

# **Finance and Planning Committee**

THE UNIVERSITY OF TEXAS SYSTEM  
BOARD OF REGENTS



April 2, 2002

# THE UNIVERSITY OF TEXAS SYSTEM

## ACTION AND INFORMATIONAL ITEMS BASED ON FINAL STAFF RECOMMENDATIONS REGARDING THE REPORT OF THE U. T. SYSTEM TECHNOLOGY TRANSFER COMMISSION

March 11, 2002

The Technology Transfer Commission submitted its report to the Chancellor on February 11, 2002. The recommendations were reviewed by the Chancellor and the following staff members: Executive Vice Chancellor for Business Affairs Kerry Kennedy, Executive Vice Chancellor for Academic Affairs Edwin Sharpe, Acting Executive Vice Chancellor for Health Affairs James Guckian, Vice Chancellor and General Counsel Cullen M. Godfrey, Dennis Stone, Vice President for Technology Development at U. T. Southwestern Medical Center, Georgia Harper, attorney in the Office of General Counsel, and Florence Mayne, Assistant to the Executive Vice Chancellor for Business Affairs. Based on a review of the Technology Transfer Commission's report, the staff developed recommendations, which appear in the Final Staff Recommendations dated March 11, 2002 (a spiral-bound copy of which is provided separately).

### ACTION ITEMS

The following is a list of items requiring action by the Board of Regents (numbered items in parentheses — e.g., "A.1" — correspond to the numbered items in the commission's report and in the Final Staff Recommendations):

#### 1. **Amendments to Part Two, Chapter XII, Intellectual Property, of the Regents' Rules and Regulations**

In order to implement certain Technology Transfer Commission recommendations, and to coordinate the rules and regulations with current practice, a number of amendments to Part Two, Chapter XII, Intellectual Property, of the Regents' Rules and Regulations are proposed. Changes of note include the following:

- Section 2.1 would be revised to clarify that the intellectual property policy applies to full and part-time faculty and staff and visiting faculty members and researchers.
- Section 2.5 would be amended to provide that the Technology Transfer Office, with the concurrence of the institutional president or his or her delegate, will decide in its sole discretion whether it will develop and commercialize an invention.
- Section 3.3 would be deleted. This section addressed the role of UTIMCO in assisting component institutions in business and financial matters relating to intellectual property. UTIMCO no longer provides such assistance.
- Section 4.25 would be revised to clarify that the expenses attributable to a particular licensing project would be recovered from revenue received before income is divided and shared with the creator.

(See items A.1, C.2, D.1, and D.3.)

**2. Amendments to Part One, Chapter I, Section 9, Delegation to Act on Behalf of the Board, of the Regents' Rules and Regulations**

Amendments to Part One, Chapter I, Section 9, Delegation to Act on Behalf of the Board, of the Regents' Rules and Regulations are also necessary to implement the Technology Transfer Commission's recommendations.

- Subdivision 9.222 would be revised so that licenses or other conveyances of intellectual property that have a value of more than \$1,000,000 may be signed by the institutional president, provided that the license or other conveyance has the prior approval of the appropriate Executive Vice Chancellor.
- Subdivision 9.291 would be revised to exclude from those contracts and agreements that must be approved by the Board via the docket or agenda sponsored research agreements and licenses or other conveyances of intellectual property prepared on an approved standard form or satisfying the requirements established by the Office of General Counsel.
- Subdivision 9.292 would be deleted. This section currently requires contracts and agreements for sponsored research with a corporation or other entity organized and operating under the laws of a foreign state to be approved by the Board via the docket or the agenda. The historical reason for this requirement was to assure compliance with state and federal reporting requirements. Component institutions now handle the reporting of those matters, so a centralized report is not necessary.

(See item C.1.)

**3. Policies and Guidelines for License Agreements, Sponsored Research, and Management and Marketing of Intellectual Property**

The Policies and Guidelines for License Agreements, Sponsored Research, and Management and Marketing of Intellectual Property would also be amended to implement the recommendations of the Technology Transfer Commission. The primary revision is the addition of sections acknowledging the authority granted by Chapter 153 of the Texas Education Code. This chapter, added in the last legislative session, authorizes technology transfer centers to perform certain activities. The revisions to the policies and guidelines permit the technology transfer offices to perform such activities provided that the institution complies with all relevant guidelines and policies. (See items C.3 and D.1.)

**4. Mission Statement**

One of the recommendations of the Technology Transfer Commission is to add technology development to the expressed missions of U. T. System and its component institutions. Staff recommends that each component institution consider including technology development in its mission statement. In addition, staff recommends that the mission statement for The University of Texas System be changed so that the third bullet point is revised to read as follows:

- *To engage in high-quality, innovative research that entails the discovery, dissemination, and application of knowledge and the development and commercialization of resulting technologies and inventions;*

(See item A.1.)

## **INFORMATIONAL ITEMS**

The following is a list of items that do not require Board action:

### **1. Technology Transfer Office at System Administration; Additional Attorney**

To assist the small component institutions in developing technology commercialization, the Technology Transfer Commission and the staff recommend the establishment of a technology transfer office within the Office of Business Affairs of System Administration. The office would consist of a technology transfer director and an administrative assistant. Estimated cost in the first year for the technology transfer office is \$304,000. (See item B.2.) In 1999, the Board approved a \$500,000 budget for the possible creation of a U. T. System Administration Technology Transfer Office. After consultant expenses associated with the Technology Transfer Commission initiative, sufficient funds remain to fund the technology transfer office in Business Affairs for the 2003 fiscal year.

Staff also recommends that after the first two years of operation of the System Administration technology transfer office, the component institutions that use the technology transfer office contribute to its funding on a graduated basis to be developed.

The Technology Transfer Commission and staff also recommend the addition of one attorney to the Office of General Counsel to assist with technology-related transactional matters at a first-year estimated cost of \$108,750. (See item B.2.)

### **2. Other Matters Not Requiring Board Action**

Several items that the Technology Transfer Commission recommended, but that require no action by staff or the Board of Regents, are noteworthy and are as follows:

- The Technology Transfer Commission recommended that representatives of U. T. System Administration and its component institutions appointed to the Governor's Council on Science and Biotechnology Development should make creation of seed capital for start-up companies their first priority. The Governor's Council has had one meeting in which it identified seed capital as one issue to be reviewed. (See item B.1.)
- The Technology Transfer Commission recommended that the creation of privatized corporations for the purpose of managing technology commercialization at component institutions be encouraged and facilitated. Staff, however, recommends that technology transfer offices consider the Technology Transfer Commission's recommendation and, if an office considers the establishment of a private corporation in the best interest of that institution's technology development efforts, the office should work with the institution's president and business officer and the Office of

General Counsel to develop a proposal to submit to the Board of Regents for approval. Section 153.004 of the Texas Education Code permits the establishment of such corporations. (See item C.3.)

- The Technology Transfer Commission recommended an expanded agenda for the existing Technology Management Council, to include sharing of best practices and other educational opportunities. In addition, staff recommends that instead of establishing the Technology Transfer Commission as a standing advisory committee, as suggested by the commission, the existing Technology Management Council serve as an advisory group with respect to policies and other matters pertaining to technology development. In that way, duplication of effort and creation of additional bureaucracy will be avoided. (See items B.4 and E.)
- The Technology Transfer Commission recommended that system-wide contracts be entered into for services that a number of the technology transfer offices might wish to obtain. Staff concurs that such a practice may result in greater efficiency and recommends that the Technology Management Council identify those services for which system-wide contracts are desired. (See item B.3.)
- The Technology Transfer Commission identified possible inconsistencies in the way leaves of absence are treated among the various component institutions. Staff recommends that the Technology Management Council review how each component institution treats leaves of absence and determine if there are inconsistencies between Board policy and a component institution's implementation of that policy. (See item C.2.)
- Staff recommends that the technology transfer offices of the three component institutions that Arthur Andersen studied prepare a report to their respective institutional presidents summarizing the component-specific recommendations and presenting a work plan for addressing those recommendations. By way of review, Arthur Andersen evaluated the technology transfer development operations at U. T. Austin, U. T. Southwestern Medical Center at Dallas, and U. T. M.D. Anderson Cancer Center. The full report of Arthur Andersen is included in Appendix D to the Technology Transfer Commission's report. (See introductory page to Final Staff Recommendations.)

### **3. Matters Requiring Further Study**

Other recommendations of the Technology Transfer Commission will require further study and evaluation. Those items include the following:

- The Technology Transfer Commission recommended that technology commercialization activity be a formal criterion for promotion and tenure considerations. Staff recommends that the Technology Transfer Commission recommendation be referred to the System Council and to the Faculty Advisory Council for study, evaluation and subsequent recommendation. Staff also wishes to clarify that the criterion would be only one of several to be used for promotion and tenure considerations and that a faculty member's failure to engage in technology commercialization activity would not be a negative factor in promotion and tenure considerations. (See item A.3.)

- The Technology Transfer Commission recommended that the current compensation sharing formula be revised from the current 50-50 split (between inventors and the component institution) to a 40/60 split between inventors (40 percent) and the institution (60 percent). In order to confirm that the proposed sharing formula is competitive with other major U.S. educational institutions, staff has requested additional data about the sharing formulas at other institutions of higher education. That data is not yet complete. Once the data is complete, staff will study it and make a subsequent recommendation to the Board of Regents and will present the data to the System Council. (See item A.4.)
- The Technology Transfer Commission recommended the encouragement of the creation of a biotechnology program within component institutions' schools of business administration. Staff recommends that the Office of Academic Affairs study, evaluate, and subsequently make a recommendation with respect to this matter. (See item B.5.)
- The Technology Transfer Commission recommended that a committee be established to assure compliance in operations and to provide jurisdiction in complicated issues dealing with conflicts of interest. An ad-hoc committee was created by the Office of General Counsel to review conflict of interest issues. Because the ad-hoc committee has not yet completed its work, staff believes it is premature to adopt the Technology Transfer Commission's recommendation. Rather, staff recommends that the Technology Management Council work with the ad-hoc committee to develop specific recommendations for the Board of Regents with respect to the management of conflicts of interest. (See item D.2.)
- The Technology Transfer Commission recommended that faculty and staff be allowed to take unpaid leaves of absence without first being required to take accrued vacation time. Such leaves of absence are not currently permitted by statute or by the Regents' Rules and Regulations. Staff recommends that the Office of Governmental Relations add this item to its deregulation efforts. (See item C.2.)

#### **4. Commission Recommendations Not Adopted by Staff**

Finally, certain recommendations of the Technology Transfer Commission are not recommended by staff for adoption. Those recommendations are: (1) directing component institutions to dedicate sufficient resources to their respective technology transfer offices, and (2) directing the component institutions to use funds received from technology transfer activities for the support of technology transfer operations and the funding of development stage projects. (See items A.2 and A.5.)

It is the staff's conclusion that because such funding decisions are made on a campus basis, the recommendations cannot be implemented at the System Administration level. It is, however, staff's opinion, that raising the visibility of technology development programs by inclusion of technology transfer operations data in the annual Key Statistical Report and in other annual reports, and the inclusion of technology commercialization activities in the mission of U. T. System and the component institutions should underscore the need for appropriate funding at the campus level for the technology transfer offices.

With respect to funding for the technology transfer offices, it should be noted that the Arthur Andersen report specifically recommended an increase of three to six full-time equivalents in the U. T. Austin technology transfer office (three professional and three support staff), and a \$600,000 increase in the legal budget of that office. (See introductory page to Final Staff Recommendations.)

The University of Texas System

Regents' Rules and Regulations

Part Two, Chapter XII  
Intellectual Property

**Sec. 1. Philosophy and Objectives** --~~While the discovery of patentable processes or inventions and the creation of other intellectual property is not the primary objective of the System, for any such discoveries or creations, it~~ It is the objective of the Board to provide an intellectual property policy that will encourage the development of inventions and other intellectual creations for the best interest of the public, the creator, and the research sponsor, if any, and that will permit the timely protection and disclosure of such intellectual property whether by development and commercialization after securing available protection for the creation, by publication, or both. The policy is further intended to protect the respective interests of all concerned by ensuring that the benefits of such property accrue to the public, to the inventor, to the System and to sponsors of specific research in varying degrees of protection, monetary return and recognition, as circumstances justify or require. Each component institution may develop in its Handbook of Operating Procedures additional policies and rules covering the subject matter of this Section not inconsistent with this Section or other policies or procedures adopted by the Board.

**Sec. 2. General Policy.**

- 2.1 The intellectual property policy shall apply to all persons employed by the U. T. System and the component institutions of the System (including, but not limited to, full and part time faculty and staff and visiting faculty members and researchers), to anyone using System facilities (~~under the supervision of System personnel~~), to undergraduates, to candidates for masters and doctoral degrees, and to postdoctoral and predoctoral fellows.
- 2.2 Except ~~as set forth~~ for intellectual property included in Subsections 2.3, 2.4 and 4.1 ~~[2.4]~~, this policy shall apply to and the Board may assert ownership in intellectual property of all types (including, but not limited to, any invention, discovery, trade secret, technology, scientific or technological development, research data and computer software) regardless of whether subject to protection under patent, trademark, copyright, or other laws.
- 2.3 The Board shall assert its interest in scholarly or educational materials, art works, musical compositions and dramatic and nondramatic literary works related to the author's academic or professional field, regardless of the medium of expression, as follows:
- 2.31 Students, professionals, faculty and researcher authors.-- The Board shall not assert ownership of works covered by this Subsection authored by students, professionals, faculty, and nonfaculty researchers. The Board encourages these authors to carefully manage their copyrights. The Board retains certain rights in these works as set forth in the Policy and Guidelines for Management and Marketing of Copyrighted Works.
- 2.32 Software.--The Board normally shall assert ownership in software as an invention; however, original software which is content covered by Subdivision 2.31, or that is integral to the



presentation of such content, shall be owned in accordance with Subdivision 2.31.

- 2.4 Notwithstanding the provisions of Subsection 2.3, the Board shall have sole ownership of all intellectual property created by an employee who was hired specifically or required to produce it or commissioned by the System or a component institution of the System. Except as may be provided otherwise in a written agreement approved by the chief administrative officer of the component institution~~and the Chancellor~~, the provisions of Subdivision 4.25~~Subdivision 5.23~~ relating to division of royalties shall not apply to intellectual property owned solely by the Board pursuant to this Subsection 2.4.
- 2.5 Any person who as a result of his or her activities creates intellectual property that is subject to this Policy, other than on government or other sponsored research projects where the grant agreements provide otherwise, should have a major role in the ultimate determination of how it is to be published; however, the chief administrative officer will decide in his or her sole discretion whether to develop and commercialize an invention~~made public, whether by publication, by development and commercialization~~ after securing available protection for the creation, if necessary~~or both~~.
- 2.6 The System, with the cooperation of the component institution, will provide review and management services for patentable inventions as well as other intellectual property either by its own staff, through a related foundation, or by other means.
- 2.7 It is a basic policy of the System that intellectual property be developed primarily to serve the public interest. This objective usually will require development and commercialization by exclusive licensing, but the public interest may best be promoted by the granting of nonexclusive licenses~~for the period of the patent~~. These determinations will be recommended and made in accordance with the administrative procedures hereinafter set out~~and with the approval of the Board~~.
- 2.8 Neither the facilities nor the resources of System or its component institutions may be used (i) to create, develop or commercialize intellectual properties unrelated to an individual's employment responsibilities (See Subsection 4.1); or (ii) to further develop or commercialize intellectual properties that have been released to an inventor (See Subdivision 4.22~~5.22~~) except as the component institution's chief administrative officer~~president and the appropriate Executive Vice Chancellor~~ may approve where System retains an interest under the terms of the release.
- 2.9 An employee whose research activities result in the creation of data that is owned by the Board pursuant hereto shall have a non-exclusive license to use such data for nonprofit educational, research and scholarly purposes within the scope of the employee's employment, subject to adherence to other provisions of this Policy.

**Sec. 3. ~~[Institutional] Intellectual Property Advisory Committees,~~ and Office of General Counsel~~, and UTIMCO~~.**

- 3.1 Intellectual Property Advisory Committees.--To help administer the intellectual property policy at each component institution and to make recommendations to chief administrative officers for further referral to the System Administration and

the Board (in those cases when action by the System Administration and/or the Board is required), departmental or institutional intellectual property advisory committees~~[Institutional Intellectual Property Advisory Committees]~~, may be established by the component institutions. ~~[Each institution at its option may use the term "Patent Advisory Committee" in lieu of "Intellectual Property Advisory Committee."]~~

3.2 Office of General Counsel.--The Office of General Counsel will assist component institutions with~~[have responsibility for]~~ all legal matters relating to intellectual property~~[and will assist component institutions with respect to such matters]~~. Among other responsibilities, the Office of General Counsel will help component institutions secure protection for intellectual property when appropriate and will police infringements; maintain central databases and files of patent applications, issued patents, copyrights, licenses and agreements; coordinate with component institutions in negotiating and preparing license and other agreements; and review and approve as to form all agreements relating to intellectual property~~]; and coordinate with and cooperate with UTIMCO in all such matters]~~.

~~[3.3] [UTIMCO.--UTIMCO will assist component institutions in business and financial matters relating to intellectual property; coordinate with component institutions in evaluating royalty and/or equity transactions and review and approve agreements relating to equity transactions; represent System on boards of directors of entities in which the Board holds equity and the right to a board position; serve as a repository for certificates of shares in entities in which the Board holds equity and represent the System's interest with respect thereto; and coordinate with and cooperate with the Office of General Counsel in all such matters.~~

#### **Sec. 4. Classification of Discoveries by Source of Support.**

4.1 Intellectual property that is unrelated to the individual's employment responsibility and has been developed as a result of the individual's efforts on his or her own time with no System support or use of System's facilities.

4.2 Intellectual property that is related to the individual's employment responsibility, or has resulted either from activities performed by the individual on System time, or with support by state funds, or from using System facilities.

