 bonus compensation budget is based on Compensation Plan participants earning 70% of the maximum incentive award. The FY11 budget also includes deferred incentive compensation earned by employees in prior years and funds for a discretionary bonus pool of up to 15% of salaries for employees who are not participants in the Compensation Plan.
- **Employee Benefits** are expected to be under budget in FY10 by \$21k (2%). Employee Benefits costs are budgeted to increase 5% to \$1.2 million in FY11.

General Operating Expenses are forecast to be 6% below budget for FY10 at \$2.0 million. General operating expenses for FY11 are budgeted to increase 8% to \$2.1 million, primarily due to increases in travel, on-line data and contract services offset by a reduction in repairs and maintenance. Travel is budgeted at \$680k, an increase of 30% over FY10 projections. The increase in travel reflects an increase in air and hotel rates rather than a volume increase in traveling.

Lease Expenses: Table 4 shows that lease expenses have stabilized in recent years since UTIMCO's move in FY06 and addition of lease space in FY08. Operating Expenses (pass through expenses to tenants) have increased significantly since FY07 due to rising utilities expenses and ad valorem taxes, and now exceed base rent.

Table 4
UTIMCO Lease Expenses FY06-FY11

| | FY06 | FY07 | FY08 | FY09 | Projected FY10 | Budget FY11 |
|--|-------------|-------------|-------------|-------------|---------------------------|------------------------|
| Property Lease | \$613,560 | \$462,722 | \$499,823 | \$518,373 | \$518,373 | \$518,373 |
| Operating Expenses | \$83,294 | \$362,755 | \$515,296 | \$515,848 | \$538,894 | \$555,323 |
| Parking Expenses | \$77,342 | \$94,805 | \$100,007 | \$96,847 | \$106,359 | \$110,400 |
| Other Expenses | \$5,166 | \$5,671 | \$10,473 | \$1,461 | \$5,672 | \$5,700 |
| Amortization (Deferred Rent Credit) | (\$124,076) | (\$148,891) | (\$150,679) | (\$170,344) | (\$170,344) | (\$170,344) |
| Total Lease Expenses (net) | \$655,286 | \$777,062 | \$974,920 | \$962,184 | \$998,954 | \$1,019,451 |

Professional Fees are expected to be \$286k in FY10, 5% lower than budgeted. Increased legal expenses were offset by reduced compensation consultant fees. Professional Fees for FY11 are budgeted at \$282k, a decrease of 2%.

V. UTIMCO Capital Expenditures

The trend for Capital Expenditures for FY07-FY11 is summarized in Table 5. In FY10, total capital expenditures are forecasted to be \$141k, mainly for ongoing technology and software upgrades. A budget of \$215k is proposed for FY11. The majority of the FY11 budget is for ongoing technology and software upgrades including videoconferencing equipment with the rest for ongoing office equipment and fixtures.

Table 5
UTIMCO Capital Expenditures FY07-FY11

| | FY07 | FY08 | FY09 | Projected FY10 | Budget FY11 |
|--|-------------|-------------|-------------|---------------------------|------------------------|
| Ongoing: Technology and Software Upgrades | \$71,271 | \$139,860 | \$113,502 | \$103,625 | \$152,500 |
| Ongoing: Office Equipment and Fixtures | \$11,599 | \$18,498 | \$22,672 | \$37,168 | \$62,500 |
| Expansion: Technology and Software Upgrades | \$0 | \$7,490 | \$0 | \$0 | \$0 |
| Expansion: Office Equipment and Fixtures | \$0 | \$152,864 | \$0 | \$0 | \$0 |
| Expansion: Leasehold Improvements (net) | \$0 | \$166,453 | \$0 | \$0 | \$0 |
| Total Capital Expenditures (net) | \$82,870 | \$485,165 | \$136,174 | \$140,793 | \$215,000 |

