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FINANCE AND PLANNING COMMITTEE
Committee Chairman Hunt

Date: May 8, 2003

Time: Following the Meeting of the Board

Place: Board Meeting Room, Ninth Floor, Ashbel Smith Hall, 201 West Seventh Street, U. T. System Administration, Austin, Texas

1. **U. T. System: Recommendation to Approve Docket No. 113**

RECOMMENDATION

It is recommended that Docket No. 113 be approved.

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

2. **U. T. System: Request for Authorization of a Permanent Self-Insurance Plan for Directors and Officers Liability and Employment Practices Liability**

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Business Affairs, and the Acting Executive Vice Chancellor for Health Affairs that the U. T. Board of Regents authorize a Permanent Self-Insurance Plan for Directors and Officers Liability and Employment Practices Liability (D&O/EPL) as follows:

a. Authorize a permanent self-insurance plan as the risk financing mechanism for U. T. System's D&O/EPL risks

b. Approve the plan design, including coverage terms and conditions, plan administration, claims management, premium allocation, deductibles, and other financial requirements

c. Allocate $2.7 million in Available University Fund (AUF) reserves to capitalize the self-insurance fund and fund a portion of the premiums for the first year.

BACKGROUND INFORMATION

In September 2002, the Board authorized creation of a Directors and Officers/ Employment Practices Liability self-insurance program. The Board also authorized an interim self-insurance plan under terms consistent with the National Union insurance policy that expired in September 2002. A risk assessment has been performed, and the design of the permanent, self-insurance plan is complete. A summary of the recommended plan is provided below:

- The limits of the permanent self-insurance plan will be $10 million per loss event and annual aggregate for Coverages A and B with an aggregate sub-limit of $5 million for Coverage C.

- There will be no deductible for Coverage A; a $100,000 per person/ $300,000 per loss event deductible for Coverage B; and a $300,000 per loss event deductible for Coverage C. Deductibles are paid by the component institution.

- Claims will continue to be administered by the Office of General Counsel (OGC) and defended to the greatest extent possible by the Attorney General, or a panel of outside counsel selected on behalf of the plan.

- In the event of a coverage dispute with an insured person or insured entity, OGC may appoint independent coverage counsel to review the claim, determine applicability of coverage, and avoid potential conflicts of interest.

- In the first year, the plan will be funded through premiums for current year losses, as well as losses incurred during previous years, but not yet reported.

- Total funding for the plan in the first year is $4.5 million. $1 million in funding was provided for the interim plan, $800,000 will be paid by System Administration and the component institutions, and an additional $2.7 million in AUF reserves will be used to fund the remaining portion of the plan in the first year.

- The plan will be evaluated annually by an actuary to determine future premiums and capitalization requirements.

- If claim costs exceed the available fund balance, a special assessment will be required.

- Component institutions will pay premiums using a methodology that distributes 80% of the premium based on exposures (employee headcount) and 20% based on losses.

This item was presented to the Finance and Planning Committee in April 2003.

3. **U. T. System: Request for Adoption of a Regental Policy Entitled Fire and Life Safety Review Policy for Acquisitions and Conversions of Buildings to be Used for Campus Purposes**

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Academic Affairs, the Executive Vice Chancellor for Business Affairs, and the Acting Executive Vice Chancellor for Health Affairs that a Fire and Life Safety Review Policy for Acquisitions and Conversions of Buildings to be Used for Campus Purposes be adopted as a Regental Policy, substantially in the form set forth on Pages 44 - 50.

The Policy requires U. T. System Administration and U. T. System component institutions to make appropriate advance inquiry as to existing fire and life safety features of any building that is proposed to be acquired, leased, or converted for campus purposes. Additionally, this policy requires an evaluation of the fire and life safety deficiencies of the building and of the corrective actions or renovations required to remedy the deficiencies to ensure compliance with the applicable fire and life safety code.

BACKGROUND INFORMATION

In 1999, the Texas State Fire Marshal's Office was given statutory authority to inspect public buildings for compliance with the National Fire Protection Association (NFPA) Life Safety Code and to make recommendations and/or order correction of identified deficiencies. The State Fire Marshal's Office is required to report its findings from these inspections to the State Senate Finance Committee and House Appropriations Committee.