4.3 Intellectual property that has resulted from research supported by a grant or contract with the Federal Government or an agency thereof, a nonprofit or for profit nongovernmental entity or by a private gift to the System.]

#### **Sec. 4[5]. Property Rights and Obligations.**

4.1[5-1] Intellectual property unrelated to the individual's employment responsibility that is developed on an individual's own time and without System support or use of System facilities ~~[(see Subsection 4.1)]~~is the exclusive property of the creator and the System has no interest in any such property and no claim to any profits resulting therefrom. Should the creator choose to offer the creation to the System, the chief administrative officer may~~[shall recommend whether the System should]~~ support and finance a patent application or other available

protective measures and manage the development and commercialization of the property under terms and conditions as may be agreeable to the parties. If the creator makes the offer after obtaining a patent or other protection, the chief administrative officer may ~~[shall recommend whether the System should]~~ reimburse the creator for expenses in obtaining such protection. ~~[If the chief administrative officer so recommends and the creation is accepted for management by the System, the procedures to be followed and the rights of the parties shall be those set out in Subdivision 5.23.]~~

4.2~~[5.2]~~ Intellectual property either related to the individual's employment responsibility, or resulting from activities performed on System time, or with support by state funds, or from using System facilities is subject to ownership by the Board. ~~[(See Subsection 2.2.)]~~

4.21~~[5.24]~~ Before intellectual property subject to ownership by the Board~~[covered by Subsection 4.2]~~ is disclosed to any party outside the System,~~[either]~~ to the public generally, or for commercial purposes, and before publishing same, the creator shall submit a reasonably complete and detailed disclosure of such intellectual property to the chief administrative officer of the creator's institution for determination of the System's interest. A component institution may establish guidelines in its Handbook of Operating Procedures for submitting different categories of intellectual property to its departmental or institutional intellectual property advisory committee~~[Institutional Intellectual Property Advisory Committee]~~ and procedures to be followed by the committee~~[Institutional Intellectual Property Advisory Committee]~~ in reviewing and evaluating such submissions. Such guidelines and procedures shall be consistent with this policy and shall be subject to approval as a part of the institutional Handbook. In those instances, however, where delay would jeopardize obtaining the appropriate protection for the property, the creator may request the approval of the chief administrative officer ~~[and the Office of General Counsel,]~~ to file a patent application or take other steps to obtain available protection prior to the administrative review provided in the following two subdivisions. If the request is granted, the creator may proceed with the filing of a patent application or other available protective measures pending the determination of the System's interest; provided, however, that the creator shall be reimbursed for reasonable expenses in filing the patent application or taking other steps to obtain protection as the parties may negotiate if the decision of the System is to assert and exploit its interests. Either the Chairman of the departmental or institutional intellectual property advisory committee~~[Institutional Intellectual Property Advisory Committee]~~ or the chief administrative officer shall notify the Office of General Counsel of any such application.

4.22~~[5.22]~~ If the chief administrative officer elects not to ~~[recommends that the System not]~~ assert and exploit System's~~[its]~~ interest, ~~[and that recommendation is approved by the Office of General Counsel,]~~ the Office of General Counsel and the creator shall be notified within one hundred eighty (180) days of the date of a complete submission that the invention will be released to the creator after which he or she will be~~[is]~~ free to obtain and exploit a patent or other intellectual

property protection in his or her own right and the System shall not have any further rights, obligations or duties with respect thereto except that, in appropriate circumstances~~[some instances]~~ the chief administrative officer~~[System]~~ may elect to impose certain limitations or obligations or retain income rights~~[, dependent upon the degree of System support involved in the creation of such property]~~.

4.23      The chief administrative officer may elect to release an invention to its creator at any time after asserting System's interest, with notice to the Office of General Counsel; however, such a release shall include provisions for the recovery of patent and licensing expenses, if any, the retention of income rights and other appropriate limits or obligations, as set forth above for creations in which the System's rights are never asserted.

4.24~~[5.23]~~      With respect to intellectual property in which the System asserts an interest, [the Office of General Counsel in consultation with] the chief administrative officer [(or his/her designee)] shall decide how, when, and where the intellectual property is to be protected~~[, if the System decides to patent or seek other available protection for such intellectual property, it]~~ and may proceed either through its own efforts or those of an appropriate private firm or attorney to obtain protection and manage the intellectual property. Outside counsel services may be contracted~~[Under appropriate circumstances, and]~~ with the consent of the Vice Chancellor and General Counsel and, if required by law, the approval of the Attorney General~~[, component institutions may arrange to have services to obtain protection for intellectual property performed by a local outside attorney on a case-by-case basis]~~. It shall be mandatory for all employees, academic and nonacademic, to assign the rights to intellectual property and patents to the Board when such creations fall within Subsection 4.2~~[5.2]~~.

4.25      In those instances where the System licenses rights in intellectual property to third parties, the costs of licensing, including the costs to operate and support a technology transfer office and departmental or institutional intellectual property advisory committees, and the costs of obtaining a patent or other protection for the property on behalf of the Board shall first be recaptured from any royalties or other license payments received by the System, and the remainder of such [royalty] income (including but not limited to license fees, prepaid royalties, [and] minimum royalties, running royalties, milestone payments and sublicense payments) shall be divided as follows:

50% to creator

50% to System.

With the prior approval of the Board as an agenda item, a component institution may include provisions in its Handbook of Operating Procedures to adjust the allocation of royalties set forth herein, but in no event shall the creator receive more than 50% or less than 25% of such proceeds. The division of royalties from patents or other intellectual property managed by an intellectual property management concern will be controlled by the terms of the System's agreement with such concern, as approved by the Board. Any other deviation from this rule requires the prior approval of the Board.

4.3~~[5-3]~~ Intellectual property resulting from research supported by a grant or contract with the Federal Government, or an agency thereof, with a nonprofit or for profit nongovernmental entity, or by a private gift or grant to the System shall be subject to ownership by the Board. [~~See Subsection 4.3.~~]

4.31~~[5-34]~~ Administrative approval of application requests to, and acceptance of grants or contracts with, the Federal Government or any agency thereof, with a nonprofit or for profit nongovernmental entity, or a private donor that contain provisions that are inconsistent with this policy, or other policies and guidelines adopted by the Board from time to time imply a decision that the value to the System of receiving the grant or performing the contract outweighs the impact of any nonconforming provisions of the grant or contract on the intellectual property policies and guidelines of the System.

4.32~~[5-32]~~ The intellectual property policies and guidelines of the System are subject to, and thus amended and superseded by, the specific terms pertaining to intellectual property rights included in federal grants and contracts, or grants and contracts with nonprofit and for profit nongovernmental entities or private donors, to the extent of any conflict.

4.33~~[5-33]~~ In those instances where it is possible to negotiate System-wide intellectual property agreements with the federal agencies or nonprofit and for profit nongovernmental entities or private donors and thereby obtain more favorable treatment for the creator and the System, every effort will be made to do so with the cooperation and concurrence of the Office of General Counsel after consultation with the institutional chief administrative officer.

4.34~~[5-34]~~ Employees of the System whose intellectual property creations result from a grant or contract with the Federal Government, or any agency thereof, with a nonprofit or for profit nongovernmental entity, or by private gift to the System shall make such assignment of such creations as is necessary in each case in order that the System may discharge its obligation, expressed or implied, under the particular agreement.

~~4.35~~~~[5-35]~~ In the event that two or more persons are entitled to share royalty income pursuant to Subdivision ~~4.25~~~~[5-23]~~ (or equity pursuant to Section 5[6]) and such persons cannot agree on an appropriate sharing arrangement as evidenced by a clear and unequivocal written agreement transmitted to the departmental or institutional intellectual property advisory committee, or if inventors are located at two or more component institutions, to the Office of General Counsel, that portion of the royalty income to which the creators are entitled under this Policy will be distributed to such persons in such portions as the institutional chief administrative officer or, in the event that the creators are located at two or more component institutions within the System, the Chancellor may deem appropriate under the circumstances and such decision shall be binding on the creators.

~~4.36~~~~[5-36]~~ A decision by the System to seek patent or other available protection for intellectual property covered by Subsection ~~4.2~~~~[5-2]~~ shall not obligate System to pursue such protection in all national jurisdictions. The System's decision relating to the geographical scope and duration of such protection shall be final.

**Sec. ~~5~~~~[6]~~. Equity Interests**

~~5.1~~~~[6-1]~~ In agreements with business entities relating to rights in intellectual property owned by the Board, the System may receive equity interests as partial or total compensation for the rights conveyed. In any such instance, the component institution where the intellectual property was created may elect, at its option~~[and with the concurrence of the Chancellor]~~, to share an equity interest, dividend income, or the proceeds of the sale of an equity interest with the creator(s) in the same manner as royalties are shared pursuant to Subdivision ~~4.25~~~~[5-23]~~. The System may also receive equity interests in a business entity as consideration for the component institution's role as a founder or co-founder of the business entity, and shall not be obligated to share such equity interests with the creator(s).

~~5.2~~~~[6-2]~~ [~~Consistent with Section 51.912, Texas Education Code, and subject to review and approval by the president of the component institution, the appropriate Executive Vice Chancellor, the Chancellor and the Board, employees]~~Employees of the System who conceive, create, discover, invent or develop intellectual property may hold an equity interest in a business entity that has an agreement with the System relating to the research, development, licensing or exploitation of that intellectual property only so long as the component institution where the intellectual property was developed is in full compliance with the requirements to have, implement and enforce for that employee an effective conflict of interest management plan approved by the component institution's chief administrative officer as set forth in "Procedure for Obtaining Approval of Plan to Manage Conflicts of Interest." In any case where actual conflict of interest is found, the employee may be required to divest the equity interest or terminate affected research.

~~5.3~~~~[6-3]~~ The System may negotiate, but shall not be obligated to negotiate, an equity interest on behalf of any employee as a part of an agreement between the System and a business entity relating to intellectual property conceived, created, discovered, invented, or developed by the employee and owned by the Board.

5.4~~[6-4]~~ Except as provided in Subsection 5.1, d~~[D]~~ividend income and income from the sale or disposition of equity interests held by the Board pursuant to agreements relating to intellectual property shall belong to the System and shall be distributed in accordance with the provisions of Section 9~~[40]~~.

5.5~~[6-5]~~ Dividend income and income from the sale or disposition of an equity interest held by a System employee pursuant to an agreement between the System and a business entity relating to rights in intellectual property conceived, created, discovered, invented or developed by such employee shall belong to the employee.

**Sec. 6**~~[7]~~. **Business Participation.**

6.1~~[7-1]~~ Any System employee who conceives, creates, discovers, invents or develops intellectual property ~~may~~~~[shall not]~~ serve as a member of the board of directors or other governing board or as an officer or an employee (other than as a consultant) of a business entity that has an agreement with the System relating to the research, development, licensing, or exploitation of that intellectual property only so long as the component institution where the intellectual property was developed is in full compliance with the requirements to have, implement and enforce for that employee an effective conflict of interest management plan approved by the component institution's chief administrative officer as set forth in "Procedure for Obtaining Approval of Plan to Manage Conflicts of Interest." In any case where actual conflict of interest is found, the employee may be required to terminate the business relationship or the relevant research~~[without prior review and approval by the chief administrative officer of the component institution, the Chancellor and the Board]~~.

6.2~~[7-2]~~ When requested and authorized by the Board, an employee may serve on behalf of the Board as a member of the board of directors or other governing board of a business entity that has an agreement with the System relating to the research, development, licensing or exploitation of intellectual property, but may not accept any consideration offered for service on such board.

**Sec. 7**~~[8]~~. **Reporting.**

~~[8-1]~~ Any employee covered by Subsections 5.2, 6.1, or 6.2~~[6-2, 7.1, or 7.2]~~ shall report in writing to the chief administrative officer of the component institution, or to such other person as may be designated by the chief administrative officer, the name of any business entity in which the person has an interest or for which the person serves as a director, officer or employee and shall be responsible for submitting a revised written report upon any change in the interest or position held by such person in such business entity. These reports shall be forwarded to the Vice Chancellor and General Counsel by October 1 of each year for filing with the Board as required by Section 51.912, Texas Education Code and inclusion in the annual financial report sent to the State officials listed in Section 51.005, Texas Education Code.

**Sec. 8**~~[9]~~. **Approval of and Execution of Legal Documents Relating to Rights in Intellectual Property.**

8.1~~[9-1]~~ Agreements that grant an interest in Board intellectual property may be executed and delivered in accordance with the provisions of the Regents' Rules and Regulations, Part Two, Chapter XI, following any required review by the Office of General Counsel.

8.2[9-2] Any document altering substantially the basic intellectual property policy of the System as set out in the preceding Sections and other policies and guidelines that may be adopted by the Board [~~shall have the advance approval of the component president, the appropriate Executive Vice Chancellor, the Chancellor, and the Board as an agenda item. Such an alteration in a sponsored research agreement shall not be considered substantial and the agreement]~~ may be executed and delivered as set forth in Section 8.1[9-4] if, in the judgment of the chief administrative officer[~~component president and with the concurrence of the appropriate Executive Vice Chancellor~~], the benefits from the level of funding for [~~the~~] proposed research and/or other consideration from a [~~the~~] sponsor, licensee or other party outweigh any potential disadvantage that may result from the policy deviation.

8.3[9-3] The Chancellor, the appropriate Executive Vice Chancellor, or the Vice Chancellor and General Counsel [~~or the authorized representative of UTIMCO~~] may execute, on behalf of the Board, legal documents relating to the Board's rights in intellectual property, including, but not limited to, declarations, affidavits, powers of attorney, disclaimers, and other such documents relating to patent applications and patents; applications, declarations, affidavits, affidavits of use, powers of attorney, and other such documents relating to trademarks; corporate documents related to the formation of new companies and other documents approved pursuant to Subsections 8.1[9-4] or 8.2[9-2]. The chief administrative officer or designee may execute, on behalf of the Board, institutional applications for registration or recordation of transfers of ownership and other such documents relating to copyrights.

**Sec. 9[40]. Income from Intellectual Property.**

9.1[40-1] The portion of the net income the System retains from royalties and any other intellectual property-related income shall be used by the component institutions where the income-producing creation originated for research and other purposes approved by the Board in accordance with standard budgetary policies. At the option of a component institution, such income may be accumulated in an endowment fund with the income to be distributed to the component institution for such purposes as may be approved by the Board.

9.2[40-2] With the prior written approval of the chief administrative officer of the component institution, payments[~~future royalties~~] payable to a faculty member pursuant to Subdivision 4.25[5-23] may be assigned to the component institution by the faculty member and designated for use in research to be conducted by such faculty member.

**Sec. 10[44]. Implementation of Intellectual Property Policy.**--The Office of General Counsel shall prepare and distribute to the component institutions such model agreements and recommended procedures as may be considered appropriate for the implementation of the provisions of this policy as well as other policies and guidelines adopted by the Board.

**Sec. 11[42]. Construction of Documents** --Unless otherwise required by law or the Regents' Rules and Regulations, each intellectual property agreement approved hereunder shall be construed in accordance with the Intellectual Property Policy in existence as of its approval date.



## The University of Texas System

### Regents' Rules and Regulations

#### Part One, Chapter I, Section 9, Delegation to Act on Behalf of the Board

9.22 All contracts or agreements, including purchase orders and vouchers, with a cost or monetary value to the U. T. System Administration or the component institution of more than \$1,000,000 must be approved by the Executive Committee of the Board or approved by the Board via the docket or the agenda except the following, which do not require prior approval by the Executive Committee of the Board or the Board regardless of the contract amount:

...

9.222 Contracts or grant proposals for sponsored research, including institutional support grants, ~~and~~[that do not include a] licenses or other [for or] conveyances of intellectual property owned or controlled by the Board; provided that licenses and other conveyances of intellectual property owned or controlled by the Board shall have the advance approval of the appropriate Executive Vice Chancellor.

...

9.29 The following contracts and agreements must be approved by the Board via the docket or the agenda, regardless of the contract amount:

9.291 Contracts and agreements of any kind or nature with a foreign government or agency thereof, except affiliation agreements and cooperative program agreements prepared on standard forms approved by the Office of General Counsel, and material transfer agreements, sponsored research agreements and licenses or other conveyances of intellectual property owned or controlled by the Board prepared on an approved standard form or satisfying the requirements set by the Office of General Counsel.

~~[9.292] [Contracts and agreements for sponsored research with a corporation or other entity organized and operating under the laws of a foreign state.]~~

9.292~~[9.293]~~ Agreements with a Chancellor, a president, a former Chancellor or president, an Executive Vice Chancellor, or a Vice Chancellor, subject to the provisions of Texas Education Code Section 51.946 or Texas Government Code Section 618.001 et seq.

...

## The University of Texas System

### Policies and Guidelines for License Agreements, Sponsored Research, and Management and Marketing of Intellectual Property

#### Intellectual Property License Agreements with Private Entities

##### Policy Statement

The Office of General Counsel shall develop a model license agreement for U. T. System intellectual property which agreement shall include, as a minimum, the guidelines set forth below. The model agreement shall be submitted to all potential licensees for U. T. System intellectual property and individuals involved in negotiation of license agreements shall endeavor to ~~[achieve utilization of]~~use the significant aspects of the model agreement for all licenses of intellectual property rights. It is understandable that under certain circumstances, it will not be possible to include all aspects of the model agreement in the final draft of a license.

No entity shall be granted the exclusive right to the development and/or commercialization of all intellectual property created at a U. T. System component institution without approval of the U. T. Board of Regents. Otherwise, agreements should grant rights only on a specific project basis.