EXHIBIT A

| | Total Budgeted Costs FY10-FY11 | | | | | | | | |
|---|--------------------------------|-------------------|----------------------------|--------------|-------------------|------------------|-------------------------------|--------------|-------------------------------|
| | FY10 | | Change from FY10 Budget | | FY11 | | Change from FY10 Projected | | Change from FY10 Budget |
| | Budget | Projected | \$ | % | Budget | \$ | % | % | |
| UTIMCO Services | | | | | | | | | |
| Salaries and Wages + Vacation | 6,722,802 | 6,517,808 | (204,994) | -3.0% | 6,724,143 | 206,334 | 3.2% | 0.0% | |
| Bonus Compensation + Interest | 3,482,645 | 3,726,719 | 244,074 | 7.0% | 4,081,154 | 354,435 | 9.5% | 17.2% | |
| Total Compensation | 10,205,447 | 10,244,527 | 39,080 | 0.4% | 10,805,297 | 560,769 | 5.5% | 5.9% | |
| Total Payroll taxes | 470,116 | 472,473 | 2,357 | 0.5% | 479,423 | 6,950 | 1.5% | 2.0% | |
| 403(b) Contributions | 493,704 | 487,083 | (6,621) | -1.3% | 504,567 | 17,484 | 3.6% | 2.2% | |
| Group Health, Dental, AD&D, Life, LTD | 632,239 | 616,867 | (15,372) | -2.4% | 653,490 | 36,623 | 5.9% | 3.4% | |
| Employee Benefits | 1,125,943 | 1,103,950 | (21,993) | -2.0% | 1,158,057 | 54,107 | 4.9% | 2.9% | |
| On-Line Data & Contract Services | 1,020,492 | 997,574 | (22,918) | -2.2% | 1,017,529 | 19,955 | 2.0% | -0.3% | |
| Recruiting and Relocation Expenses | 20,000 | 1,100 | (18,900) | -94.5% | 7,500 | 6,400 | 581.8% | -62.5% | |
| Travel | 593,586 | 523,134 | (70,452) | -11.9% | 680,000 | 156,866 | 30.0% | 14.6% | |
| Phone and Telecommunications | 77,540 | 77,874 | 334 | 0.4% | 74,600 | (3,274) | -4.2% | -3.8% | |
| Computer & Office Supplies | 81,963 | 93,684 | 11,721 | 14.3% | 97,950 | 4,266 | 4.6% | 19.5% | |
| Employee Education | 29,263 | 35,596 | 6,333 | 21.6% | 37,685 | 2,089 | 5.9% | 28.8% | |
| Repairs/Maintenance | 198,844 | 179,828 | (19,016) | -9.6% | 146,874 | (32,954) | -18.3% | -26.1% | |
| BOD Meetings | 18,000 | 11,004 | (6,996) | -38.9% | 12,000 | 996 | 9.1% | -33.3% | |
| Other Operating Expenses | 32,511 | 31,003 | (1,508) | -4.6% | 34,195 | 3,192 | 10.3% | 5.2% | |
| Total General Operating | 2,072,199 | 1,950,796 | (121,403) | -5.9% | 2,108,333 | 157,536 | 8.1% | 1.7% | |
| Total Lease Expense | 978,729 | 998,954 | 20,225 | 2.1% | 1,019,452 | 20,498 | 2.1% | 4.2% | |
| Invest., Hiring & Board Consultants | 30,000 | 30,000 | 0 | 0.0% | 30,000 | 0 | 0.0% | 0.0% | |
| Legal Expenses | 150,000 | 183,067 | 33,067 | 22.0% | 150,000 | (33,067) | -18.1% | 0.0% | |
| Compensation Consultant | 77,500 | 39,600 | (37,900) | -48.9% | 60,000 | 20,400 | 51.5% | -22.6% | |
| Accounting fees | 42,500 | 33,450 | (9,050) | -21.3% | 41,500 | 8,050 | 24.1% | -2.4% | |