Adoption of a Fire and Life Safety Review Policy for Acquisitions and Conversions of Buildings to be Used for Campus Purposes as a Regental Policy would implement prudent business practices, which would enhance U. T. System's compliance with applicable codes and further demonstrate U. T. System's commitment to fire and life safety protection.

The Office of Business and Administrative Services, the Real Estate Office, and the Office of Facilities Planning and Construction worked with the U. T. System Environmental Advisory Committee to draft the Policy. Additionally, each component institution's Chief Business Officer was given the opportunity to provide comments and recommended changes to the Policy. Adoption of the Policy as a Regental Policy would be consistent with the current Regental Environmental Review Policy for Acquisitions of Real Property Assets.

This Policy has been reviewed by the U. T. System Office of General Counsel.

This item was presented to the Finance and Planning Committee in April 2003.

THE UNIVERSITY OF TEXAS SYSTEM
FIRE AND LIFE SAFETY REVIEW POLICY
FOR ACQUISITIONS AND CONVERSIONS OF BUILDINGS TO BE USED FOR CAMPUS PURPOSES

Effective Date: Upon Board of Regents' Approval proposed for 5/8/03

It is the policy of The University of Texas System to ensure that, before the U. T. System uses any building for campus purposes, it is in compliance with the applicable fire and life safety code. Consequently, this policy requires advance inquiry about the fire and life safety features of any building that the U. T. System proposes to acquire or to convert for campus purposes. Additionally, this policy requires an evaluation of the fire and life safety deficiencies of the building and of the corrective actions or renovations required to remedy the deficiencies.

Scope

Buildings owned or leased by U. T. System and used for campus purposes shall comply with the edition of the National Fire Protection Association Life Safety Code 101 (NFPA 101), or when applicable, National Fire Protection Association Code 101A (NFPA 101A) adopted and enforced by the Texas State Fire Marshal's Office of the Texas Department of Insurance, as such codes may be amended or supplanted from time to time. This policy governs acquisitions of real property with buildings to be used for campus purposes, whether the acquisition of the real property interest is by gift, purchase, or lease, and conversions of buildings that are to be used for campus purposes. This policy applies to acquisitions and conversions that are initiated after the effective date of this policy. Acquisitions and conversions in process before the policy effective date are exempt from the requirements of this policy.

Definitions

Assembly Occupancy: As defined by the NFPA, a building (1) used for a gathering of 50 or more persons for deliberation, worship, entertainment, eating, drinking, amusement, awaiting transportation, or similar uses; or (2) used as a special amusement building, regardless of occupant load.

Building Used for Campus Purposes: A building or space within a building that is used by U. T. System for education, research, patient care, auxiliary enterprises, business functions, or such other related purposes and uses for the furtherance and fulfillment of the missions of the U. T. System and that is intended for human occupancy.

Component Institution: Component institutions include U. T. Arlington, U. T. Austin, U. T. Brownsville, U. T. Dallas, U. T. El Paso, U. T. Pan American; U. T. Permian Basin, U. T. San Antonio, U. T. Tyler, U. T. Southwestern Medical Center - Dallas, U. T. Medical Branch -

Galveston, U. T. Health Science Center - Houston, U. T. Health Science Center - San Antonio, U. T. M. D. Anderson Cancer Center, U. T. Health Center - Tyler, and U. T. System Administration.

Component Institution Staff Member Responsible for Campus Structures: The staff member at a component institution who is responsible for campus structures and who may have the job title of Director of Campus Planning or Physical Plant Director. The term also includes that staff member's designee.

Component Institution Staff Member Responsible for Campus Safety: The staff member at a component institution who is responsible for campus safety and who may have the job title of Director of Environmental Health and Safety or Institution Safety Officer. The term also includes that staff member's designee.

Life Safety Evaluation: An evaluation to determine a building's compliance with the edition of the NFPA 101, or when applicable, NFPA 101A, adopted and enforced by the Texas State Fire Marshal's Office of the Texas Department of Insurance at the time of building acquisition or conversion.

Qualified Campus Safety Staff Member: A campus safety staff member with the following qualifications: Board of Certified Safety Professionals - Certified Safety Professional; Texas Workers' Compensation - State Approved Professional Safety Source; National Fire Protection Association (NFPA 1031) Fire Inspector Certification; or a certification currently recognized by the Texas State Fire Marshal's Office of the Texas Department of Insurance.

Special Structure: As defined by the NFPA, special structures are open structures, towers, water-surrounded structures, piers, vehicles and vessels, underground and windowless structures.