The following guidelines ~~[shall be applicable]~~apply to license agreements with private entities including those formed primarily for the purpose of developing and/or commercializing intellectual property created at a U. T. System component institution:

##### Guidelines

- a. If an entity is granted the exclusive rights with respect to a particular invention, product, process or other item of intellectual property, the agreement should provide that such rights will revert to the U. T. Board of Regents in the event the entity fails to diligently develop and commercialize the property within a specified period of time that is appropriate to the particular circumstances.
- b. An entity that is granted exclusive rights to develop or commercialize intellectual property that is patentable should be required to reimburse the Board for all expenses incurred by the Board in obtaining a patent or, if a patent has not been obtained, should be required to prosecute and bear the expense of obtaining patent protection for the benefit of the Board and, in either event, the entity should be required to take all actions necessary, including litigation, to protect and preserve such patented rights from infringement.
- c. The U. T. System, the component institution, and the officers and employees of each should be protected and indemnified from all liability arising from the development, marketing, or use of the particular intellectual property.
- d. Restrictions on use by the component institution for research and teaching purposes and the publication rights of researchers should be minimized.
- e. The entity should be required to comply with all applicable federal, state, and local laws and regulations, particularly those concerning biological materials and necessary testing and approval by the Food and Drug Administration.
- f. The entity should be required to maintain confidentiality with regard to any unpatented technology or know-how.
- g. An entity that grants a license or sublicense to some other entity for property or technology that is in whole or in part derived from or based on that which is licensed to the entity by the Board, should be required to share with the U. T. System: 50% of any royalty received by the entity and 50% of any equity position to which the entity may be entitled.

- h. License agreements should contain such other provisions as may be determined to be in the best interest of the U. T. System by the Office of General Counsel.

## **Negotiation, Review and Approval of Sponsored Research Projects With Nonprofit and For Profit Nongovernmental Entities**

### **Guidelines**

U. T. System component institutions and individual faculty are encouraged to use their best efforts to obtain sponsored funding for research projects from governmental agencies as well as nonprofit and for profit nongovernmental entities. Each component institution should establish an appropriate organizational structure to solicit sponsors for research projects and to negotiate appropriate agreements with such sponsors with the assistance of the [~~Office of Asset Management and the~~]Office of General Counsel as provided below.

While it is recognized that sponsored research agreements with governmental entities and some nonprofit entities are not normally subject to change through negotiation, the Office of General Counsel shall develop a model sponsored research agreement that the component institution shall submit to all other potential sponsors for research projects.

~~[Additionally, in its *Handbook of Operating Procedures*, each U. T. System component institution shall devise a system for early identification of proposed sponsored research projects that: (a) have potential for significant research results that may be marketable; and (b) are being developed by sponsors who are unwilling to utilize the significant aspects of the model agreement. Review currently conducted by the Office of the Chancellor and the Office of the U. T. System Comptroller with regard to the appropriateness of any financial obligations on the part of the U. T. System or its component institutions will be continued and, in addition, all sponsored research agreements evolving from the early identification procedure shall be reviewed and approved by the Office of Asset Management and the Office of General Counsel prior to submission to the Board for approval in the institutional docket. In order to facilitate such review and approval, the Office of Asset Management and the Office of General Counsel should be consulted at an early stage with regard to the negotiation of the terms that deviate from the model agreement. The Office of the Chancellor, the Office of Asset Management, and the Office of General Counsel shall adopt procedures that insure prompt review and response so that important research projects are not delayed by U. T. System Administrative involvement.]~~

It is particularly important that the following guidelines be adhered to if at all possible in sponsored research agreements with nonprofit and for profit nongovernmental entities:

- a. The U. T. System Board of Regents should own the rights to all patentable discoveries, unpatentable technology, technical know-how, and other intellectual property that results from the research project.
- b. The sponsoring entity may have an option for either an exclusive or non-exclusive right to a license to develop and commercialize any intellectual property resulting from the project for a royalty in an amount to be negotiated.
- c. In the event the sponsor exercises the option for a license, it should be required to reimburse the Board for all expenses incurred with respect to a patent that has been secured on any patentable discovery or, in the event a patent has not been obtained, the sponsor should be required to bear the expense of securing patent protection for the benefit of the Board.
- d. The rights of researchers to publish scholarly work with respect to the research project should be restricted only to the extent necessary to protect the potential value of any discovery resulting from the research.
- e. The agreement should contain appropriate indemnification from the sponsor for all damage or liability that may result when a research project involves the use of materials, processes, or procedures that are furnished by or required by the sponsor to be used in such project and such damage or liability is not due to negligence of the persons performing the research.

- f. License agreements that result from the exercise of options in the sponsored research contracts are subject to the approval [of the Board through the docket] as set forth in the Intellectual Property Policy and should contain [provisions for the reversion to the Board of all rights to the intellectual property if it is not developed and marketed in a timely manner] the provisions set forth in the model license agreement provided by the Office of General Counsel, pursuant to the policy statement and guidelines for agreements licensing U. T. System intellectual property.

### **Management and Marketing of Intellectual Property**

The U. T. System Board of Regents finds that intellectual property and technology created at the component institutions are valuable assets with potential for commercialization for the benefit of the citizens of the state, state government, the component institutions, and the U. T. System.

Currently existing technology transfer offices shall constitute "Centers" as defined in Texas Education Code, Chapter 153, Section 153.001 (1); System Administration and any component institution that does not have a Center is authorized to create one.

Such Centers may continue to perform the activities set forth in Sections 153.004 (1), (2), (3) and (4) and Section 153.006 in accordance with the Intellectual Property Policy, these and other Intellectual Property Guidelines and all other relevant Board policies.

Centers may also engage in activities set forth in Sections 153.004 (5), (6), (7) and (8) in accordance with the Intellectual Property Policy, these and other Intellectual Property Guidelines and all other relevant Board policies; provided, however, that institutional ownership interests in such entities established and operated pursuant to Section 153.004 (7) shall belong to the Board.

Centers may institute and operate programs as described in Section 153.005 (a) in accordance with the criteria required to be established by components and approved by the Board, as set forth in Section 153.006, and in accordance with the Intellectual Property Policy, these and other Intellectual Property Guidelines and all other relevant Board policies.

Component institutions shall provide the information required by Section 153.008 and such other information as may be necessary or desirable to evaluate the success of technology commercialization throughout the U. T. System.

As a part of its Handbook of Operating Procedures, each component institution of the U. T. System shall adopt procedures for identifying, evaluating, and marketing intellectual property and technology created at the component institution:

- a. that are not already subject to an option or license pursuant to a sponsored research agreement;
- b. that have not been committed to an entity, including those formed for the primary purpose of development and commercialization of intellectual property created at the component institution; or
- c. the control of which has been regained by the U. T. System through reversion provisions contained in license agreements.

The intellectual property management and marketing procedures that are to be included in institutional Handbooks of Operating Procedures shall ~~[contain provisions that recognize and provide the opportunity for the creator and other knowledgeable institutional personnel to play a major role in marketing while making]~~ make provision for appropriate involvement of the Office[s] of ~~[Asset Management and]~~ General Counsel in the management and marketing of the assets of the Board.

~~[In developing handbook procedures, consideration should be given to the utilization of the Center for Technology Development and Transfer at The University of Texas at Austin (established by Section 65.45, Texas Education Code) as a means of developing and marketing available intellectual property created at component institutions.~~

~~The Office of General Counsel shall continue to assist in marketing efforts through its activities, such as submitting available intellectual property and technology to appropriate computer data listing services, and to publications that reach prospective licensees.~~

~~The Office of Asset Management shall develop appropriate expertise in the area of marketing of technology to complement the efforts of the component institutions and the Office of General Counsel.~~

~~On a selective basis, the Office of General Counsel and Office of Asset Management with the concurrence of the component institution, may utilize the services of intellectual property marketing agencies pursuant to contractual agreements that have been approved by the Board.]~~

# The University of Texas System

## Mission Statement

The mission of The University of Texas System is to provide high-quality educational opportunities for the enhancement of the human resources of Texas, the nation, and the world through intellectual and personal growth.

This comprehensive mission statement applies to the varied elements and complexities of a large group of academic and health institutions. Individually, these institutions have distinct missions, histories, cultures, goals, programs, and challenges. Collectively, these institutions share a common vision and a fundamental commitment to enhance the lives of individuals and to advance a free society. Through one or more of its individual institutions, The University of Texas System seeks:

- To provide superior, accessible, affordable instruction and learning opportunities to undergraduate, graduate, and professional school students from a wide range of social, ethnic, cultural, and economic backgrounds, thereby preparing educated, productive citizens who can meet the rigorous challenges of an increasingly diverse society and an ever-changing global community;
- To cultivate in students the ethical and moral values that are the basis of a humane social order;
- To engage in high-quality, innovative research that entails the discovery, dissemination, and application of knowledge and the development and commercialization of resulting technologies and inventions;
- To render service to the public that produces economic, technical, social, cultural, and educational benefits through interactions with individuals and with local, Texas, national, and international organizations and communities;
- To provide excellent, affordable, and compassionate patient care through hospitals and clinics that are of central importance to programs of teaching, scholarship, research, and service associated with medicine and related health sciences;
- To enrich and expand the appreciation and preservation of our civilization through the arts, scholarly endeavors, and programs and events which demonstrate the intellectual, physical, and performance skills and accomplishments of individuals and groups;
- To serve as a leader of higher education in Texas and to encourage the support and development of a superior, seamless system of education – from pre-kindergarten through advanced post-graduate programs, and encompassing life-long learning and continuing education.

To accomplish its mission, The University of Texas System must:

- Attract and support serious and promising students from many cultures who are dedicated to the pursuit of broad, general educational experiences, in combination with the pursuit of areas of personal, professional, or special interest;
- Acquire, retain, and nourish a high-quality, dedicated, diverse faculty of competence, distinction, and uncompromising integrity;
- Recruit and appropriately recognize exemplary administrators and staff members who provide leadership and support of the educational enterprise in an energetic, creative, caring, and responsible manner.
- Create and sustain physical environments that enhance and complement educational goals, including appropriate classrooms, libraries, laboratories, hospitals, clinics, computer and advanced technological facilities, as well as university centers, museums, performance facilities, athletic spaces, and other resources consistent with institutional objectives;
- Encourage public and private-sector support of higher education through interaction and involvement with alumni, elected officials, civic, business, community and educational leaders, and the general public.

# The University of Texas System

## Final Staff Recommendations Regarding the Report of the U. T. System Technology Transfer Commission

### Worksheet A.

#### ***Issue Identified by TTC:***

The component institutions of U. T. System comprise the dominant technology generator within the state of Texas. This core of intellectual property, properly commercialized, can drive the development of an entirely new industry within our state, an observation that has recently resulted in significant support for this initiative by the legislative and executive branches of the Government of the State of Texas. In addition, it can be expected that proactive development of the technologies within the institutions of U. T. System will provide a highly significant revenue stream to the fostering components. Texas, however, faces broad competition for development of this sector. U. T. System thus needs to join with state and local initiatives to promote and facilitate this development activity. Currently, the degree of commitment to technology development by components of the U. T. System is highly variable and needs to be emphasized as a System-wide priority.

#### ***TTC Recommendation:***

##### **A. MAKE COMMERCIALIZATION OF TECHNOLOGIES A SYSTEM-WIDE PRIORITY**

1. Add technology development to the expressed missions of U. T. System and its components.
2. Insure that component institutions with mature research programs dedicate sufficient resources to their respective TTOs.
3. Make technology commercialization activity a formal criterion for promotion and tenure considerations.
4. Modify the current compensation sharing formula to increase the institutional incentives for technology commercialization; in cases of cash compensation, a 40/60 split between inventors (40%) and the component (60%) is recommended.
5. Obligate a portion of the institutional share of net compensation to support of technology transfer operations and funding of development stage projects with imminent and apparent commercialization potential.



Final Staff Recommendations  
**Worksheet A.1.**

**Issue Identified by TTC:**

Currently, the Regents' Rules and Regulations except technology development from the core missions of U. T. System.

**TTC Recommendation:**

**A.1. Add technology development to the expressed missions of U. T. System and its components.**

**Action Recommended by TTC:**

Amend Regents' Rules and Regulations, Part Two, Ch. XII, § 1 as provided in Appendix G.

**Law, Rule, or Policy Affected:**

Regents' Rules and Regulations, Part Two, Ch. XII, § 1.

**Pro:**

Aligns Regents' Rules and Regulations with expressed interests of Board of Regents, Governor, and Texas Legislature by establishing technology development as a core mission of U. T. System.

**Con:**

None identified.

**Cost:**

None identified.

**Issues Raised:**

None identified.

**Staff Recommendation:**

1. Adopt the TTC recommendation and amend Regents' Rules and Regulations, Part Two, Ch. XII, § 1 as provided in Appendix G.
2. In addition, each component institution and System Administration should consider including technology development in its mission statement; suggested revisions to the U. T. System Administration mission statement appear on the attached pages. This issue should be referred to the System Council at its July 2002 meeting.

Final Staff Recommendations  
**Worksheet A.2.**

**Issue Identified by TTC:**

Formal review of TTO operations within selected U. T. components revealed that there is significant variance in administrative and financial support for technology development between campuses, and that insufficient resources are retarding performance of these offices in some instances, as indicated in the report by Arthur Andersen.

**TTC Recommendation:**

**A.2. Insure that component institutions with mature research programs dedicate sufficient resources to their respective TTOs.**

**Action Recommended by TTC:**

The Board of Regents should periodically assess the performance of component institutions in technology development activities to assure that adequate resources have been made available for this activity.

**Law, Rule, or Policy Affected:**

Appropriations Act, sections pertaining to each institution, if financial resources are to come from state appropriations.  
Appropriations Act, Art. IX, § 6.14, if additional FTEs are planned.

**Pro:**

1. Increasing resources will close gap between comparable institutions and should lead to better performance of TTO.

**Con:**

1. Financial resources are limited.
2. Each institution has set its own priorities.

**Cost:**

Per AA report, cost for U. T. Austin is at least (a) \$600,000 for increase to legal budget and (b) three to six FTEs (3 professional and 3 support staff).

**Issues Raised:**

1. What is the basis for assessing performance? In other words, are there measurable standards?
2. What constitutes “adequate resources”?
3. How does the Board communicate this expectation to the institution and how is it enforced?
4. Are there other institutions besides U. T. Austin that currently need additional resources?

**Staff Recommendation:**

1. Because there is no mechanism for “insuring” sufficient resources to the TTOs, staff does not recommend adopting the TTC recommendation. Raising the visibility of the technology development programs at the component institutions by including the Association of University Technology Managers data in the annual Key Statistical Report and in other annual reports should benefit the TTOs. The proposed amendments to the Policies and Guidelines, as provided in Appendix F, require component institutions to provide data annually on technology commercialization in the U. T. System.

Final Staff Recommendations  
**Worksheet A.3.**

**Issue Identified by TTC:**

Currently tenure and promotion considerations focus on teaching, research, academic publication, and excellence in provision of services; intensive and successful participation in technology development by faculty is not so recognized. This ignores the enormous impact that successful product development can have on society.

**TTC Recommendation:**

**A.3. Make technology commercialization activity a formal criterion for promotion and tenure considerations.**

**Action Recommended by TTC:**

Amend institutional Handbook of Operating Procedures to include technology development and commercialization as a criterion on which promotion and tenure decisions are based.

**Law, Rule, or Policy Affected:**

Regents' Rules and Regulations, Part One, Ch. III, § 6 (no changes anticipated)  
Institutional Handbook of Operating Procedures

**Pro:**

1. Consistent with Board's emphasis on technology transfer as a core mission of U. T. System.

**Con:**

1. Possible resistance by some faculty.

**Cost:**

None identified.

**Issues Raised:**

1. How is this recommendation implemented over the entire System?
2. Should this issue be raised with Faculty Advisory Council?

**Staff Recommendation:**

1. Refer the TTC recommendation to the System Council and to the Faculty Advisory Council for study, evaluation and subsequent recommendations. Dr. Dennis Stone should coordinate the referral with Dr. Ed Sharpe.
2. Clarify that technology commercialization is only one of several criteria to be used for promotion and tenure considerations and that a faculty member's failure to engage in technology commercialization will not negatively affect promotion and tenure opportunities.

# Final Staff Recommendations

## Worksheet A.4

(Page 1 of 2)

**Issue Identified by TTC:**

The current 50/50 sharing of net compensation between inventors and component institutions far exceeds the sharing agreements of almost every other major U.S. university system. The costs of supporting technology transfer offices (TTOs) during development years are extensive and the average time for such offices to reach a 'break-even' point exceeds 10 years. Component institutions often view this investment requirement as a disincentive to providing needed resources.

**TTC Recommendation:**

**A.4. Modify the current compensation sharing formula to increase the institutional incentives for technology commercialization; in cases of cash compensation, a 40/60 split between inventors (40%) and the component (60%) is recommended.**

**Action Recommended by TTC:**

Amend Regents' Rules and Regulations, Part Two, Ch. XII, § 5.23, as provided in Appendix G.

**Law, Rule, or Policy Affected:**

Regents' Rules and Regulations, Part Two, Ch. XII, § 5.23.

**Pro:**

1. Provides additional funds for technology transfer operations at institutions.
2. Sharing formula is competitive with other major U.S. educational institutions (see pp. 104-105 of Arthur Andersen report).
3. Component institutions may find it difficult to change the sharing formula on a campus-by-campus basis.

**Con:**

1. Resistance from faculty is likely to be strong.
2. Faculty may contend that reduced percentage to inventor may serve as a disincentive in recruiting faculty and may result in loss of some faculty.
3. Regents' Rules and Regulations already permit individual institutions to change the 50-50 split, with the consent of the Board.

**Cost:**

Costs associated with loss and replacement of faculty.

**Issues Raised:**

1. Is there to be an amendment to the Regents' Rules and Regulations to require that institutions use a portion of increased proceeds for technology transfer projects?
2. All existing divisions should be grandfathered.
3. Need additional data on sharing rates at comparable institutions.