| Total Professional Fees | 300,000 | 286,117 | (13,883) | -4.6% | 281,500 | (4,617) | -1.6% | -6.2% | |
| Property/Liability Package | 15,000 | 11,924 | (3,077) | -20.5% | 15,000 | 3,077 | 25.8% | 0.0% | |
| Umbrella Policy | 4,500 | 4,459 | (41) | -0.9% | 4,500 | 41 | 0.9% | 0.0% | |
| Workers Compensation | 15,000 | 20,211 | 5,211 | 34.7% | 17,500 | (2,711) | -13.4% | 16.7% | |
| Business Auto | 850 | 851 | 1 | 0.1% | 850 | (1) | -0.1% | 0.0% | |
| Commercial Bonding Policy | 35,000 | 30,729 | (4,271) | -12.2% | 30,000 | (729) | -2.4% | -14.3% | |
| Prof., D&O & Emp. Practices Liability | 180,000 | 179,953 | (47) | 0.0% | 180,000 | 47 | 0.0% | 0.0% | |
| Total Insurance | 250,350 | 248,126 | (2,224) | -0.9% | 247,850 | (276) | -0.1% | -1.0% | |
| Depreciation of Equipment | 574,341 | 584,571 | 10,230 | 1.8% | 531,393 | (53,178) | -9.1% | -7.5% | |
| Total UTIMCO Services | 15,977,125 | 15,889,516 | (87,609) | -0.5% | 16,631,305 | 741,789 | 4.7% | 4.1% | |
| Direct Costs to Funds | | | | | | | | | |
| External Management Fees | 18,695,142 | 24,330,686 | 5,635,544 | 30.1% | 35,860,764 | 11,530,078 | 47.4% | 91.8% | |
| External Performance Fees | 10,052,352 | 16,863,993 | 6,811,641 | 67.8% | 8,297,356 | (8,566,637) | -50.8% | -17.5% | |
| External Management/Performance Fees | 28,747,494 | 41,194,678 | 12,447,184 | 43.3% | 44,158,120 | 2,963,442 | 7.2% | 53.6% | |
| Custodian Fees and Other Direct Costs | 2,008,927 | 2,186,708 | 177,781 | 8.8% | 2,444,776 | 258,067 | 11.8% | 21.7% | |
| Performance Measurement | 429,374 | 433,775 | 4,401 | 1.0% | 407,350 | (26,426) | -6.1% | -5.1% | |
| Analytical Tools | 348,178 | 349,140 | 962 | 0.3% | 335,335 | (13,805) | -4.0% | -3.7% | |
| Risk Measurement | 432,000 | 392,458 | (39,542) | -9.2% | 315,500 | (76,958) | -19.6% | -27.0% | |
| Custodian and Analytical Costs | 3,218,479 | 3,362,082 | 143,603 | 4.5% | 3,502,960 | 140,878 | 4.2% | 8.8% | |
| Consultant Fees | 744,500 | 517,290 | (227,210) | -30.5% | 490,000 | (27,290) | -5.3% | -34.2% | |
| Auditing | 735,000 | 719,092 | (15,908) | -2.2% | 691,092 | (28,000) | -3.9% | -6.0% | |
| Controls Assessment (Sarbanes-Oxley) | 0 | 0 | 0 | N/A | 0 | 0 | N/A | N/A | |
| Printing | 0 | 0 | 0 | N/A | 0 | 0 | N/A | N/A | |
| Legal Fees | 677,500 | 909,150 | 231,650 | 34.2% | 696,000 | (213,150) | -23.4% | 2.7% | |
| Background Searches & Other | 61,200 | 144,717 | 83,517 | 136.5% | 124,650 | (20,067) | -13.9% | 103.7% | |
| Other Direct Costs Total | 2,218,200 | 2,290,250 | 72,050 | 3.2% | 2,001,742 | (288,508) | -12.6% | -9.8% | |
| Total Direct Costs to Funds | 34,184,173 | 46,847,010 | 12,662,837 | 37.0% | 49,662,822 | 2,815,812 | 6.0% | 45.3% | |
| Total Budgeted Costs | 50,161,298 | 62,736,526 | 12,575,228 | 25.1% | 66,294,127 | 3,557,601 | 5.7% | 32.2% | |