The Life Safety Evaluation Process

Requirement for a Life Safety Evaluation

A Life Safety Evaluation shall be performed under the following circumstances:

- Before a decision is made by a component institution to acquire real property that has any building(s) to be used for campus purposes; and,
- Before a building owned or leased by U. T. System that is not used for campus purposes is converted to a building used for campus purposes.

A Life Safety Evaluation may need to be performed when a component institution proposes to convert a building that is currently used for campus purposes to a different use that is also for campus purposes. The component institution's chief business officer shall consult with the component institution staff member responsible for campus safety to determine if a Life Safety Evaluation should be performed.

Performance of the Life Safety Evaluation

Before deciding whether to acquire or convert a building covered by this policy, the component institution's chief business officer shall direct the component institution staff member responsible for campus structures or the component institution staff member responsible for campus safety, to gather the following preliminary data regarding the building:

- Last or current occupancy type,
- Historic changes in occupancy,
- Approximate age and general use,
- Special hazards or processes,
- Previous fire history,
- Results of previous fire safety inspections,
- Fire safety equipment (original or additional), and
- Functionality and general condition of all fire and life safety features that may be considered inherent to the structure.

The component institution's staff member may elect to complete the Preliminary Building Risk Assessment Checklist, included as Attachment I to this policy, in order to collect some of the preliminary data.

Such preliminary data will be forwarded to the component institution's chief business officer and the component institution staff members responsible for campus structures and safety. If, based upon review of the preliminary data, and after consultation with the component institution staff members responsible for campus structures and safety, the chief business officer decides to proceed with acquisition or conversion of the building, a Life Safety Evaluation shall be performed.

A Life Safety Evaluation must be conducted by a fire protection-engineering firm, by a qualified campus safety staff member, or by the U. T. System property insurance carrier engineer (if available as an additional service under the U. T. System's Comprehensive Property Protection Program). A fire protection-engineering firm must be retained to conduct a Life Safety Evaluation whenever the building is over seven stories high or classified by the NFPA as a high-rise structure or whenever the building is intended to be used as a medical treatment facility, a research laboratory, a dormitory, an assembly occupancy, or a special structure. Refer to the Definitions section of this policy for the definitions of assembly occupancy and special structure.

The person who conducts the Life Safety Evaluation shall prepare and deliver to the chief business officer a written report that notes all deficiencies, if any, that may prevent the building from meeting applicable NFPA 101 or NFPA 101A standards. Unless a donor, lessor or other outside party agrees to pay for the Life Safety Evaluation, the component institution shall pay all costs to perform a Life Safety Evaluation.

Evaluation of the Life Safety Evaluation Report

Upon review of the Life Safety Evaluation report, and after consultation with the component institution staff members responsible for campus structures and safety, the component institution's chief business officer may decide to abandon the acquisition or conversion, to change to a more compatible use, to demolish the structure, or to continue the evaluation of the possible corrective actions and renovations. The continued evaluation should take into consideration the actual costs of the corrective actions/renovations, the indirect costs resulting from the delay in use of the building, and the advantages to be gained by the use of the building. The component institution staff members responsible for campus structures and safety will be consulted regarding corrective action/renovation matters. In addition, U. T. System's Office of Facilities Planning and Construction (OFPC) will be consulted regarding corrective action/renovation matters if the magnitude of the corrective action/renovation would normally require management by OFPC.

Plan and Budget for Corrective Actions/Renovations

If the chief business officer elects to acquire or convert a building for which the Life Safety Evaluation of the building notes NFPA 101 or NFPA 101A deficiencies, the chief business officer shall prepare a plan that outlines when and how all identified NFPA 101 or NFPA 101A deficiencies will be corrected; or a plan to implement alternative fire and life safety measures that are satisfactory to the State Fire Marshal. U. T. System, Business and Administrative Services, Risk Management shall be available to assist with negotiations with the State Fire Marshal. The chief business officer shall also establish a budget for the corrective action plan or alternative fire and life safety measures plan. The chief business officer shall send a copy of the plan and budget to U. T. System, Business and Administrative Services, Risk Management for informational purposes.