## Final Staff Recommendations

### **Worksheet A.4.**

(Page 2 of 2)

#### ***Staff Recommendation:***

1. Final staff recommendation is contingent on the data to be gathered about the sharing formulas of other institutions of higher education and a determination as to whether that data supports the proposition that the proposed sharing formula is competitive with other major U. S. education institutions.
2. Also contingent on the data to be gathered, staff recommends presenting the data, once gathered, to the presidents of the component institutions, presenting the TTC recommendation to the System Council at its July 2002, meeting, and advising Executive Officers of the staff's recommendation.

Final Staff Recommendations  
**Worksheet A.5.**

**Issue Identified by TTC:**

In order to maximize the chances of success in commercialization activities, the financial gains from such ongoing activities need to be reinvested in the process.

**TTC Recommendation:**

**A.5. Obligate a portion of the institutional share of net compensation to support of technology transfer operations and funding of development stage projects with imminent and apparent commercialization potential.**

**Action Recommended by TTC:**

Amend Regents' Rules and Regulations, Part Two, Ch. XII  
Amend policies within component institutions in compliance with Regents' Rules and Regulations.

**Law, Rule, or Policy Affected:**

Regents' Rules and Regulations, Part Two, Ch. XII  
Institutional policies (not identified).

**Pro:**

1. Demonstrates to faculty that change from 50-50 split to 60-40 split is intended to provide other benefits to faculty.

**Con:**

1. Faculty may perceive that they have lost funds while TTO has gained additional funds for administration.

**Cost:**

None identified.

**Issues Raised:**

1. How are institutions "obligated" to use a portion of funds for development stage projects? Does amendment to the Regents' Rules and Regulations, Part Two, Ch. XII, § 5.23 to require recovery of costs to operate and support a TTO include such efforts?
2. Arthur Andersen recommended that a portion of institution's share should go to inventor's lab. What is commission's position on that recommendation?

**Staff Recommendation:**

1. Because decisions about the funding mechanism for technology transfer operations are made at the component institution level, staff does not recommend adopting the TTC recommendation. The greater visibility of and emphasis on technology development, however, should underscore the need for each component institution to adequately fund technology transfer operations. The TTC recommendation regarding use of the institution's share of net proceeds should be considered as a good use of the funds.

## Final Staff Recommendations Worksheet B.

### ***Issue Identified by TTC:***

The individual TTOs of the components of U. T. System differ in their relative maturity and in their particular needs. The more mature TTOs are constrained in their ability to launch startup companies by the difficulty of attracting venture capital to Texas and by the shortage of individuals with proven senior management expertise in biotechnology. Some institutions are only beginning to participate in technology transfer activities and lack local resources necessary to effectively commercialize technologies developed at their respective institutions.

Although the majority of TTO activities are most effectively conducted by the autonomous operation of individual TTOs in the environment and culture of their host institutions, certain resources can be more efficiently provided through a centralized TTO housed administratively within U.T System. This office would result in less net cost to all of U. T. component institutions than would duplicate services created by each individual component.

### ***TTC Recommendation:***

#### **B. PROVIDE CENTRALIZED RESOURCES**

1. Work in coordination with the Texas Legislature and other Texas universities to facilitate the development of venture capital funds for support of Texas-based startup companies that result from technologies developed at universities within Texas.
2. Create an administrative and professional unit within the Office for Business Affairs for the purposes of managing licensing activities of small component institutions and to facilitate service contract procurement. Expand staff within the Office of General Counsel to accommodate increasing load and to provide a dedicated resource for small components.
3. Identify and implement open contracts whereby TTOs within components can contract with essential service providers (auditors and consultants) without a *per* instance requirement for RFP submissions.
4. Establish quarterly meetings for technology transfer officers to facilitate staff education and sharing of best practices.
5. Encourage the creation of a biotechnology program within component schools of business administration.

Final Staff Recommendations  
**Worksheet B.1.**

**Issue Identified by TTC:**

Meetings with numerous East- and West-coast biotechnology venture groups have revealed that such firms are more critical in their assessment of Texas-based startups than in their review of companies located in environments with established infrastructure; especially, the lack of Texas-based venture funds that might co-invest in Texas companies has been cited as a major barrier in securing non-Texas venture capital. Creation of a biotechnology industry in Texas requires the coordinated efforts of many institutions and agencies. U. T. System, as the dominant generator of technologies, needs to work proactively with other institutions and agencies to facilitate this development.

**TTC Recommendation:**

**B.1. Work in coordination with the Texas Legislature and other Texas universities to facilitate the development of venture capital funds for support of Texas-based startup companies that result from technologies developed at universities within Texas.**

**Action Recommended by TTC:**

The representatives of U. T. System and its component institutions appointed to the Governor's Council on Science and Biotechnology Development should make creation of seed capital for startup companies their first priority.

**Law, Rule, or Policy Affected:**

Unidentified legislation may be required, depending on what is proposed.

**Pro:**

1. Availability of funds would encourage growth of start-ups.

**Con:**

1. Limited state resources
2. Unlikely that state pension funds or other state funds, such as the Permanent School Fund or the Permanent University Fund, would be available for such investments.

**Cost:**

Significant, but not yet identified.

**Issues Raised:**

1. How is seed capital to be "created"? What sources of funds are available?
2. Data is needed regarding amount of seed capital needed and expected results.

**Staff Recommendation:**

1. Staff supports the action recommended by the TTC, but with the clarification that an *evaluation of the need* for the creation of seed capital should be a part of the process of the council's consideration of the issue of creation of seed capital. No action by the Board of Regents or staff is required.



# Final Staff Recommendations

## Worksheet B.2.

(Page 1 of 2)

### **Issue Identified by TTC:**

The financial commitment to supporting a TTO in its development stage can be extensive. Currently, many components lack a TTO with staff versed in appropriate domain expertise for all steps in the technology development process. Creation of a central office with the resources necessary for all stages of the technology development process would serve as a valuable and efficient means through which components with small TTOs could fully participate in commercialization of their individual technologies.

### **TTC Recommendation:**

**B.2. Create an administrative and professional unit within the Office for Business Affairs for the purposes of managing licensing activities of small component institutions and to facilitate service contract procurement (see B.3. below). Expand staff within the Office of General Counsel to accommodate increasing load and to provide a dedicated resource for small components.**

### **Action Recommended by TTC:**

Establish TTO in the Office of Business Affairs and hire a director and an administrative associate.

Hire one additional attorney in the Office of General Counsel.

### **Law, Rule, or Policy Affected:**

Appropriations Act, Art. IX, §6.14 regarding limitations on FTE increases.

### **Pro:**

1. Additional, centralized resources should help smaller institutions to develop technology transfer operations.

### **Con:**

1. Cost
2. Additional FTEs may exceed cap.

### **Cost:**

Per Appendix H:

Year 1: Estimated \$304,000 for TTO in Office of Business Affairs and \$108,750 for additional attorney in Office of General Counsel

Subsequent Years: Decrease of approximately \$30,000 in patent prosecution costs in Year 2, but increases in personnel costs in Year 2 and subsequent years.

### **Issues Raised:**

1. Is TTC Report inconsistent regarding duties of new attorney? Appendix B, Small Component Assessment, identifies need for attorney for legal assistance in preparation and negotiation of start-ups, particularly with regard to securities matters. Appendix H, Budget, refers to attorney for technology transfer transactions (i.e., contracts?).

## Final Staff Recommendations

### **Worksheet B.2.**

*(Page 2 of 2)*

***Staff Recommendation:***

1. Adopt the TTC recommendation to establish a TTO in the Office of Business Affairs (OBA) and hire a director and an administrative associate and hire one additional attorney in the OGC.
2. In addition, require that, after the first two years of operation of the TTO in the OBA, the component institutions that use the TTO contribute to its funding on a graduated basis to be developed.

Final Staff Recommendations  
**Worksheet B.3.**

**Issue Identified by TTC:**

Currently, no TTO within the component institutions of U. T. System is in compliance with good business practices in auditing licensees. Market assessment for the purpose of licensing valuable technologies and launching startup companies often requires contracting with consultants for specialty expertise. A critical barrier to contracting with auditors and consultants is the existing requirement that each engagement be solicited through an RFP process.

**TTC Recommendation:**

**B.3. Identify and implement open contracts whereby TTOs within components can contract with essential service providers (auditors and consultants) without a per instance requirement for RFP submissions.**

It is recommended that the central TTO office negotiate annual contract agreements with such service providers, as is currently done with law firms providing patent prosecution and management services. Under this format, an individual component TTO office would be allowed to execute license- and deal-specific contracts with these pre-approved service providers without requirement for the RFP process. It is expected that component TTOs would be financially responsible for payment for the services rendered under such deal-specific contracts.

**Action Recommended by TTC:**

The TTO of U. T. System would negotiate System-wide contracts with service providers for those services that institutions have identified.

**Law, Rule, or Policy Affected:**

Texas Government Code Chapters 2155 and 2254 (no changes anticipated).

**Pro:**

1. Expedites access to service providers.
2. System-wide contract may result in lower rates.

**Con:**

1. Unless actual needs are identified, system-wide contracts may not be used by institutions and then become a wasted effort.

**Cost:**

Depends on services used. Cost would be paid by institution accessing the services.

**Issues Raised:**

1. Need to specifically identify those services that institutions are most likely to use.

**Staff Recommendation:**

1. Adopt the TTC recommendation. No Board of Regents action is required.
2. The Technology Management Council should identify those services for which system-wide contracts are desired.

Final Staff Recommendations  
**Worksheet B.4.**

<b>Issue Identified by TTC:</b>
<b>TTC Recommendation:</b> <b>B.4. Establish quarterly meetings for technology transfer officers to facilitate staff education and sharing of best practices.</b>
<b>Action Recommended by TTC:</b> Modify the agenda of the existing University of Texas Technology Management Council (UTTMC) to consist of quarterly meetings held in Austin under joint direction by the TTOs of U. T. System and its individual components.
<b>Law, Rule, or Policy Affected:</b> None.
<b>Pro:</b> 1. Sharing of best practices and provision of staff development opportunities should improve overall quality of technology transfer system-wide.
<b>Con:</b> None identified.
<b>Cost:</b> Travel expenses to be incurred by institutions.
<b>Issues Raised:</b> None identified.
<b>Staff Recommendation:</b> 1. Adopt the TTC recommendation. No Board of Regents action is required.

Final Staff Recommendations  
**Worksheet B.5.**

**Issue Identified by TTC:**

Lack of entrepreneurs with proven expertise in biotechnology remains the dominant barrier to the launch of start up companies in Texas.

**TTC Recommendation:**

**B.5. Encourage the creation of a biotechnology program within component schools of business administration.**

**Action Recommended by TTC:**

Sub-programs within existing component schools of business administration could fill this need. Course work and training could be jointly developed with components having health care and biotechnology research and development initiatives.

**Law, Rule, or Policy Affected:**

Institutional Handbook of Operating Procedures

Institutional Course Catalogs

Texas Education Code § 61.051 requires Coordinating Board approval of any new degree programs.

Texas Education Code § 61.052 requires institutions to notify the Coordinating Board at the time the institution begins planning a new degree program.

Texas Education Code § 61.055 establishes criteria for partnership between academic and health components and requires approval of the Coordinating Board.

**Pro:**

1. An avenue to advance core mission of technology development.

**Con:**

1. Limited resources

**Cost:**

Unknown at this time. Potential costs include additional faculty.

**Issues Raised:**

1. Which institution(s) would be the most likely location for such a degree program?
2. What would be the curriculum?
3. Are there such degree programs at other Texas institutions currently?
4. Has commission confirmed that no such degree programs currently exist at U. T. institutions?

**Staff Recommendation:**

1. Refer the TTC recommendation to Academic Affairs for further study, evaluation and subsequent recommendations. Dr. Dennis Stone should coordinate with Dr. Ed Sharpe.

## Final Staff Recommendations Worksheet C.

### ***Issue Identified by TTC:***

Many of the existing rules, regulations, policies and guidelines governing technology development activities were generated at a time when the launch of startup companies was not an initiative of component institutions of U. T. System. While many of these governances have been useful and appropriate for the regulation of traditional out-licensing activities of TTOs, they create unforeseen problems in the negotiations necessary to launch startup companies. Modification of these governances would allow component TTOs to operate in a more timely and business-like manner in startup launches.

### ***TTC Recommendation:***

#### **C. ENABLE ADDITIONAL FREEDOM TO OPERATE AT THE COMPONENT LEVEL.**

1. Allow component institutions to have final signatory authority for licenses exceeding \$1mm in upfront payments, licenses to foreign entities, and management of conflict of interest in equity-based licenses. It is proposed that final approval for such agreements not await formal approval at standing Board of Regents meetings, provided that such agreements have been reviewed and approved by appropriate authorities at U. T. System and designated component officers.
2. Modify and clarify outside employment and leave of absence policies to better enable faculty and staff to facilitate transfer of university technologies to commercial entities.
3. Encourage and facilitate the creation of privatized corporations for the purpose of managing technology commercialization at components with advanced technology transfer programs.

# Final Staff Recommendations

## Worksheet C.1.

(Page 1 of 2)

### **Issue Identified by TTC:**

Currently, final approval of these particular items requires approval at quarterly meetings of the Board of Regents of the University of Texas System. The timing of the need to execute documents necessary for the launch of startup companies and major license agreements frequently is not coincident with the scheduled meetings of the Board of Regents. This can result in lost interest in the case of major license agreements, and also jeopardize closure of the deals themselves. (For instance, financing of a startup company might be delayed for three months after all parties have reached an agreement – a real scenario that is ill-received by venture capitalists.) All such items have already been reviewed by the Office of General Counsel (and in some instances, additionally by the Vice-Chancellor for Health Affairs) prior to submission to the Board of Regents for review.

### **TTC Recommendation:**

**C.1. Allow component institutions to have final signatory authority for licenses exceeding \$1mm in upfront payments, licenses to foreign entities, and management of conflict of interest in equity-based licenses. It is proposed that final approval for such agreements not await formal approval at standing Board of Regents meetings, provided that such agreements have been reviewed and approved by appropriate authorities at U. T. System and designated component officers.**

### **Action Recommended by TTC:**

Modify Regents' Rules and Regulations, Part One, Ch. I, § 9, as indicated in Appendix G2.

Modify Regents' Rules and Regulations, Part Two, Ch. XII, §§ 6.2 and 7.1, as indicated in Appendix G.

### **Law, Rule, or Policy Affected:**

Regents' Rules and Regulations, Part One, Ch. I, § 9.

Regents' Rules and Regulations, Part Two, Ch. XII, §§ 6.2 and 7.1.

### **Pro:**

1. Provides greater flexibility.
2. Enables quicker turnaround time on transactions.

### **Con:**

1. Removes Board oversight of what may be significant contracts (although the option remains to take any contract to the Board for approval).

### **Cost:**

None identified.

### **Issues Raised:**

1. For clarity, revised Section 9.222 should add "licenses and other" before "conveyances" in the clause after the semicolon.

## Final Staff Recommendations

### **Worksheet C.1.**

*(Page 2 of 2)*

***Staff Recommendation:***

1. Adopt the TTC recommendation and amend Regents' Rules and Regulations, Part One, Ch. I, § 9, as indicated in App. G2 and Regents' Rules and Regulations, Part Two, Ch. XII, §§ 6.2 and 7.1, as indicated in App. G. All current reviews of contracts and conflicts of interest management plans by OGC and the appropriate Executive Vice Chancellors, or their delegates, continue unchanged.



## Final Staff Recommendations

### Worksheet C.2.

(Page 1 of 2)

#### **Issue Identified by TTC:**

In order to conduct the effective transfer of technologies to startup companies, it is often necessary for faculty and staff to directly participate in the process. Policies regulating outside employment and leave of absence policies are not well defined and vary among component institutions. Some components permit only paid leave in which employees are expected to use vacation time, and limit such leaves to short periods each year (for example, 30 days). In some circumstances, faculty may take “partial leave” by becoming part-time employees for the University and part-time for a company. In this circumstance it is not clear whether the Intellectual Property Policy applies.

#### **TTC Recommendation:**

**C.2. Modify and clarify outside employment and leave of absence policies to better enable faculty and staff to facilitate transfer of university technologies to commercial entities.**

It is recommended:

- That faculty and staff be allowed to take unpaid leaves of absence without penalty to accrued vacation time, if any, and tenure considerations, provided that (1) the leave is approved on an annual basis by appropriate officers and departmental administrators within components, and (2) the commercial entity provides all compensation and benefits to the employee during the leave period. In such instances, intellectual property developed by the employee during the leave period would be the property of the company.
- That paid leaves (leaves that utilize vacation time) be permitted to the full extent of accrued vacation time, under which intellectual property developed by the employee during such paid leave would belong to the Board of Regents, and that unpaid leave be made available thereafter under the circumstances described above; and
- That part-time unpaid leaves of absence be available on the same terms as full-time unpaid leave of absence (with the commercial entity providing proportionate compensation and benefits to the employee), except that the intellectual property developed by the employee during the leave period would belong to the Board of Regents.

#### **Action Recommended by TTC:**

Amend Regents' Rules and Regulations, Part Two, Ch. XII, §§ 2.1 and 4.1, as provided in Appendix G.

Amend Regents' Rules and Regulations, Part One, Ch. III, § 16 (amendments not yet drafted and contingent on amendments to statute).

Amend Texas Education Code § 661.909 to except leave for technology transfer activities from (a) requirement that all paid leave be used before unpaid leave may be taken, and (b) limitation of duration of leave to 12 months.

## Final Staff Recommendations

### Worksheet C.2.

(Page 2 of 2)

**Law, Rule, or Policy Affected:**

Regents' Rules and Regulations, Part Two, Ch. XII, §§ 2.1 and 4.1

Regents' Rules and Regulations, Part One, Ch. III, § 16

Texas Education Code § 661.909

**Pro:**

1. Revisions to leave policy in Regents' Rules and Regulations may result in greater consistency in practices among the various institutions.
2. More flexible leave policy may encourage more technology development.