EXHIBIT B

| | Total Budgeted Costs FY06-FY11 | | | | | |
|---|--------------------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| | FY06 | FY07 | FY08 | FY09 | FY10 | FY11 |
| | Actual | Actual | Actual | Actual | Projected | Budget |
| UTIMCO Services | | | | | | |
| Salaries and Wages + Vacation | 4,492,078 | 4,908,821 | 5,377,233 | 6,443,360 | 6,517,808 | 6,724,143 |
| Bonus Compensation + Interest | 2,164,963 | 2,082,700 | 3,016,393 | 3,245,765 | 3,726,719 | 4,081,154 |
| Total Compensation | 6,657,040 | 6,991,521 | 8,393,626 | 9,689,126 | 10,244,527 | 10,805,297 |
| Total Payroll taxes | 312,023 | 337,117 | 394,313 | 449,846 | 472,473 | 479,423 |
| 403(b) Contributions | 327,724 | 329,083 | 404,671 | 478,096 | 487,083 | 504,567 |
| Group Health, Dental, AD&D, Life, LTD | 406,756 | 420,593 | 510,154 | 602,258 | 616,867 | 653,490 |
| Employee Benefits | 734,480 | 749,676 | 914,825 | 1,080,354 | 1,103,950 | 1,158,057 |
| On-Line Data & Contract Services | 811,883 | 840,578 | 851,499 | 894,096 | 997,574 | 1,017,529 |
| Recruiting and Relocation Expenses | 216,927 | 400,617 | 108,198 | 16,697 | 1,100 | 7,500 |
| Travel | 205,965 | 176,929 | 515,494 | 290,632 | 523,134 | 680,000 |
| Phone Equipment and Charges | 46,965 | 43,743 | 38,400 | 72,014 | 77,874 | 74,600 |
| Computer & Office Supplies | 143,372 | 67,733 | 140,512 | 93,136 | 93,684 | 97,950 |
| Employee Education | 13,728 | 16,817 | 20,311 | 6,230 | 35,596 | 37,685 |
| Repairs/Maintenance | 85,412 | 109,592 | 179,217 | 188,875 | 179,828 | 146,874 |
| BOD Meetings | 52,375 | 49,711 | 58,615 | 12,760 | 11,004 | 12,000 |
| Other Operating Expenses | 106,401 | 42,205 | 40,748 | 29,426 | 31,003 | 34,195 |
| Total General Operating | 1,683,029 | 1,747,924 | 1,952,993 | 1,603,865 | 1,950,796 | 2,108,333 |
| Total Lease Expense | 655,286 | 777,062 | 974,920 | 962,184 | 998,954 | 1,019,452 |
| Invest., Hiring & Board Consultants | 20,175 | 25,124 | 30,000 | 30,000 | 30,000 | 30,000 |
| Legal Expenses | 362,045 | 567,339 | 225,172 | 337,065 | 183,067 | 150,000 |
| Compensation Consultant | 95,920 | 13,100 | 146,455 | 99,650 | 39,600 | 60,000 |
| Accounting fees | 54,106 | 38,980 | 53,414 | 41,035 | 33,450 | 41,500 |
| Total Professional Fees | 532,246 | 644,542 | 455,041 | 507,750 | 286,117 | 281,500 |
| Property/Liability Package | 22,993 | 18,685 | 15,100 | 12,372 | 11,924 | 15,000 |
| Umbrella Policy | 5,500 | 5,500 | 4,977 | 4,454 | 4,459 | 4,500 |
| Workers Compensation | 13,109 | 20,132 | 17,315 | 16,653 | 20,211 | 17,500 |
| Business Auto | 756 | 779 | 811 | 836 | 851 | 850 |
| Commercial Bonding Policy | 27,752 | 40,900 | 39,785 | 33,839 | 30,729 | 30,000 |
| Prof., D&O & Emp. Practices Liability | 150,525 | 164,300 | 164,300 | 172,064 | 179,953 | 180,000 |
| Total Insurance | 220,634 | 250,295 | 242,288 | 240,217 | 248,126 | 247,850 |
| Depreciation of Equipment | 504,637 | 564,076 | 556,450 | 590,929 | 584,571 | 531,393 |
| Total UTIMCO Services | 11,299,376 | 12,062,213 | 13,884,456 | 15,124,270 | 15,889,516 | 16,631,305 |
| Direct Costs to Funds | | | | | | |
| External Management Fees | 17,815,353 | 16,413,106 | 20,767,775 | 15,656,987 | 24,330,686 | 35,860,764 |
| External Performance Fees | 29,648,938 | 18,010,650 | 8,087,324 | 17,129,808 | 16,863,993 | 8,297,356 |
| External Management/Performance Fees | 47,464,291 | 34,423,756 | 28,855,099 | 32,786,795 | 41,194,678 | 44,158,120 |
| Custodian Fees and Other Direct Costs | 1,634,942 | 1,531,924 | 1,771,313 | 1,918,015 | 2,186,708 | 2,444,776 |
| Performance Measurement | 484,660 | 453,612 | 459,962 | 417,322 | 433,775 | 407,350 |
| Analytical Tools | 338,630 | 644,597 | 370,497 | 347,713 | 349,140 | 335,335 |
| Risk Measurement | 276,000 | 372,990 | 491,986 | 416,416 | 392,458 | 315,500 |
| Custodian and Analytical Costs | 2,734,232 | 3,003,123 | 3,093,758 | 3,099,466 | 3,362,082 | 3,502,960 |
| Consultant Fees | 852,000 | 1,289,394 | 736,654 | 567,125 | 517,290 | 490,000 |
| Auditing | 177,944 | 204,550 | 829,938 | 733,097 | 719,092 | 691,092 |
| Controls Assessment (Sarbanes-Oxley) | 97,110 | 109,750 | 0 | 0 | 0 | 0 |
| Printing | 163,790 | 178,155 | 152,719 | 132,932 | 0 | 0 |
| Legal Fees | 761,764 | 825,621 | 1,348,784 | 464,600 | 909,150 | 696,000 |
| Background Searches & Other | 59,147 | 24,747 | 50,512 | 35,107 | 144,717 | 124,650 |
| Other Direct Costs Total | 2,111,755 | 2,632,217 | 3,118,607 | 1,932,861 | 2,290,250 | 2,001,742 |
| Total Direct Costs to Funds | 52,310,278 | 40,059,096 | 35,067,464 | 37,819,122 | 46,847,010 | 49,662,822 |
| Total Budgeted Costs | 63,609,654 | 52,121,309 | 48,951,920 | 52,943,392 | 62,736,526 | 66,294,127 |