ATTACHMENT I

PRELIMINARY BUILDING RISK ASSESSMENT CHECKLIST

Building:______________________ Address:______________________

Inspector:______________________ Date:______________________

Construction Type		Description
A. Type I, Fire Resistive		
B. Type II, Noncombustible		
C. Type III, Masonry Walls, Wood Joist Roof		
D. Type IV, Heavy Timber		
E. Type V, Wood Frame		

Occupancy Classification	Yes/No	Description
A. Specific use		
B. Number of stories		
C. Number of sublevels		
D. Area in sq. ft. per floor proposed for use		
E. Mixed Occupancy? If Yes, specify		
F. Area separation		
G. Construction separation		
H. Occupancy separation		
I. Structural frame protection		
J. Roof covering		
K. Exterior wall construction		
L. Interior wall construction		
M. Vertical shafts		
N. Interior finish		
O. Fire Protection Maintenance Provider		

Fire Extinguishers	Yes/No	Description
A. Fire Extinguishers present		
B. Inspected/tested monthly		
C. Inspected/tested annually		
D. Fire Protection Maintenance Provider		

Sprinklers	Yes/No	Description
A. Sprinklers Present?		
1. Testing Periodicity		
2. Date of last inspection/test		
3. Fire Protection Maintenance Provider		
4. Hydraulic Design Information Sign/Plate Present		

Standpipes and Hose	Yes/No	Description
A. Standpipes and Hoses present?		
1. Inspection Periodicity		
2. Date of last inspection/test		
3. Fire Protection Maintenance Provider		

Fire Alarm System	Yes/No	Description
A. Fire Alarm System present?		
1. Manual		
2. Automatic		
3. Voice		
4. Annunciated		
5. Testing Periodicity		
B. Details of System		
1. Units		
2. System		
3. Heat detectors		
4. Smoke detectors		
5. Adequately spaced		
6. Type		
7. Locations		
8. Inspected/tested at what intervals		
9. Date of last service		
10. Fire Protection Maintenance Provider		

Life Safety Components	Yes/No	Description
A. Emergency Power Available		
1. Type		
2. Locations		
3. Test Frequency		
4. Test log up to date		
5. Date of last service		
6. Service/maintenance provider		
B. Exit Illumination present?		
1. Means of egress; LSC		
2. Signs		
3. Emergency power		
C. Fire Doors present?		
1. Unlocked		
2. Time Delay		
3. Rating		
4. Hardware		
5. Frame		
6. Closing Device		
7. Latching		
8. Gasketing/Bumpers		
9. Fire door/panic hardware maintained in good working order		
10. Facility maintains a Hazard Surveillance program to include stairwells and MoE		
11. Exit discharge area maintained free & clear		

Life Safety Components (continued)	Yes/No	Description
D. Corridor Width		
1. Height		
2. Fire Rating		
3. Dead ends		
4. In Compliance		
E. Stairs and Ramps in Compliance?		
1. Width		
2. Height		
3. Enclosure		
4. Gradient		
5. Landing		
6. Venting		
7. Vestibule		
8. Roof access		
9. Handrails		
10. Barrier at Exit discharge		

Elevator Testing	Yes/No	Description
A. Elevator Fire Recall System		
B. Elevators are tested monthly		
C. Elevator Maintenance Provider		

Other Fire Protection Services	Yes/No	Description
A. Other Fire Protection Services Available		
1. Type		
2. Inspection Periodicity		
3. Date of last inspection/test		
4. Fire Protection Maintenance Provider		

Comments:____

4. **U. T. System: Request for Approval of a New Regental Policy Entitled The University of Texas System Debt Policy**

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Business Affairs and the Vice Chancellor and General Counsel that the U. T. Board of Regents adopt a Regental Policy entitled The University of Texas System Debt Policy, substantially in the form set out on Pages 52 - 54.

BACKGROUND INFORMATION

The U. T. System issues debt through three primary programs: the Revenue Financing System (RFS), the Permanent University Fund (PUF), and the Higher Education Assistance Fund (HEAF). The U. T. System Debt Policy will govern the use of debt under each of these programs to finance capital projects within the U. T. System.

In addition to compliance with the U. T. System Debt Policy, any debt incurred by the U. T. System will be issued pursuant to a resolution approved by the U. T. Board of Regents and in accordance with the laws of the State of Texas. Before any debt can be issued, the U. T. System must obtain an opinion from bond counsel that the issue complies with applicable State and federal laws. The U. T. System must also receive the necessary approvals from both the Texas Bond Review Board and the Texas Attorney General.