**Con:**

1. Absence of faculty may place burden on other faculty, place financial burden on institution that must recruit and hire temporary, replacement faculty, or create gap in institution's curriculum.

**Cost:**

Not yet determined.

**Issues Raised:**

1. How does unpaid leave affect tenure, benefits?
2. Should there be limits on the duration and number of leaves in a given period?

**Staff Recommendation:**

1. Refer revisions to the Texas Education Code to the Office of Governmental Relations for inclusion in deregulation efforts. Florence Mayne should coordinate with OGR. Amendments to Regents' Rules and Regulations, Part One, Ch. III, § 16 would be proposed if legislation is passed.
2. Adopt the TTC recommendation that Board of Regents revise Regents' Rules and Regulations, Part Two, Ch. XII, §§ 2.1 and 4.1, as provided in Appendix G.
3. The Technology Management Council should hold a meeting to discuss leave policies in an effort to develop a better understanding of how leave is handled at each of the component institutions and to determine if there are inconsistencies between Board policy and a component institution's implementation of the policy. The Technology Management Council should involve representatives from Human Resources, the Office of General Counsel and other individuals who may be of help in advising the council on applicable law and the current policies of the Board of Regents pertaining to leave.

# Final Staff Recommendations

## Worksheet C.3.

(Page 1 of 2)

### **Issue Identified by TTC:**

TTOs, operating within components, are hampered in their effectiveness in forming startup companies because of their inability to directly engage service providers and CEOs and because of their inability to assume debt for the purpose of launching a for-profit startup company.

### **TTC Recommendation:**

**C.3. Encourage and facilitate the creation of privatized corporations for the purpose of managing technology commercialization at components with advanced technology transfer programs. It is expected that the sponsoring institution would negotiate a contract with its respective 501(c)(3) for the purpose of managing technology development activities and that compensation from these activities would continue to be directly received by the sponsoring institution.**

### **Action Recommended by TTC:**

Amend Regental Policies and Guidelines as indicated in Appendix F.  
Draft guidelines or policy for establishment, governance, and operation of such corporations.

### **Law, Rule, or Policy Affected:**

Regents' Rules and Regulations, Part One, Ch. VII, § 5 (regarding internal corporations) (no amendment yet identified).  
Regental Policies and Guidelines (Appendix F), "Management and Marketing of Intellectual Property"  
Texas Education Code § 153.004 (permitting the establishment of corporations and LLCs for the development and commercialization of technology) (no amendment identified).

### **Pro:**

1. Permits the effective launch of companies in a timely, business-like manner.

### **Con:**

1. Adequate oversight of corporation's activities may be difficult.

### **Cost:**

Not yet determined.

## Final Staff Recommendations

### **Worksheet C.3.**

(Page 2 of 2)

#### **Issues Raised:**

1. What is the mechanism for a 501(c)(3) corporation transferring money to institutions that will be consistent with Internal Revenue Code?
2. What are the guidelines under which such corporations will be established, governed, and operated so that appropriate oversight by the Board is maintained?
3. Will such corporations be subject to the Open Meetings Act, the Public Information Act, or other laws applicable to state agencies?
4. Would intellectual property be transferred to the corporation and, if so, what would be the consideration for transferring the Board's interest in intellectual property to the corporation?
5. Should the entity be a non-profit or a for-profit corporation or a limited liability company (tax issues and other choice of entity issues)?

#### **Staff Recommendation:**

1. TTOs should consider the TTC recommendation and, if a TTO considers the establishment of a private corporation in the best interest of that institution's technology development efforts, the TTO should work with the institution's president and business officer and the Office of General Counsel to develop a proposal to submit to the Board of Regents for approval. Among the matters that should be evaluated by the TTO are the five issues raised above.

Final Staff Recommendations  
**Worksheet D.**

***Issue Identified by TTC:***

With the additional rights recommended in this proposal comes the additional responsibility of making certain that commercialization activities are conducted in a manner that will not materially, or by perception, damage U. T. System. To assure this, it is necessary to realign our policies so that they are congruent with the practices of technology development activities.

***TTC Recommendation:***

**D. ASSURE PROPRIETY IN TECHNOLOGY TRANSFER ACTIVITIES**

1. Modernize and clarify rules, regulations, guidelines and procedures under which technology development is to occur.
2. Establish a committee to assure compliance in operations and to provide jurisdiction in complicated issues.
3. Establish component TTOs, rather than faculty, as the final authority in commercialization decisions.

Final Staff Recommendations  
**Worksheet D.1.**

**Issue Identified by TTC:**

Current rules, regulations, policies and procedures were drafted in the infancy of technology development and have subsequently been amended on several occasions. As a result, the intent of these regulations is often not clear. Specifically, distinctions need to be drawn between absolute requirements and suggested terms.

**TTC Recommendation:**

**D.1. Modernize and clarify rules, regulations, guidelines and procedures under which technology development is to occur.**

**Action Recommended by TTC:**

Amend Regents' Rules and Regulations, Part Two, Ch. XII as specified in Appendix G.  
Amend Regental Policies and Guidelines as specified in Appendix F.

**Law, Rule, or Policy Affected:**

Regents' Rules and Regulations, Part Two, Ch. XII as specified in Appendix G.  
Regental Policies and Guidelines as specified in Appendix F.

**Pro:**

Specific issues are discussed in connection with specific recommendations in the report.

**Con:**

Specific issues are discussed in connection with specific recommendations in the report.

**Cost:**

Specific issues are discussed in connection with specific recommendations in the report.

**Issues Raised:**

Specific issues are discussed in connection with specific recommendations in the report.

**Staff Recommendation:**

1. Adopt TTC recommendations to amend Regents' Rules and Regulations, Part Two, Ch. XII as specified in Appendix G and amend Regental Policies and Guidelines as specified in Appendix F.

Final Staff Recommendations  
**Worksheet D.2.**

**Issue Identified by TTC:**

Management of conflicts of interest within individual components has become increasingly problematic. Certain instances have arisen which require management of conflicts of interest by non-component staff and administration. As a result, there is a need for surveillance in compliance with conflict of interest management plans that is more properly conducted by a committee at U. T. System.

**TTC Recommendation:**

**D.2. Establish a committee to assure compliance in operations and to provide jurisdiction in complicated issues.**

**Action Recommended by TTC:**

During the past several months, an ad hoc committee was created by the Office of General Counsel to review conflict of interest issues related to technology transfer. The preliminary conclusions of this group are provided in Appendix I. The TTC recommends that the ad hoc group identified by the Office of General Counsel to study this issue and make recommendations for strengthening the management of conflicts of interest continue its work over the next several months in coordination with the TTC.

**Law, Rule, or Policy Affected:**

Not yet identified.

**Pro:**

Not yet identified.

**Con:**

Not yet identified.

**Cost:**

Not yet identified.

**Issues Raised:**

Not yet identified.

**Staff Recommendation:**

1. Because the ad hoc committee has not completed its work, it is premature to adopt the TTC's recommendation to establish a conflict of interest committee. The Technology Management Council should work with the ad hoc committee to develop specific recommendations for the Board of Regents with respect to the management of conflicts of interest.

Final Staff Recommendations  
**Worksheet D.3.**

**Issue Identified by TTC:**

Currently, the policies governing commercialization of intellectual property indicate that TTOs should, when possible abide by the wishes of the inventor in the licensing process. Faculty remains an important source for identification of potential licensees. However, conflicts of interest issues increasingly create situations where the faculty inventor must be distanced from the licensing/commercialization process. Moreover, faculty involvement in the negotiations of terms for agreements often is an impediment to timely execution of a contract with the best terms for U. T. components and faculty.

**TTC Recommendation:**

**D.3. Establish component TTOs, rather than faculty, as the final authority in commercialization decisions.**

**Action Recommended by TTC:**

Amend Regents' Rules and Regulations, Part Two, Ch. XII, § 2.5 as indicated in Appendix G.

**Law, Rule, or Policy Affected:**

Regents' Rules and Regulations, Part Two, Ch. XII, § 2.5

**Pro:**

1. More business-like approach.
2. Reduces potential for conflicts of interest.
3. Allows decisions to be made that are consistent with institution's mission.

**Con:**

1. Faculty resistance.
2. A disincentive to faculty to get involved in marketing technology, although faculty may have best idea and connections for marketing because of familiarity with technology.

**Cost:**

None identified.

**Issues Raised:**

**Staff Recommendation:**

1. Adopt the TTC recommendation and amend Regents' Rules and Regulations, Part Two, Ch. XII, § 2.5 as indicated in Appendix G, except that the reference to the "component institution" should instead refer to the "chief administrative officer."



Final Staff Recommendations  
**Worksheet E.**

**Issue Identified by TTC:**

Through this report, the TTC has completed its mission as originally chartered. However, the TTC believes that there is an immediate need to coordinate the implementation of the recommendations under development by the Ad Hoc Committee on Conflict of Interest with those herein proposed by the TTC. More generally, it may be important to create a standing advisory committee that is charged with the responsibility of reviewing technology operations conducted by the TTOs of U. T. System and its component institutions on an ongoing basis. Such a commission has been created within the University of California and has served to oversee the decentralization of technology management, develop policies to adapt to the changing landscape of technology transfer, and provide recommendations to the central TTO of the UC system.

**TTC Recommendation:**

**E. CONVERT THE TTC TO A STANDING ADVISORY COMMITTEE.**

It is recommended that the TTC continue to stand as an advisory committee for an additional two-year period. It may be appropriate to modify the existing composition of the TTC to include representatives from additional component institutions of U. T. System.

**Action Recommended by TTC:**

Board and Chancellor must approve establishment of committee.

**Law, Rule, or Policy Affected:**

**Pro:**

**Con:**

**Cost:**

**Issues Raised:**

**Staff Recommendation:**

1. To avoid duplication of effort and creation of additional bureaucracy, staff recommends that, in lieu of creating a new committee, as recommended by the TTC, the existing Technology Management Council serve as an advisory group with respect to policies and other matters pertaining to technology development. The council should, as it deems appropriate, invite other participants to its meetings to obtain input and gain a broader perspective.

**Employee Group Insurance Report**  
**on**  
**Status of Plan Changes and Rate Increases for 2003**

The cost of providing healthcare continues to increase at an alarming rate. Nationally, annual trends of 11%-23% are being observed as employers search for ways to provide affordable health insurance. These trends can be attributed to the following:

- State and Federal Legislative Action
- Demand for Higher Reimbursement Levels from Providers
- New, More Costly Prescription Medications and Medical Treatments
- Patient Demand for Greater Access to Providers

The University of Texas System (U.T. System), is no exception to these trends as it attempts to balance Employee Group Insurance revenue with expenses.

U.T. System employees and retirees have indicated a strong desire for insurance vendor stability; therefore, the office of Employee Group Insurance (EGI) began discussion of contract renewals with Humana Inc. and HMOBlue Texas for fiscal year 2003. Humana currently provides Health Maintenance Organization (HMO) coverage for most of the southern region of the state while HMOBlue Texas provides HMO coverage for the northern region of the state. Blue Cross and Blue Shield of Texas provides third party administration for the self-funded UT Select plan and will be in the second year of a three-year contract in FY 2003. Texas Universities Health Plan (TUHP) currently provides HMO coverage for 300 members in the San Antonio area and will not be offered next year.

The 77<sup>th</sup> Texas Legislature appropriated 12.4% additional funding for premium sharing for FY 2003. By modifying the HMO plan design, which includes out-of-pocket increases at the time services are rendered, EGI was able to negotiate 12%-17% rate increases for FY 2003. The final rates for the self-funded UT Select plan have not been finalized pending February 2002 utilization data; however, similar plan design modifications are being considered for the plan. The final rates for all plans will be included for your approval in an agenda item to be presented at the May Board of Regents' meeting.

In addition to negotiating competitive rate increases, EGI will also introduce new health management programs to UT Select and HMO members in 2003, in addition to health management programs currently being offered to enrolled participants of HMOBlue. The health management programs will help members learn specific details concerning their medical condition(s) and how to maintain a healthy lifestyle with their condition(s), and will also assist members in utilizing and accessing their health benefits appropriately.

The System Wide Insurance Advisory Committee requested EGI review with CIGNA Life Insurance, the current life insurance carrier, the possibility of increasing the amount of spouse life insurance from the current maximum of \$10,000. After discussing options for spousal coverage with CIGNA, an agreement was reached to continue to offer the \$10,000 option plus allow spouse coverage to be increased to a total of \$25,000 or \$50,000 beginning September 1, 2002.

EGI currently offers a dental HMO to plan participants and for FY 2003, will introduce enhancements to the plan design. The current dental HMO carrier, Fortis Dental (formerly Protective/United Dental), has agreed to offer U. T. employees and retirees the following enhancements:

- Larger Selection of Providers
- No Referrals Necessary for Specialty Care
- Out-of-Network Coverage
- More Covered Services
- Quicker Access to Appointments
- Same Monthly Premium Rate for Employee Only Coverage and Lower Monthly Premium Rate for Dependent Coverage

While it is difficult to effectively reach all enrolled members, EGI is developing a comprehensive strategy that is designed to create awareness of healthcare trends and explain the reasons for rate changes, plan design changes, and other enhancements.

**The University of Texas System Administration Audit Office**  
**Quality Assurance Review**  
**January 2002**

A Quality Assurance Review was conducted of The University of Texas System Audit Office in accordance with professional standards and current practices within the internal audit profession. The review team consisted of Patrick Reed, University Auditor for the University of California System; Frank Bossle, Executive Director of Internal Audit for the Johns Hopkins University and Health System; David Coury, Inspector General for Florida State University; and Andrea Marks, Director of Internal Audit at The University of Texas Health Science Center at San Antonio.

It was concluded that the System Audit Office **is in compliance** with the Institute of Internal Auditors' professional standards, meeting all of the *Attribute* and *Performance* standards. Audit personnel are experienced, competent, and well supervised. Its customers are well satisfied with the services received, and the range of services provided is well aligned with management's objectives and appropriate to the profession's revised definition.

The review team observed certain opportunities for consideration which may further improve the audit program at both the System Administration level and System-wide. The observations are as follows:

- Continue to promote collaboration among internal audit directors and opportunities for sharing knowledge and exemplary practices, tools and techniques wherever they may exist within the System.
- Promote consistent application of risk assessment and planning guidance.
- Continue to strengthen the information technology audit program and reinforce the need for components to do the same.
- Consider development of application guidance for new professional standards in concert with the Internal Audit Directors' Council.

In a separate letter, the following observations were made:

- It was also noted that communication between the System Audit function and the Board of Regents should be increased and possibly would be better managed through the establishment of a subcommittee within the Finance and Planning Committee of the Board of Regents.
- The team observed that the authority and responsibility of the System audit director should be more clearly defined as it relates to the component audit functions.
- The system-wide internal audit function can benefit greatly through sharing and collaboration without compromising the independence of the components; however, for this to occur, there must be a culture facilitating a willingness to focus on similarities, a belief in the value of coming together, and building mutual respect.
- Consider utilizing performance measures to demonstrate the quality of audit performance across the System.

***Overall Response: We concur. We will develop an action plan to implement the suggestions provided in this peer review and present it to our Internal Audit Committee.***

The University of Texas Board of Regents  
Finance and Planning Committee  
**Internal Audit and Compliance Subcommittee**

Duties

The Internal Audit and Compliance Subcommittee is the designated oversight agent of the Board of Regents for internal assurance activities in The University of Texas System. Its primary responsibility is to monitor the quality and level of assurance provided from both internal and external sources on the risk management and control processes of the U.T. System. Specific duties include:

- Responsible for overseeing all internal and external auditing and compliance functions within the U. T. System.
- Approves the hiring of the System Director of Audits after nomination by the Chancellor.
- Approves the annual system-wide risk assessment and annual internal auditing plan.
- Initiates system administration and institutional audits and compliance activities as deemed necessary to ensure appropriate risk management and control processes within The University of Texas System.
- Provides the Finance and Planning Committee and the Board of Regents with relevant information obtained from on-going reviews of auditing and compliance activities and reports of internal auditors, external auditors, and the State Auditor's Office.
- Meets with external auditors, internal audit directors, and compliance officers as deemed necessary to discuss specific risk management and control issues.

Membership

The Internal Audit and Compliance Subcommittee is composed of a chairman and two (2) members appointed by the Chairman of the Finance and Planning Committee from the membership of that committee. Subcommittee members serve at the pleasure of the Chairman of the Finance and Planning Committee.

Meetings

The Internal Audit and Compliance Subcommittee will meet at least quarterly and report through the Finance and Planning Committee. Each meeting will provide for an Executive Session as authorized by Texas law.