EXHIBIT C

UTIMCO Reserve Analysis for August 31, 2010

| | | |
|--|------------|-------------------|
| Projected Cash Reserves at August 31, 2010 | | |
| Cash | | 8,681,150 |
| Prepaid Expenses | | 411,844 |
| Less: Accounts Payable | | (3,931,361) |
| (Includes bonuses & earnings payable) | | |
| Expected Cash Reserves at August 31, 2010 | | \$ 5,161,633 |
| FY11 Proposed Operating Budget | 16,631,305 | |
| Applicable Percentage | 25% | 4,157,826 |
| FY11 Proposed Capital Expenditures | 215,000 | 215,000 |
| Required Cash Reserves at August 31, 2010 | | \$ 4,372,826 |
| Balance Available for Distribution | | \$ 788,806 |
| Recommended Distribution | | \$ - |

7. **U. T. System Board of Regents: Approval of revisions to the amended and restated University of Texas Investment Management Company (UTIMCO) Compensation Program**

RECOMMENDATION

The University of Texas Investment Management Company Board of Directors (UTIMCO Board) recommends that the U. T. System Board of Regents (U. T. System Board) approve revisions to Appendix E of the amended and restated UTIMCO Compensation Program (Plan), as set forth in congressional style on Pages 165 - 166. Revisions to Appendices C and D will be discussed by the UTIMCO Compensation Committee on November 4, 2010, and the UTIMCO Board on November 9, 2010, and are expected to be recommended to the U. T. System Board for approval at the November 10-11, 2010 meeting. The revisions to the amended and restated Plan are to be effective for the Plan Year beginning July 1, 2010.