This policy has been reviewed by outside bond counsel and the U. T. System Office of General Counsel.

This item was presented to the Finance and Planning Committee in April 2003.

The University of Texas System Debt Policy

Purpose

This policy governs the use of debt to finance capital projects within The University of Texas System ("System"). The prudent use of debt can help the System achieve its strategic objectives while maintaining a credit rating that appropriately balances financial flexibility with cost of capital.

Financing Programs

The System issues debt through three primary programs, the Revenue Financing System ("RFS"), the Permanent University Fund ("PUF"), and the Higher Education Assistance Fund ("HEAF"). This policy will govern the issuance of all System debt.

Revenue Financing System - The RFS was created by the Board of Regents of The University of Texas System ("Board") through the adoption of a Master Resolution on February 14, 1991. The Board established the RFS for the purpose of assembling the System's revenue-supported debt capacity into a single financing program in order to provide a cost-effective debt program to component institutions of the System and to maximize the financing options available to the Board.

Permanent University Fund - Article VII, Section 18 of the Texas Constitution authorizes the Board to issue bonds and notes secured by the System's interest in the Available University Fund ("AUF"). The AUF consists of distributions from the total return of PUF investments. The Constitution limits the amount of PUF debt that may be issued by the System to 20% of the cost value of investments and other assets of the PUF. The Constitution prohibits the issuance of PUF debt for auxiliary projects.

Higher Education Assistance Fund ("HEAF") - Article VII, Section 17 of the Texas Constitution authorizes the Board to issue bonds and notes secured by pledged revenues consisting of up to 50% of the money allocated annually to the Board for U. T. Pan American and U. T. Brownsville. Bonds issued under this authority are typically referred to as HEAF bonds or constitutional appropriation bonds. The Constitution prohibits the issuance of HEAF debt for auxiliary projects, except to the extent of a project's use for educational and general activities.

Authority

All debt incurred by the System will be issued or incurred pursuant to resolutions approved by the U. T. Board of Regents and in accordance with the general laws of the State of Texas, including particularly Article VII, Sections 17 and 18 of the Texas Constitution, Chapters 55 and 65 of the Texas Education Code, and Chapters 1207 and 1371 of the Texas Government Code. Before any debt can be issued, the System must obtain an opinion from bond counsel that the issue complies with applicable Texas and federal laws. The System must also receive the necessary approvals from both the Texas Bond Review Board and the Texas Attorney General.

Debt Guidelines

Any debt must be issued in strict compliance with applicable law. The following debt guidelines will apply:

I. *Project Funding*- The System will borrow money, through the issuance of debt, to finance only those projects that have been approved for financing by the Board of Regents. Capital projects are generally evaluated and prioritized through the System's Capital Improvement Program. For construction projects that require debt financing, bond proceeds will be provided only after design development approval and appropriation of funds by the Board of Regents.

II. *Interest Rate Exposure-* The Office of Finance will evaluate and determine the appropriate amount of its interest rate exposure, defined as the possible increase in capital costs resulting from rising short-term interest rates. The System will limit its variable rate debt in accordance with rating agency guidelines for assessing the debt structure of peer institutions of higher education with comparable credit ratings. In determining the amount of variable rate debt, the Office of Finance will evaluate the level of variable rate assets that may be available to provide a natural hedge to interest rate fluctuations. The System will seek to minimize its cost of capital within a prudent level of exposure to interest rate volatility. The System shall broadly target variable rate debt of 30-50% of total outstanding debt.

III. *Amortization-* The amortization of tax-exempt debt will be based on the types of assets financed, the expected availability of cashflows to meet debt service requirements, and tax regulations. Generally, the amortization of tax-exempt debt should not exceed the useful life of the financed asset and may never exceed the Internal Revenue Service limit of 120% of the useful life of the financed asset. The maximum maturity of RFS debt is limited to 50 years by Chapter 55 of the Texas Education Code. The maximum maturity of PUF debt is limited to 30 years by Article VII, Section 18 of the Texas Constitution. The maximum maturity of HEAF debt is limited to 10 years by Article VII, Section 17 of the Texas Constitution.

IV. *Financial Ratios-* The System will use selected actual and pro forma financial ratios, consistent with major credit rating agency criteria, to ensure the System is operating within appropriate financial bounds. Although other ratios may also be evaluated, the primary financial ratios to be analyzed include the debt service coverage ratio, the debt burden ratio, and the leverage ratio.