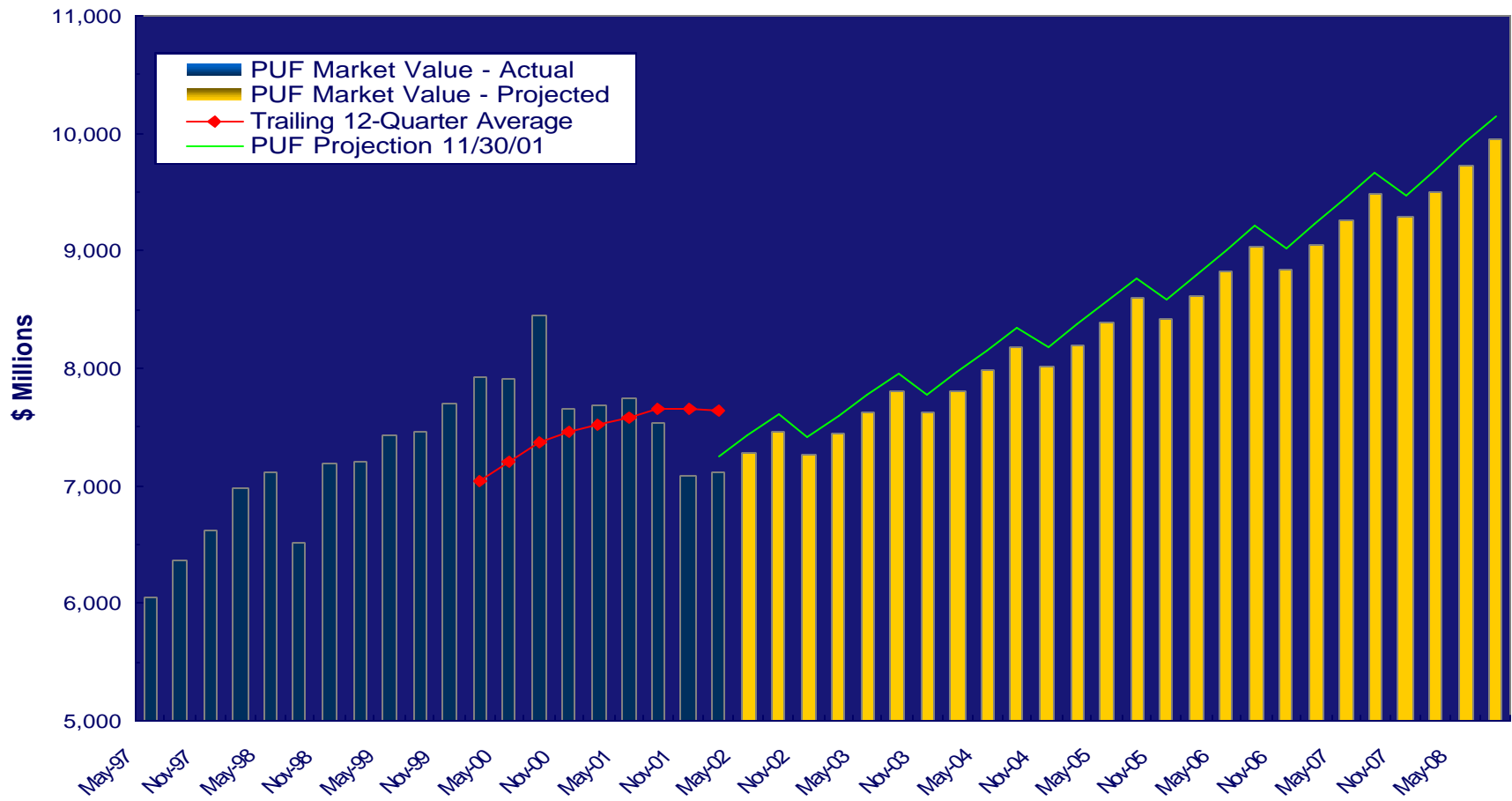
Support

The System Director of Audits and the System-wide Compliance Officer is/(are) the primary contact(s) between the Internal Audit and Compliance Subcommittee and both the internal and external assurance organizations. The System Audit Office provides support services for the Internal Audit and Compliance Subcommittee.

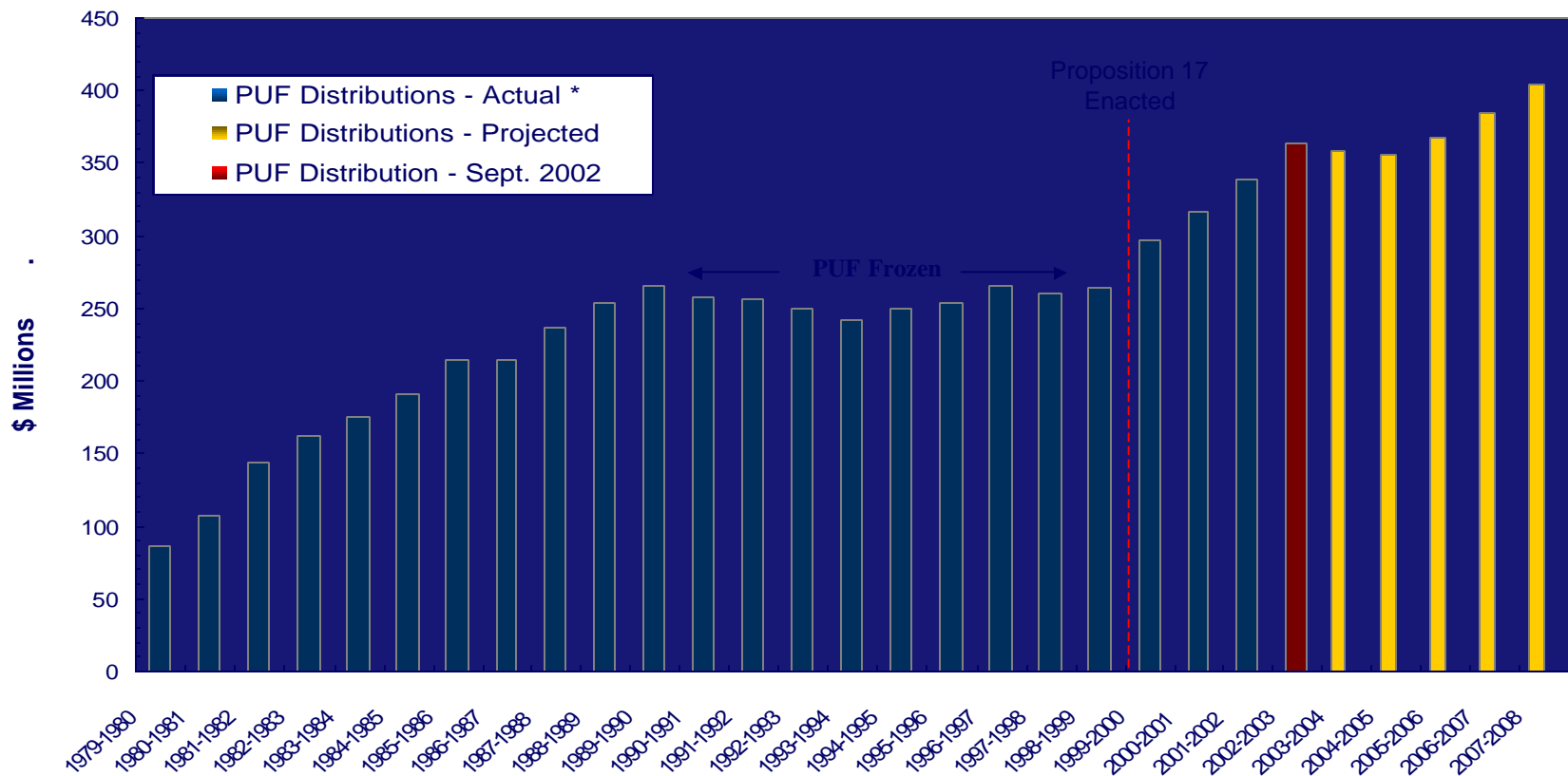
# Quarterly Permanent University Fund Update-Executive Summary

- As of February 28, 2002, the market value of the PUF was \$7.114 billion. As a result, the FY 2003 distribution to the AUF will be \$363.0 million, an increase of \$24.6 million over the \$338.4 million distributed during FY 2002.
- The current PUF debt capacity is projected as \$102.7 million, down slightly from the \$116.5 projected in January 2002. This decline is the result of lower than forecasted returns on the PUF, partially offset by better than expected debt service savings as a result of the PUF Series 2002A and Series 2002B refunding transactions.
- The current analysis incorporates the revised PUF debt service as a result of the Series 2002A and Series 2002B refundings. The analysis also incorporates a potential \$30 million cash defeasance of outstanding PUF debt during FY 2002. Similar cash defeasances of outstanding debt were accomplished in FY 1998, FY 1999, and FY 2000, thereby reducing future debt service payable from the PUF.

# Permanent University Fund – Market Value Through February 28, 2002



# Permanent University Fund Distributions



\* Effective September 1, 1997, a statutory amendment changed the distribution of income from cash to an accrual basis, resulting in a one-time distribution adjustment to the AUF of \$47.3 million, which is not reflected.



# Permanent University Fund - Debt Capacity

## *Base Case Assumptions*

- PUF Distribution equals 4.75% of the PUF net asset value for the trailing 12 quarters, beginning FY 2003.
- U.T. Austin Excellence Funds equal 45% of the income available to U.T. System.
- AUF balance never falls below \$45 million. Includes all PUF projects approved through February 2002.
- Forecasted PUF distribution amounts provided by UTIMCO based on long-term expected average annual rate of return of 9.35%, starting from the PUF market value as of February 28, 2002.
- Annual LERR appropriations of \$30 Million are projected to continue from FY 2003 through FY 2008.
- Includes PUF Refunding Bonds, Series 2002A and PUF Bonds, Series 2002B. Remaining new PUF debt service structured as 20-year, tax-exempt debt with level debt service. The analysis includes a proposed \$30 million cash defeasance of outstanding PUF debt during FY 2002.
- Projected debt service costs based on current forward interest rates (approximately 5.48%). This analysis assumes the PUF arbitrage exemption is restored.

# Permanent University Fund - Debt Capacity

## Base Case

Additional PUF Debt Capacity (\$102.7 Million)		\$0.0	\$102.7	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Cumulative Additional PUF Debt Capacity		\$0.0	\$102.7	\$102.7	\$102.7	\$102.7	\$102.7	\$102.7
<b>Available University Fund Operating Statement Forecast Data (\$ Millions)</b>	<b>Actual</b>	<b>Estimated</b>	<b>Projected</b>					
	<b>FY 01</b>	<b>FY 02</b>	<b>FY 03</b>	<b>FY 04</b>	<b>FY 05</b>	<b>FY 06</b>	<b>FY 07</b>	<b>FY 08</b>
PUF Distribution Amount	\$317.08	\$338.43	\$363.02	\$358.81	\$355.47	\$366.97	\$385.05	\$404.39
Surface & Other Income	9.3	6.9	7.1	7.4	7.5	7.6	7.8	8.0
Divisible Income	326.3	345.3	370.1	366.2	362.9	374.6	392.9	412.4
UT System Share (2/3)	217.6	230.2	246.8	244.1	241.9	249.7	261.9	274.9
AUF Interest Income	12.4	7.9	9.3	12.5	14.1	14.7	15.4	16.1
Income Available to U.T.	229.9	238.1	256.1	256.6	256.0	264.5	277.3	291.0
TRANSFERS:								
UT Austin Excellence Funds (45%)	(102.5)	(107.2)	(115.2)	(115.5)	(115.2)	(119.0)	(124.8)	(131.0)
PUF Debt Service on Approved Projects	(60.7)	(76.5)	(88.7)	(105.4)	(109.0)	(111.9)	(114.7)	(117.4)
PUF Cash Defeasance of Outstanding Debt	-	(30.0)	-	-	-	-	-	-
PUF Debt Service on Add. Debt Capacity	-	-	(5.4)	(8.6)	(8.6)	(8.6)	(8.6)	(8.6)
System Adm	(28.1)	(26.2)	(28.5)	(29.8)	(31.2)	(32.6)	(34.2)	(35.8)
Other	(2.1)	(2.5)	(4.5)	(1.1)	(1.1)	(1.1)	(1.1)	(1.1)
Debt Service (Bldg Rev)	(3.4)	(3.4)	(3.4)	(3.4)	-	-	-	-
Net Surplus/(Deficit)	33.1	(7.7)	10.3	(7.1)	(9.0)	(8.7)	(6.0)	(2.8)
Ending AUF Balance - System	76.2	68.5	78.8	71.6	62.6	53.8	47.8	45.0
PUF Debt Service Coverage	3.79:1	3.11:1	2.73:1	2.26:1	2.18:1	2.20:1	2.26:1	2.32:1

# Permanent University Fund - Debt Capacity Sensitivities

Board-Determined	Board-Determined	Board-Determined	Market-Dependent	Market-Dependent	Additional Debt Capacity (\$ Millions)						TOTAL	Projected PUF
Annual LERR	U.T. Austin Excellence	PUF Distribution Rate	PUF Investment Return	Change in Tax-Exempt Rates	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY 2003- FY 2008	Market Value in FY 2030
\$30 Million	45.0%	4.75%	9.35%	NA	102.7	0.0	0.0	0.0	0.0	0.0	102.7	26,613,443,719
<b>\$30 Million</b>	45.0%	4.75%	9.35%	NA	102.7	0.0	0.0	0.0	0.0	0.0	102.7	26,613,443,719
<b>\$20 Million</b>	45.0%	4.75%	9.35%	NA	112.7	10.0	10.0	10.0	10.0	10.0	162.7	26,613,443,719
<b>\$10 Million</b>	45.0%	4.75%	9.35%	NA	122.7	20.0	20.0	20.0	20.0	20.0	222.7	26,613,443,719
<b>None</b>	45.0%	4.75%	9.35%	NA	132.7	30.0	30.0	30.0	30.0	30.0	282.7	26,613,443,719
\$30 Million	<b>40.0%</b>	4.75%	9.35%	NA	272.8	0.0	0.0	0.0	0.0	0.0	272.8	26,613,443,719
\$30 Million	<b>45.0%</b>	4.75%	9.35%	NA	102.7	0.0	0.0	0.0	0.0	0.0	102.7	26,613,443,719
\$30 Million	<b>50.0%</b>	4.75%	9.35%	NA				"Negative" Debt Capacity				26,613,443,719
\$30 Million	45.0%	<b>4.50%</b>	9.35%	NA	27.8	0.0	0.0	0.0	0.0	0.0	27.8	28,414,840,407
\$30 Million	45.0%	<b>4.75%</b>	9.35%	NA	102.7	0.0	0.0	0.0	0.0	0.0	102.7	26,613,443,719
\$30 Million	45.0%	<b>5.00%</b>	9.35%	NA	177.3	0.0	0.0	0.0	0.0	0.0	177.3	24,912,480,922
\$30 Million	45.0%	4.75%	<b>8.35%</b>	NA	77.5	0.0	0.0	0.0	0.0	0.0	77.5	20,241,883,999
\$30 Million	45.0%	4.75%	<b>9.35%</b>	NA	102.7	0.0	0.0	0.0	0.0	0.0	102.7	26,613,443,719
\$30 Million	45.0%	4.75%	<b>10.35%</b>	NA	128.5	0.0	0.0	0.0	0.0	0.0	128.5	34,942,568,797
\$30 Million	45.0%	4.75%	9.35%	<b>+ 50 bps</b>	72.8	0.0	0.0	0.0	0.0	0.0	72.8	26,613,443,719
\$30 Million	45.0%	4.75%	9.35%	<b>NA</b>	102.7	0.0	0.0	0.0	0.0	0.0	102.7	26,613,443,719
\$30 Million	45.0%	4.75%	9.35%	<b>-50 bps</b>	135.3	0.0	0.0	0.0	0.0	0.0	135.3	26,613,443,719

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March 13, 2002

MEMORANDUM

TO: Finance and Planning Committee of the U. T. System Board of Regents

FROM: Philip R. Aldridge  
Terry A. Hull

SUBJECT: Revenue Financing System Presentation

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Executive Summary

On April 2, the Office of Finance will be making a presentation to the Finance and Planning Committee of the Board, entitled, "Revenue Debt Strategy." It is a follow-up to the "Revenue Debt Capacity Presentation," which was made at the February Board meeting. You will recall that the February presentation concluded that, based on current trends and financial projections, the U. T. System is steadily using up its revenue debt capacity at the 'AAA' credit level.

The Office of Finance has been studying alternatives to improve the Revenue Financing System (RFS) debt profile. Those efforts have resulted in three recommendations from the Office of Finance:

- Increase the minimum debt service coverage for all components from the current 1.25 times, to 1.30 times effective 9/1/02, and to 1.35 times effective 9/1/03.
- Target 30% -50% floating rate debt as a percentage of the System's total revenue debt (as compared to approximately 20% historically).
- Extend the weighted average life of the debt portfolio by issuing longer-term debt.

The anticipated benefits of these proposals include improved asset/liability matching, a reduction in expected annual debt service, and an enhanced credit profile for the System's debt.

Attachment

cc: Mr. Kerry L. Kennedy

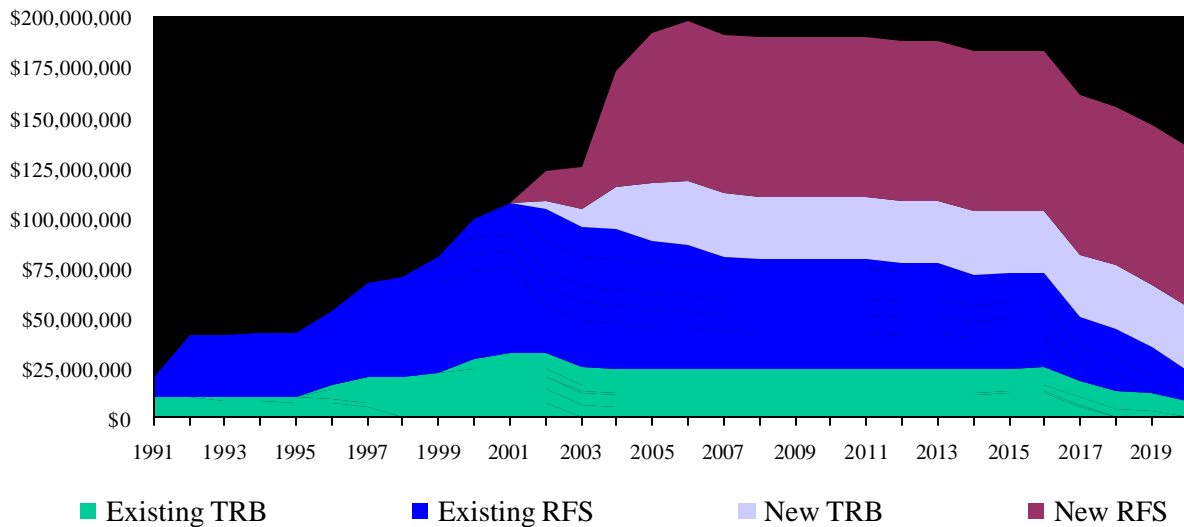
## Appendix: U. T. System Revenue Debt Strategy

### I. Growing Debt Load and Tighter Credit Standards

Access to Revenue Financing System (RFS) debt has traditionally not been restricted as long as a component institution has the ability to repay the debt (the Finding of Fact). The relatively low approval threshold has worked well over the years due to the historically conservative use of RFS debt by some of the larger, financially strong components. Over the past several years, large capital needs and low interest rates have made RFS debt a more attractive financing option for all of the components. The attractiveness of RFS debt is expected to continue, as evidenced by the fact that the Office of Finance is projecting to issue \$750 million of new RFS debt over the next 24 months.