BACKGROUND INFORMATION

The UTIMCO Board engaged Mercer as its compensation consultant to review the design of the Plan and to provide advice and counsel to the UTIMCO Board and the UTIMCO Compensation Committee. On August 6, 2010, the UTIMCO Board considered the recommendations from Mercer, UTIMCO's performance, and other relevant factors and approved certain changes to Appendices C, D, and E of the Plan, which was last approved by the U. T. System Board on August 20, 2009. Additional revisions to Appendices C and D will be considered by the UTIMCO Board on November 9, 2010, and Executive Vice Chancellor Kelley will present all major changes at the Finance and Planning Committee meeting on November 10, 2010.

Appendix C, Table 1

Appendix C, Table 1 sets forth the Eligible Positions, Weightings, Incentive Award Opportunities, and Percentage of Award Deferred for each Eligible Position. The UTIMCO Board will consider the approval of three new Eligible Positions and increases to the Maximum Incentive Award Opportunity for certain Eligible Positions. The proposed revised Appendix C will be presented at the Finance and Planning Committee meeting. A current copy of Appendix C is shown on Pages 161 - 162.

Appendix D, Table 2

Appendix D, Table 2 sets forth two of the Performance Goals categories referenced in the Plan for the Plan Participants: the Entity Performance and the Asset Class/Investment Type Performance Goals, including the benchmarks for Asset Class/Investment Type and the Threshold, Target, and Maximum Performance Standards for the Total Endowment Funds, Intermediate Term Fund, and the Asset Class/Investment Types. The UTIMCO Board will consider changes to the Policy Portfolio Weights for the Total Endowment Funds consistent with changes to the Investment Policy Statements previously approved by the U. T. System Board on August 12, 2010.

The proposed revised Appendix D will be presented at the Finance and Planning Committee meeting. A current copy of Appendix D is shown on Pages 163 - 164.

Appendix E, Table 3

Appendix E, Table 3 sets forth the Eligible Positions of Affected Participants. Table 3 is required to be revised each Performance Period to identify the Eligible Positions for which Performance Incentive Awards are subject to automatic adjustment as to timing and amount pursuant to the Plan. The UTIMCO Board is recommending changes to the Eligible Positions in Table 3 as shown on Page 166.

Appendix C

**Eligible Positions
Weightings
Incentive Award Opportunities for each Eligible Position
Percentage of Award Deferred**

TABLE 1 (For the Performance Periods beginning after June 30, 2009)

| Eligible Position | Weighting | | | Incentive Award Opportunity (% of Salary) | | | | Percentage of Award Deferred |
|--|-----------|---------------------------------|------------|---|-----------|--------|---------|------------------------------|
| | Entity | Asset Class/ Investment Type | Individual | < Threshold | Threshold | Target | Maximum | |
| <i>Investment Professionals</i> | | | | | | | | |
| CEO & Chief Investment Officer | 60% | 0% | 40% | 0% | 0% | 100% | 200% | 50% |
| President & Deputy CIO | 40% | 40% | 20% | 0% | 0% | 95% | 190% | 50% |
| Managing Director | 30% | 40% | 30% | 0% | 0% | 85% | 170% | 40% |
| Managing Director - Private Investments | 30% | 30% | 40% | 0% | 0% | 85% | 170% | 40% |
| Senior Director, Investments | 25% | 35% | 40% | 0% | 0% | 60% | 120% | 35% |
| Senior Portfolio Manager | 20% | 40% | 40% | 0% | 0% | 60% | 120% | 35% |
| Senior Director, Risk Management | 30% | 0% | 70% | 0% | 0% | 50% | 100% | 35% |
| Portfolio Manager | 20% | 40% | 40% | 0% | 0% | 50% | 100% | 30% |
| Director, Investments | 20% | 40% | 40% | 0% | 0% | 50% | 100% | 30% |
| Director - Private Investments | 20% | 30% | 50% | 0% | 0% | 50% | 100% | 30% |
| Director, Risk Management | 30% | 0% | 70% | 0% | 0% | 40% | 80% | 30% |
| Senior Associate, Investments | 15% | 35% | 50% | 0% | 0% | 40% | 80% | 20% |
| Associate, Investments | 15% | 30% | 55% | 0% | 0% | 35% | 70% | 15% |
| Associate - Private Investments | 15% | 20% | 65% | 0% | 0% | 35% | 70% | 15% |
| Associate, Risk Management | 30% | 0% | 70% | 0% | 0% | 35% | 70% | 15% |
| Senior Analyst, Investments | 10% | 20% | 70% | 0% | 0% | 30% | 60% | 0% |
| Analyst, Investments | 10% | 20% | 70% | 0% | 0% | 25% | 50% | 0% |
| Analyst, Risk Management | 30% | 0% | 70% | 0% | 0% | 25% | 50% | 0% |
| <i>Operations/Support Professionals</i> | | | | | | | | |
| Senior Managing Director | 20% | 0% | 80% | 0% | 0% | 60% | 120% | 40% |
| Managing Director | 20% | 0% | 80% | 0% | 0% | 50% | 100% | 30% |
| General Counsel & Chief Compliance Officer | 0% | 0% | 100% | 0% | 0% | 50% | 100% | 30% |
| Manager | 20% | 0% | 80% | 0% | 0% | 40% | 80% | 25% |