V. *Economies of Scale-* Debt financings will be coordinated to the extent practical so that multiple project needs can be accommodated in a single borrowing, thereby increasing the efficiency of the debt issuance. Since many issuance costs do not vary with the size of a borrowing, a large bond issue increases the efficiency of the financing by spreading fixed costs over a greater number of projects.

VI. *Refunding Opportunities-* The Office of Finance will actively consider refinancing of outstanding debt issues when net savings for that refinancing, measured on a net present value basis, are positive. Since there are limitations on the number of allowable refinancings, it is important to use refinancing opportunities wisely. In evaluating refunding opportunities, the Office of Finance will consider the value of the call option to be exercised, including the amount of time to the call date and the amount of time from the call date to maturity. Based on these and other factors, the Office of Finance will determine the minimum savings threshold for any particular refunding transaction. Refundings that do not produce savings may be considered under certain circumstances, such as eliminating restrictive bond covenants or other situations that produce a greater benefit to the System.

VII. *Disclosure-* The Office of Finance will provide updated financial information and operating data and timely notice of specified material events to each nationally recognized municipal securities information repository and any state information depository, pursuant to its continuing disclosure undertakings with respect to Rule 15c2-12 promulgated by the Securities and Exchange Commission.

VIII. *Hedging Instruments-* The Office of Finance will consider the use of interest rate swaps and other interest rate risk management tools after carefully evaluating the risks and benefits of any proposed transaction, in accordance with the U. T. System Interest Rate Swap Policy. By using swaps in a prudent manner, the System can take advantage of market opportunities to minimize expected costs and manage interest rate risk. As outlined in the U. T. System Interest Rate Swap Policy, the use of swaps must be tied directly to System debt instruments. The System shall not enter into swap transactions for speculative purposes.

IX. *Project Financing-* The Office of Finance will consider the use of project financing in those limited circumstances where the benefits of such a transaction exceed the increased costs. Project financing can be a useful financing technique in certain circumstances; however, these transactions are typically less efficient and more costly than traditional financing due to lower credit ratings, fewer economies of scale, the funding of a reserve fund, and the cost of bond insurance. Project financing does not preserve or increase debt capacity relative to traditional financing. The credit rating agencies and the System include project debt when assessing the debt capacity of component institutions.

X. *Taxable Debt-* The System may use taxable debt for those projects that have an intended use or other characteristics that preclude the use of tax-exempt debt. The System will strive to allocate its available resources, including equity capital, among its various capital projects to minimize or eliminate the need to issue taxable debt, thereby minimizing the System's cost of capital. Any use of taxable debt would require separate Board approval and be subject to the same statutory requirements as tax-exempt debt.

XI. *Reporting Requirements-* The Annual Financial Report ("AFR") prepared by the System and presented to the Board will discuss the status of all outstanding bond and note indebtedness. The AFR presented to the Board provides detailed information on the System's outstanding bonds and notes, including, by series, the amount outstanding, interest rates, maturity dates, a summary of the changes in outstanding indebtedness, and the associated debt service requirements.

5. **U. T. System: Request for Approval of Amendments to the Regental Policy Entitled Available University Fund Spending Policy**

RECOMMENDATION

The Chancellor concurs in the recommendation of the Executive Vice Chancellor for Business Affairs and the Vice Chancellor and General Counsel that the Regental Policy entitled Available University Fund Spending Policy be amended as set forth in congressional style on Pages 56 - 57.

BACKGROUND INFORMATION

The Board approved the Available University Fund (AUF) Spending Policy in April 1993 to establish procedures for the approval of Permanent University Fund (PUF) funded projects, criteria for project selection, minimum debt service coverage, and minimum reserve balance.

The amendments primarily update the AUF spending policy to reflect current U. T. System practices, such as quarterly reporting on the PUF, and to make the AUF spending policy consistent with other U. T. System policies such as the PUF investment policy. Other changes amend the PUF project justification criteria to make them consistent with criteria included in the Capital Improvement Program.

This Policy has been reviewed by the U. T. System Office of General Counsel.

This item was presented to the Finance and Planning Committee in April 2003.