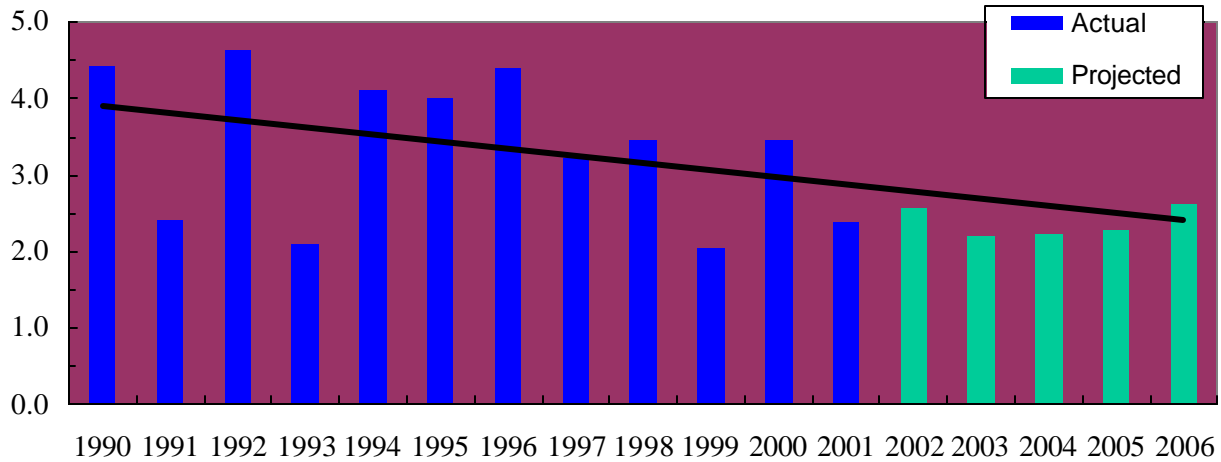
The chart below shows the anticipated growth in RFS debt service based on projects that are already in the CIP. Annual RFS debt service is projected to increase from almost \$100 million in FY 2000 to approximately \$200 million in FY 2006. Beyond 2006, the components have identified an additional \$3.9 billion of capital projects on the “futures list” which, if approved, would require even greater levels of debt issuance.

Figure 1: Revenue Financing Debt Service by Type



The primary financial ratio used to determine the components' ability to repay the debt, excluding tuition revenue bonds, for which debt service is reimbursed by the State, is the components' debt service coverage ratio (DSC). A 1.25 times DSC indicates that the component is expected to maintain an annual operating margin at least 25% greater than the projected annual debt service. It is a relatively low threshold that is intended to be a minimum standard, and not an investment grade-equivalent standard. The next chart shows the impact on the System's DSC from the greater use of RFS debt in recent years.

**Figure 2: U. T. System Declining Debt Service Coverage**

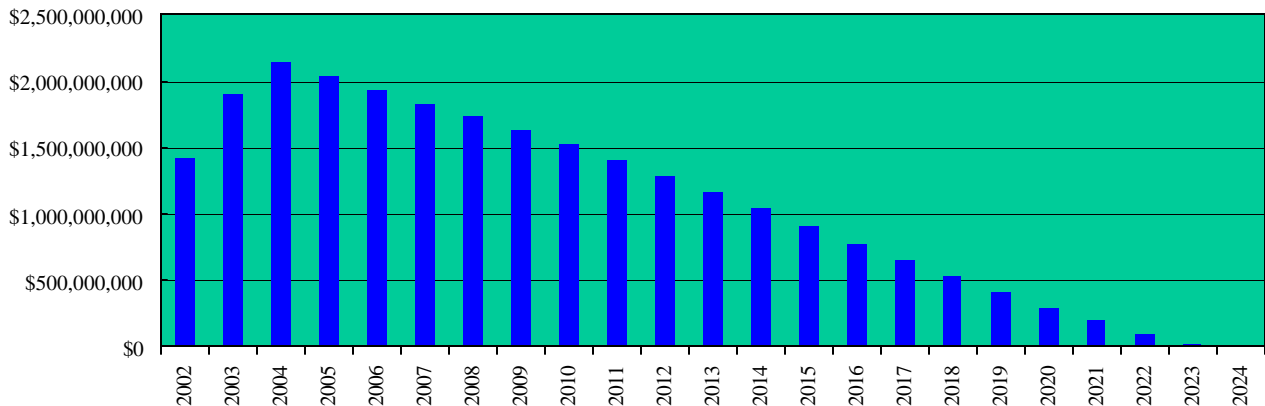


The Office of Finance is proposing to increase the minimum debt service coverage for all components from the current 1.25 times, to 1.30 times effective 9/1/02, and to 1.35 times effective 9/1/03. While this step alone will not significantly reduce the amount of RFS debt approved and issued at the System, it does “raise the bar” to a low investment grade level and send a signal to the components that RFS debt is not an unlimited resource.

**II. Existing Debt Structure**

The table that follows shows the System’s current RFS debt profile, which includes debt that is approved but not yet issued. You’ll note that all RFS debt is completely repaid in a relatively short 21 years.

**Figure 3: Projected RFS Debt Outstanding**



Traditionally, the System has used short term, variable rate debt for interim construction needs and for the purchase of equipment. Short term debt is issued in the form of commercial paper, which allows for significant flexibility in choosing the appropriate term (overnight to as long as 270 days) and financing amounts (the minimum issuance amount is \$100,000). Long term debt has traditionally been issued with a 20-year term, a fixed rate, and level debt service (just like a 20 year, fixed rate mortgage). This form of long term financing is very conservative, in that very long-term assets with an average life of 40 to 50 years are fully paid for in 20 years. The weighted average life of the current RFS fixed-rate debt portfolio is 9.7 years, a very short average life given the long-term nature of the assets financed. For example, Stanford has a 21.4 year weighted average life; Michigan, 13.4 years; Harvard, 23.7 years, and Chicago, 23.7 years.

## A. The Case for Issuing Longer Term Debt

Over the past ten years there has been a trend among major higher education institutions away from the traditional 20-year and 30-year amortizing debt with serial and term bonds, in favor of variable rate debt, longer maturities, and both amortizing and non-amortizing bonds with bullet maturities. There are a number of factors that have contributed to this trend.

The fact that universities are now issuing debt with longer terms, 40 or more years (Boston University issued 60-year tax-exempt debt), reflects in part the long life of most university assets. In addition, the availability of tax-exempt financing makes it appealing to borrow as much as possible, for as long as possible, given the opportunity cost of using internally generated funds or endowment corpus to finance capital assets. The following table shows the longest-dated maturities for AAA institutions of higher education.

Figure 4: AAA Length of Longest Maturity

Institution	Issue	Longest Maturity Due	Notes
Michigan		2028	
UVA	Series 1998A	2024	University Debt
Texas	Series 1999A&B	2020	University Debt
Harvard	Series R	2048	
Dartmouth	Series 1999	2039	University Debt
Rockefeller	Series 1998	2037	
Notre Dame	Series 1998	2033	
Yale	Series U	2033	Medium-Term Notes due 2096
MIT	Series J-1 & J-2	2032	Medium-Term Notes due 2096
Stanford	CEFA	2032	
Princeton	Series 2001H	2030	
Rice	Series 199A	2029	maturing 2023-2029
Caltech	Series 1998	2028	
Columbia	Series 2000A	2025	

Source: Morgan Stanley, as of FYE 2001; based on issued debt only

Similarly, the use of bullet maturities is appealing for institutions which want to take advantage of the arbitrage opportunity and pay interest only for as long as possible. The rating agencies are

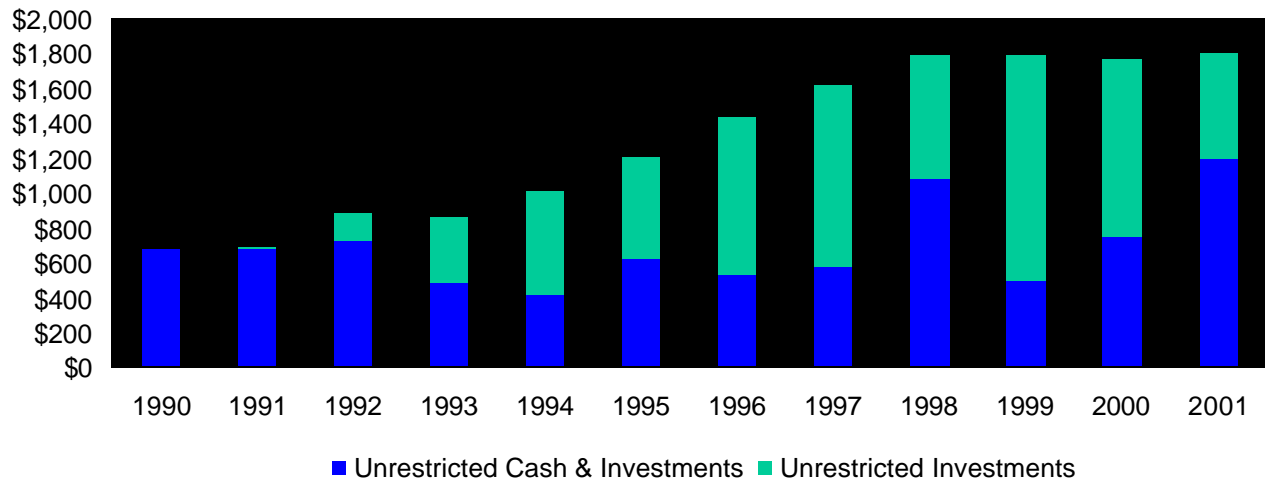
comfortable with bullet maturities for higher education institutions because they are confident that highly rated universities will have the funds to retire debt at maturity. Some universities, while not required to make any sinking fund payments, do amortize their debt internally as a means of imposing budgetary discipline. However, the university has the benefit of keeping all investment earnings until the bullet comes due.

## B. The Case for Permanent Variable Rate Debt

Many of the top schools have developed significant financial resources and have aggressively utilized permanent variable rate borrowing to build their balance sheets. The natural “hedge” resulting from short-term cash and securities has acted both as a form of self liquidity for these programs and as an interest rate hedge moving up and down to correlate with changes in interest rates. Both the desire to increase balance sheet assets and the desire to benefit from lower historic interest rates favors some reasonable amount of permanent variable rate debt.

First, with respect to the increase in variable rate debt, both issuers and the rating agencies have recognized that universities have a natural hedge against increases in short-term interest rates as a result of their sizeable cash and endowment balances. Rating agencies have concluded that if an appropriate level of variable rate exposure for any issuer is 25%–30%, a college or university as a result of this natural hedge can have as much 50%–75% or more of their total debt in a variable rate mode. The chart below shows that the System has a large amount of unrestricted investments, much of which is invested in floating rate assets such as money market funds and other short-term assets.

Figure 5: U. T. Short Term Investments (in millions)



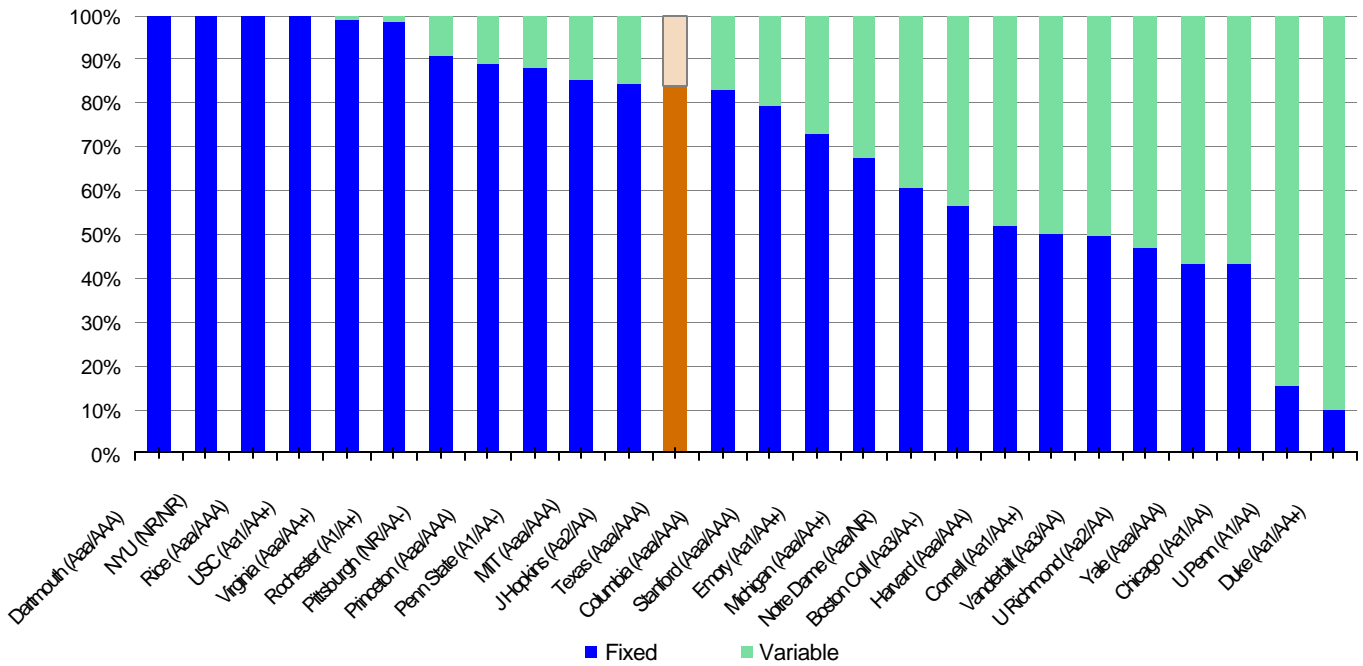
As of August 31, 2001, the System had unrestricted cash and investments of approximately \$1.8 billion. This level of short-term investments could theoretically hedge approximately \$2.7 billion of variable rate debt (\$1.8 billion divided by 66% relating to the Marginal Tax Rate).



We believe the System could comfortably have 50% or more of its total debt structure as variable without making any adjustments to its investment portfolio.

The following is a list of highly rated institutions and the percentage of debt that is fixed and variable.

**Figure 6: Fixed Rate vs. Variable Rate Debt**



Source: Morgan Stanley, as of FYE 2001

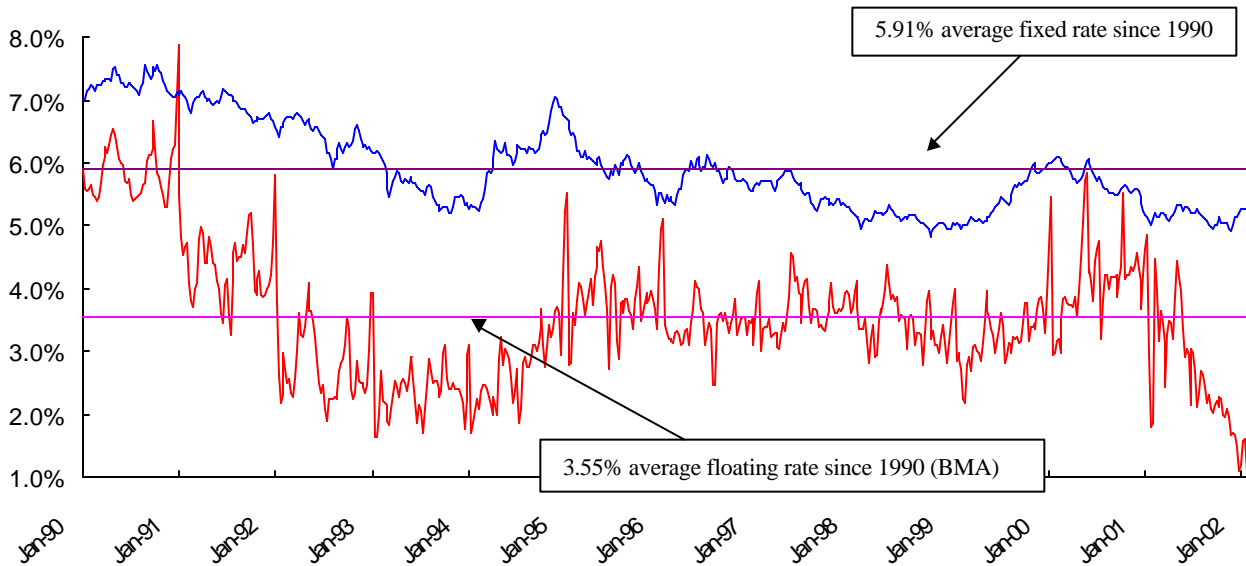
### C. Financing Alternatives

**Figure 7: Advantages and Disadvantages of Fixed Rate and Variable Rate Debt**

	<u>Advantages</u>	<u>Disadvantages</u>
<b>Fixed Rate Debt</b>	<ul style="list-style-type: none"> <li>• Future credit and tax risk shifted to investors</li> <li>• Usually callable in 10 years</li> <li>• Lock in low current rates</li> </ul>	<ul style="list-style-type: none"> <li>• Historically higher cost than variable rates</li> <li>• Less prepayment flexibility</li> </ul>
<b>Variable Rate Debt</b>	<ul style="list-style-type: none"> <li>• Lowest historical rates</li> <li>• Callable at any time</li> <li>• Range of variable rate structures</li> </ul>	<ul style="list-style-type: none"> <li>• Subject to future rate fluctuations</li> <li>• Future tax and credit risks remain with the University</li> </ul>

The Office of Finance issued fixed-rate debt in September of 2001. Fixed rate debt was issued in order to lock-in long-term rates that were at historical lows, and to preserve variable capacity for higher interest rate environments. The opportunity to issue variable rate debt going forward is significant. The following chart shows the relative cost advantage of variable rate debt versus fixed rate debt since 1990.