Revisions forthcoming

Appendix D

Benchmarks for Asset Class/Investment Type Threshold, Target, and Maximum Performance Standards

Performance Standards for Intermediate Term Fund

UPDATED TABLE 2 (7/1/09 through 6/30/10)

| Asset Class/Investment Type | Benchmark | Policy Portfolio Weights | | Performance Standards | | |
|---|---|--------------------------|------------------|-----------------------|-----------|----------|
| | | Total Endowment | ITF | Threshold | Target | Maximum |
| | | Assets | | | | |
| | | (% of Portfolio) | (% of Portfolio) | | | |
| Entity: Benchmark (Total Endowment Funds) | Policy Portfolio | n/a | n/a | +0 bps | +75 bps | +150 bps |
| Entity: Benchmark (Intermediate Term Fund) | Policy Portfolio | n/a | n/a | +0 bps | +50 bps | +100 bps |
| Investment Grade Fixed Income | Barclays Capital Global Aggregate Index | 7.5% | 30.0% | +0 bps | +25 bps | +50 bps |
| Real Estate | FTSE EPRA/NAREIT Developed Index | 3.5% | 5.0% | +0 bps | +50 bps | +100 bps |
| Natural Resources | 50% Dow Jones-UBS Commodity Total Return Index and 50% MSCI World Natural Resources Index | 5.5% | 7.5% | +0 bps | +50 bps | +100 bps |
| Developed Country Equity | MSCI World Index with net dividends | 19.0% | 15.0% | +0 bps | +62.5 bps | +125 bps |
| Emerging Markets Equity | MSCI Emerging Markets with net dividends | 13.0% | 7.5% | +0 bps | +75 bps | +150 bps |
| Hedge Funds (Less Correlated & Constrained Investments) | Hedge Fund Research Indices Fund of Funds Composite Index | 30.0% | 35.0% | +0 bps | +75 bps | +150 bps |
| Private Investments (excludes Real Estate) | Venture Economics Custom Index | 20.5% | 0% | +0 bps | +100 bps | +200 bps |
| Private Investments Real Estate | NACREIF Custom Index | 1.0% | 0% | +0 bps | +100 bps | +200 bps |
| Specific asset class benchmarks: | | | | | | |
| Credit-Related Fixed Income | Barclays Capital Global High Yield Index | | | +0 bps | +37.5 bps | +75 bps |
| Internal Investment Grade Fixed Income | US Barclays Capital Aggregate | | | +0 bps | +25 bps | +50 bps |

Revisions forthcoming

Appendix E

Eligible Positions of Affected Participants

TABLE 3 (7/1/10 through 6/30/11)

| Eligible Position |
|---|
| <p style="text-align: center;"><i>Investment Professionals</i></p> <p>CEO & Chief Investment Officer President & Deputy CIO Managing Director Managing Director - Private Investments Senior Director, Investment Senior Portfolio Manager Senior Director, Risk Management Portfolio Manager Director, Investment Director - Private Investments Director, Risk Management</p> <p style="text-align: center;"><i>Operations/Support Professionals</i></p> <p>Senior Managing Director Managing Director General Counsel & Chief Compliance Officer <u>Senior Manager</u> Manager</p> |