AVAILABLE UNIVERSITY FUND SPENDING POLICY

In order to provide a consistent and dependable level of funding and to maintain the highest credit ratings level possible, the appropriation of the Available University Fund (AUF) shall be governed by the following:

A. Any staff recommendation to appropriate funds from the AUF or from Permanent University Fund (PUF) bond proceeds will be presented in the context of that appropriation's impact on: (a) AUF funding for the support and maintenance of U. T. Austin[~~U. T. Austin operations~~], (b) bond ratings, (c) projected AUF balances, and (d) other PUF projects in the Capital Improvement Program [~~Plan~~] (CIP). As such, the following procedures will apply:

1. A forecast of at least six years of the income and expenditures of the AUF will be presented at each meeting of the U. T. Board of Regents' Finance and Planning Committee by the Office of Finance. Quarterly, The University of Texas Investment Management Company (UTIMCO) shall provide to the Office of Finance a forecast of the PUF distributions to the AUF that will be the basis of the AUF forecast. Included as part of the AUF forecast will be the projected amount of remaining PUF debt capacity calculated in accordance with this policy. [~~Prior to each meeting of the U. T. Board of Regents at which a PUF funded project or AUF expenditure is submitted for approval, a forecast of at least seven years of the income and expenditures of the Available University Fund shall be completed. That forecast shall include, as separately identified expenditures, each of the proposed PUF projects recommended for approval in that agenda.~~]

2. As a part of each agenda item requesting approval of AUF expenditures or PUF funded projects, a statement indicating compliance with this policy based on the most recent forecast shall be included.

[~~3. Accompanying the forecast, there will be a listing of all PUF projects from the CIP which are in a delayed or pending status and the amount of time they have already been delayed, plus a listing of all other projects which may be delayed as a result of the actions recommended for that meeting.~~]

[4]3. In preparing recommendations for projects to be approved, the staff will be guided by the following [~~general priorities~~]justification criteria:

   a. [~~Repair and renovation projects~~]Consistency with institution's mission;

   b. [~~Library and equipment projects~~]Project need;

   c. [~~New construction projects.~~]Unique opportunity;

   d. Matching funds/leverage;

   e. Cost effectiveness;

   f. State of existing facility condition; and

   g. Other available funding sources.

   [~~While these general priorities will shape recommendations, the specific merits of an individual proposed project will determine which of several pending projects across all categories as well as within each category may be recommended for funding as resources become available. In selecting which projects will be recommended, the staff will consider the following attributes:~~]

[~~a. Emergency needs~~

~~b. Contribution to the mission of the U. T. System as well as to the mission of the component~~

~~c. Availability of alternate sources of funding including the use of revenue bonds~~

~~d. Leveraging effect from external financial participation and internal sources and operating efficiencies.~~]

[5]4. No project will be recommended for approval, if in any of the forecasted years, the required appropriations from the AUF or PUF bond proceeds would cause:

a. The forecasted AUF expenditures for program enrichment at U. T. Austin to fall below 45 percent, of the sum of the projected U. T. System share of the net divisible AUF annual income and interest income on AUF balances (subject to the limits imposed by b. and c. below);

b. Debt service coverage to be less than 1.50:1.00 and;

c. The forecasted end of year AUF balance to be less than $30 million.

B. Permanent University Fund Investment Income Forecast and AUF Expenditures

1. In conjunction with the annual U. T. System budget process, UTIMCO shall recommend to the U. T. Board of Regents in May of each year an amount to be distributed to the AUF during the next fiscal year. UTIMCO's recommendation on the annual distribution shall be an amount equal to 4.75% of the trailing twelve quarter average of the net asset value of the PUF for the quarter ending February of each year.[~~The University of Texas Investment Management Company shall provide a forecast of the investment income of the Permanent University Fund at least annually prior to the adoption of the U. T. System Capital Budget and Operating Budgets of U. T. Austin and the U. T. System Administration. In order to assure a high level of confidence in the results, the forecast will be based on the lower of current interest rates or long-term historical interest rates and explicitly stated assumptions. Concurrence of the Investment Advisory Committee on assumptions will be sought.~~]

2. Operating expenditures of the U. T. System Administration will be carefully controlled in order to maximize the opportunity to meet the capital needs of the component institutions and the operating budget needs of U. T. Austin. Wherever possible, alternate funding from component institutions, State [~~state~~] funds, or other sources will be sought. Programs for which alternative funding cannot be obtained will be evaluated for possible reductions or phase out.