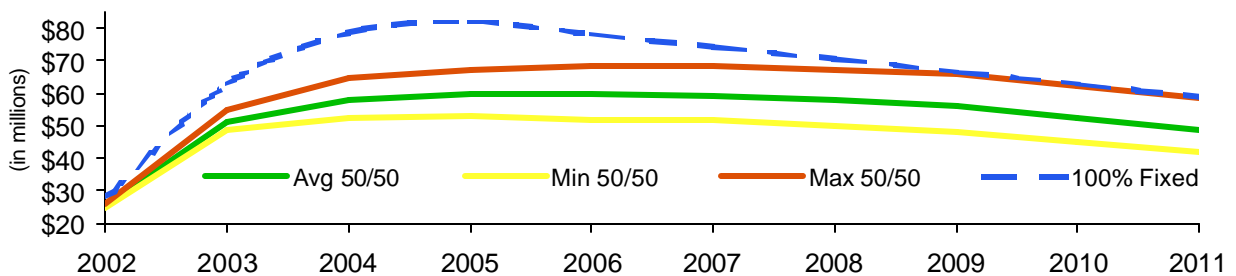
**Figure 8: Fixed vs. Floating Tax Exempt Rates**



If the System were to move towards a 50% / 50% fixed/variable mix of revenue debt, the potential annual interest savings could be \$20 million to \$30 million by FY 2004, depending upon the overall level of interest rates.

**Figure 9: Projected U.T. System Annual Interest Cost (100% Fixed vs. 50%/50% Fixed/Variable)**

Source: JP Morgan



## **D. Conclusions**

Based on current trends and financial projections, The U. T. System is steadily using up its revenue debt capacity at the 'AAA' credit level. Large capital needs and low interest rates have made RFS debt a more attractive financing option for many of the components, a trend which is expected to continue for the foreseeable future.

The U. T. System has traditionally issued long-term debt with a 20-year term, fixed interest rates, and level debt service. Short term, variable rate debt has been used solely for the purposes of providing interim construction funding and financing equipment purchases. The Office of Finance believes that the credit profile of the System can be improved by pursuing the following strategies:

- Increase the minimum debt service coverage for all components from the current 1.25 times, to 1.30 times effective 9/1/02, and to 1.35 times effective 9/1/03.
- Target 30% -50% floating rate debt as a percentage of the System's total revenue debt (as compared to approximately 20% historically).
- Extend the average life of the RFS debt portfolio by issuing longer-term debt (30-year, debt shift, bullets, etc.).

The anticipated benefits of these proposals include better asset/liability matching and a reduction in expected annual debt service.

**The University of Texas System  
TEXAS Grant Program**

During the 76<sup>th</sup> Legislative Session H.B. 713 created the Toward Excellence, Access and Success (TEXAS) Grant Program. Administration of this financial aid program was assigned to the Texas Higher Education Coordinating Board (THECB). Students attending both public and independent nonprofit institutions in Texas are eligible to participate in this program that emphasizes retention, rather than recruitment. Students must meet the following criteria to receive a TEXAS Grant award:

- Be a Texas resident;
- Show financial need;
- Graduate from a public or private high school in Texas no earlier than the 1998-99 academic year;
- Have completed the recommended or distinguished curriculum in high school;
- Enroll on at least a three-quarter time basis;
- Enroll in college within 16 months of high school graduation; and,
- Not be convicted of a felony or crime involving a controlled substance.

The TEXAS Grant Program awards to students attending public institutions must be for the student's full tuition and fees. The amount received from the THECB for FY 2002 is **\$1,344** per semester, which is the statewide average tuition and fees for full-time students. If an institution's actual tuition and fee charges exceed the statewide average, the difference between a student's actual tuition and fees and the statewide average must be made up by the institution either through a waiver or through financial assistance other than Pell and loans. Students continue to be eligible to receive awards:

- up to six years (SB 1057, 77<sup>th</sup> Texas Legislature, now provides for some hardship exemptions to the six year limit);
- up to completion of 150 semester credit hours; or,
- until a baccalaureate degree is received, whichever comes first.

Total awards at the universities are increasing from year to year as eligible students continue to receive awards along with the new awards given to incoming freshmen. The following table reflects the awards to U. T. institutions since the inception of the program.

<b>Institution</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>
U.T. Arlington	\$ 565,260	1,002,616	1,809,514
U.T. Austin	1,360,132	2,331,680	7,132,671
U.T. Brownsville	24,960	334,917	955,337
U.T. Dallas	101,760	271,366	979,537
U.T. El Paso	1,116,010	2,085,323	4,387,748
U.T. Pan American	2,094,845	3,057,951	6,538,693
U.T. Permian Basin	39,375	116,740	274,025
U.T. San Antonio	773,069	1,325,284	3,088,766
U.T. Tyler	27,440	116,603	260,237
UTHSC Houston	-	-	1,800
UTSMC Dallas	-	-	3,300
<b>Total</b>	<b>\$ 6,102,851</b>	<b>10,642,480</b>	<b>25,431,628</b>

In fiscal years 2000 and 2001, these institutions reflected these awards as State Grants and Contracts pass-through revenue, since the funds were passed through to the university from another state agency, THECB. When the funds were awarded to the student, the university reported tuition and fee revenue, with an offsetting expense to Scholarships and Fellowships. This accounting procedure basically reflected this revenue twice on the university's books – once for the Contract and Grant revenue and once for the Tuition and Fees revenue. In fiscal year 2002, universities implemented NACUBO's Advisory Report 2000-5, *Accounting and Reporting Scholarship Discounts and Allowances to Tuition and Other Fee Revenues by Public Higher Education*. The new accounting treatment for these grant award transactions is to **net** the Scholarship and Fellowship expense against the Tuition and Fees revenue, and only report the grant revenue once in the universities' financial records. Under either method, the final utilization of the revenue is to pay the operating expenses (i.e., faculty salaries, supplies, utilities, etc.) of the university needed to educate these grant recipients.

The creation of the TEXAS Grant Program has benefited Texas college bound students, with limited financial resources, tremendously. Also, SB 1057, passed in 2001, provides for a new publicity program to be developed by the THECB and by the Commissioner of Education to assure that students and their parents are aware of the benefits of the TEXAS Grant Program. The benefit to Texas universities varies from institution to institution, depending upon the circumstances of the particular school. For example, some U. T. schools like U. T. Pan American, U. T. Brownsville, U. T. San Antonio and U. T. El Paso have benefited by increasing enrollment at their institutions since more financial aid is now available for their students. These campuses are not at "fixed enrollment" and can accommodate this influx of new students. However, institutions like U. T. Austin, which has an enrollment management program to limit total enrollment, have not benefited as much. Students who meet the qualifications to obtain admission to U. T. Austin and also qualify to receive a TEXAS Grant benefit the most. U. T. Austin would have no difficulty filling an enrollment slot with another worthwhile student who did not qualify for a TEXAS Grant. Additionally, since the amount of the TEXAS Grant award is limited to the statewide average tuition and fees rate, institutions with costs that exceed the average, like U. T. Austin, must make up the difference (discussed above).

## **Out-of-State Students / Tuition Issues**

Nonresident students pay two forms of tuition: Base Tuition and, for graduate and pharmacy students, Differential Tuition. The purpose of Differential Tuition is to provide an institution with the ability to recover the costs of the more expensive graduate programs.

The Texas Higher Education Coordinating Board, using a formula prescribed by statute, computes the Base Tuition for nonresidents. Increases to the Base Tuition for resident students have been larger than those increases for nonresident students over the last four academic years. However, obtaining an increase in the Base Tuition for nonresident students would be of no advantage to an institution given that the tuition is returned to the State as part of the formula funding. This is similar to the way 50% of the indirect cost revenue is returned to the State. It would only be an advantage to increase the rates if there was a change in the method of financing formula funding provided by the State.

The U. T. Board of Regents is given statutory authority to establish the Differential Tuition for all graduate programs and the undergraduate pharmacy program within a range set by law. The Board is allowed by statute to set the Differential Tuition at a rate that is not more than the Base Tuition rate. Unlike the Base Tuition, increases to the Differential Tuition are of direct benefit to an institution, as this income is not part of the formula funding method of finance.

The number and percentage of nonresident students at public academic universities in Texas during fall 2000 is contained in **Attachment A**. The number and percentage of semester credit hours, submitted for state formula funding, generated by nonresident students is contained in **Attachment B**.

While the General Appropriations Act limits enrollment to 10 percent nonresident in medical and dental programs and 20 percent in law programs, the U. T. Board of Regents Rules extends similar limitations to all programs with the U. T. System component institutions (see **Attachment C**).

**Resident and Nonresident Students  
Texas Public Universities, Fall 2000**

Institution	Resident		Out-of-State		Foreign		Total
	Number	Percent	Number	Percent	Number	Percent	
Midwestern State University	5,063	87.1%	408	7.0%	341	5.9%	5,812
Stephen F. Austin State University	11,192	97.7%	206	1.8%	55	0.5%	11,453
Texas A&M University System							
Prairie View A&M University	6,104	92.4%	376	5.7%	129	2.0%	6,609
Tarleton State University	7,166	95.0%	329	4.4%	50	0.7%	7,545
Texas A&M International University	2,875	94.6%	10	0.3%	153	5.0%	3,038
Texas A&M University	37,908	86.1%	2,773	6.3%	3,345	7.6%	44,026
Texas A&M University at Galveston	1,025	75.2%	324	23.8%	14	1.0%	1,363
Texas A&M University-Commerce	7,017	93.8%	153	2.0%	313	4.2%	7,483
Texas A&M University-Corpus Christi	6,603	96.8%	137	2.0%	83	1.2%	6,823
Texas A&M University-Kingsville	5,533	93.1%	83	1.4%	326	5.5%	5,942
Texas A&M University-Texarkana	834	69.8%	360	30.1%	1	0.1%	1,195
West Texas A&M University	6,094	89.9%	489	7.2%	192	2.8%	6,775
Texas Southern University	5,848	84.9%	695	10.1%	343	5.0%	6,886
Texas State University System							
Angelo State University	6,094	96.9%	117	1.9%	79	1.3%	6,290
Lamar University-Beaumont	8,099	94.5%	130	1.5%	339	4.0%	8,568
Sam Houston State University	12,060	97.7%	191	1.5%	97	0.8%	12,348
Southwest Texas State University	21,726	96.9%	341	1.5%	356	1.6%	22,423
Sul Ross State University	1,959	97.5%	33	1.6%	18	0.9%	2,010
Sul Ross State University Rio Grande College	825	99.6%	-	0.0%	3	0.4%	828
Texas Tech University System							
Texas Tech University	21,459	88.7%	1,687	7.0%	1,053	4.4%	24,199
Texas Woman's University	7,913	94.2%	302	3.6%	189	2.2%	8,404
The University of Texas System							
The University of Texas at Arlington	18,161	88.9%	399	2.0%	1,864	9.1%	20,424
The University of Texas at Austin	40,590	81.2%	5,120	10.2%	4,286	8.6%	49,996
The University of Texas at Brownsville	2,812	89.1%	1	0.0%	344	10.9%	3,157
The University of Texas at Dallas	7,942	72.6%	220	2.0%	2,783	25.4%	10,945
The University of Texas at El Paso	12,885	84.6%	481	3.2%	1,858	12.2%	15,224
The University of Texas-Pan American	12,393	97.1%	72	0.6%	295	2.3%	12,760
The University of Texas of the Permian Basin	2,214	97.4%	31	1.4%	27	1.2%	2,272
The University of Texas at San Antonio	17,979	95.5%	382	2.0%	469	2.5%	18,830
The University of Texas at Tyler	3,459	96.3%	76	2.1%	57	1.6%	3,592
University of Houston System							
University of Houston	28,664	89.2%	1,058	3.3%	2,401	7.5%	32,123
University of Houston-Clear Lake	6,517	86.0%	74	1.0%	989	13.0%	7,580
University of Houston-Downtown	8,574	95.8%	26	0.3%	351	3.9%	8,951
University of Houston-Victoria	1,661	97.8%	1	0.1%	36	2.1%	1,698
University of North Texas System							
University of North Texas	23,722	87.7%	1,282	4.7%	2,050	7.6%	27,054

Total	370,970	89.5%	18,367	4.4%	25,289	6.1%	414,626	Attachment A
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**Sch Attempted by Residence Code  
Fall 2000**

<u>Institution</u>	<u>In-State SCH</u>	<u>Percent of Total SCH</u>	<u>Out-of-State SCH</u>	<u>Percent of Total SCH</u>	<u>Foreign SCH</u>	<u>Percent of Total TCH</u>	<u>Total</u>
Angelo State University	72,670	96.9%	1,271	1.7%	1,041	1.4%	74,982
Lamar University	81,210	97.5%	1,090	1.3%	991	1.2%	83,291
Midwestern State University	53,811	88.0%	3,069	5.0%	4,295	7.0%	61,175
Prairie View A&M University	69,037	91.1%	5,479	7.2%	1,292	1.7%	75,808
Sam Houston State University	136,775	98.4%	1,639	1.2%	530	0.4%	138,944
Southwest Texas State University	237,792	97.8%	3,285	1.4%	2,075	0.9%	243,152
Stephen f. Austin State University	134,129	98.0%	2,383	1.7%	382	0.3%	136,894
Sul Ross Rio Grande College	4,578	100.0%	-	-	-	-	4,578
Sul Ross State University	19,049	97.9%	332	1.7%	79	0.4%	19,460
Texas A&M University-Galveston	14,256	74.6%	4,654	24.4%	198	1.0%	19,108
Tarleton State University	74,666	96.5%	2,261	2.9%	419	0.5%	77,346
Texas A&M University-Commerce	53,336	96.3%	1,406	2.5%	654	1.2%	55,396
Texas A&M University-Corpus Christi	61,161	96.5%	1,610	2.5%	609	1.0%	63,380
Texas A&M University-Kingsville	57,581	96.2%	934	1.6%	1,329	2.2%	59,844
Texas A&M University-TeXarkana	4,827	70.8%	1,989	29.2%	-	-	6,816
Texas A&M University-International	23,311	97.7%	19	0.1%	535	2.2%	23,865
Texas A&M University	452,171	94.5%	19,652	4.1%	6,660	1.4%	478,483
Texas Southern University	55,777	85.6%	6,080	9.3%	3,272	5.0%	65,129
Texas Tech University	249,103	92.4%	15,800	5.9%	4,654	1.7%	269,557
Texas Woman's University	49,470	97.0%	835	1.6%	680	1.3%	50,985
University of Houston - Clear Lake	34,129	91.2%	245	0.7%	3,036	8.1%	37,410
University of Houston - Downtown	81,676	95.1%	212	0.2%	4,022	4.7%	85,910
University of Houston - Victoria	6,783	99.3%	-	-	47	0.7%	6,830
University of Houston	265,413	93.0%	8,166	2.9%	11,793	4.1%	285,372
University of North Texas	233,812	90.5%	10,664	4.1%	13,858	5.4%	258,334
The University of Texas at Arlington	155,208	93.2%	3,199	1.9%	8,085	4.9%	166,492
The University of Texas at Austin	445,057	91.6%	23,368	4.8%	17,223	3.5%	485,648
The University of Texas at Dallas	59,307	81.2%	1,640	2.2%	12,058	16.5%	73,005
The University of Texas at El Paso	127,465	84.2%	3,883	2.6%	19,968	13.2%	151,316
The University of Texas of the Permian Basin	18,512	97.4%	206	1.1%	293	1.5%	19,011
The University of Texas at San Antonio	172,675	95.9%	3,633	2.0%	3,759	2.1%	180,067
The University of Texas at Tyler	27,828	96.9%	474	1.7%	404	1.4%	28,706
The University of Texas at Brownsville	16,291	89.2%	-	-	1,979	10.8%	18,270
The University of Texas - Pan American	119,050	97.2%	789	0.6%	2,583	2.1%	122,422
West Texas A&M University	63,098	90.4%	5,856	8.4%	840	1.2%	69,794
<b>Total</b>	<b>3,731,014</b>	<b>93.4%</b>	<b>136,123</b>	<b>3.4%</b>	<b>129,643</b>	<b>3.2%</b>	<b>3,996,780</b>

**U. T. System Board of Regents' Rule:**

Admission of Nonresident Students

No nonresident of the State of Texas shall be enrolled as a new or transfer student in any school, college, or degree-granting program at any component institution of the System when all of the three following conditions occur: (1) when there is a limitation on the number of students who will be enrolled in the class of which such nonresident would be a member if he or she were enrolled; (2) when the result of enrolling such nonresident would be to increase to greater than 10% the percentage of nonresidents enrolled in the class of which such nonresident would be a member if he or she were enrolled; and (3) when at the time of the proposed enrollment of such nonresident, admission to the school, college, or degree-granting program is being denied to one or more Texas residents who have applied for admission and who reasonably demonstrate that they are probably capable of doing the quality of work that is necessary to obtain the usual degree awarded by the school, college, or degree-granting program. It is provided, however, that the nonresident enrollment at the School of Law, The University of Texas at Austin, may be equal to 20% of each class of which nonresidents are a part provided that the admission of such nonresidents is on the basis of academic merit alone.