3. [~~Each two years beginning in June 1993 the~~]The [~~Capital Improvement Plan (~~]CIP[~~)~~] will be reviewed and updated every two years. The update will include an estimated start date for each project which will be based on the criteria set forth in Section [A4] A3 above, project readiness, projected fund availability, and relative urgency of need for the completed project.

[~~4. During each fiscal year, the aggregate transfers to U. T. Austin from its annual AUF appropriation will be limited to no more than the ratable portion of the appropriation for the year unless prior approval is obtained from the Chancellor.~~]

6. **U. T. System: Recommendation to Approve Fiscal Year 2004 Budget Preparation Policies and Limitations for General Operating Budgets, Auxiliary Enterprises, Contracts and Grants, Restricted Current Funds, Designated Funds, and Service and Revolving Funds Activities; and Calendar for Budget Operations**

RECOMMENDATION

With the concurrence of the U. T. System Executive Officers, the Chancellor recommends that the U. T. Board of Regents approve Budget Preparation Policies and Limitations and Calendar for use in preparing the Fiscal Year 2004 Operating Budget for the U. T. System as set out below:

U. T. System FY 2004 Budget Preparation Policies

General Guidelines – The regulations and directives that will be included in the General Appropriations Act enacted by the 78th Texas Legislature serve as the basis for these guidelines and policies. In preparing the draft of the FY 2004 Operating Budget, the president of each component institution should adhere to guidelines and policies as detailed below and as included in the General Appropriations Act. Following legislative approval of the General Appropriations Act, the Chancellor will issue detailed instructions regarding the implementation of those regulations and directives into the component budget process.

Overall budget totals, including reasonable reserves, must be limited to the funds available for the year from General Revenue Appropriations, Estimates of Educational and General Income, and limited use of institutional unappropriated balances.

Salary Guidelines – Recommendations regarding salary policy are subject to the following directives:

1. Salaries Proportional by Fund – Unless otherwise restricted, payment for salaries, wages, and benefits paid from appropriated funds, including local funds and educational and general funds as defined in Texas Education Code Section 51.009 (a) and (c), shall be proportional to the source of funds.

2. Merit Increases – Subject to available resources and resolution of any major salary inequities, institutions should give priority to implementing merit salary increases for faculty and staff.

   Merit increases or advances in rank for faculty are to be on the basis of teaching effectiveness, research, and public service.

Merit increases or promotions for administrative and professional staff and classified staff are to be based on evaluation of performance in areas appropriate to work assignments.

To be eligible for a merit increase, classified staff must have been employed by the institution for at least six months as of August 31, 2003.

3. Other Increases – Equity adjustments, competitive offers, and increases to accomplish contractual commitments may also be granted in this budget and should also consider merit where appropriate, subject to available resources. Such increases should be noted and explained in the supplemental data accompanying the budget.

4. New Positions – Subject to available resources, new administrative and professional, classified staff and faculty positions are to be requested only when justified by workloads or to meet needs for developing new programs.

5. Tobacco Settlement Funds – The distribution from the Endowment Funds appropriated to Higher Education and to the Permanent Health Fund for Health Related Institutions should be estimated at $0.047 per unit as shown in the following tables:

Individual Endowments

Component	Annual
U. T. El Paso	$1,175,000
U. T. SWMC Dallas	2,350,000
U. T. MB Galveston	1,175,000
U. T. HSC Houston	1,175,000
U. T. HSC San Antonio	9,400,000
U. T. MDA Cancer Ctr.	4,700,000
U. T. HC Tyler	1,175,000
U. T. RAHC*	940,000

*Lower Rio Grande Valley Regional Academic Health Center (RAHC)

Permanent Health Fund

Component	Annual
U. T. SWMC Dallas	$2,210,594
U. T. MB Galveston	1,875,745
U. T. HSC Houston	1,807,273
U. T. HSC San Antonio	1,651,546
U. T. MDA Cancer Ctr.	1,751,117
U. T. HC Tyler	1,219,323

6. It is the expectation that FY 2004 salary increases for merit, equity, or other reasons be included in the Operating Budgets.

Staff Benefits Guidelines – Recommendations regarding the State contribution for employee staff benefits such as group insurance premiums, teacher retirement, and optional retirement are subject to legislative determination via the General Appropriations Act. Upon approval of this legislation, the Chancellor will issue appropriate instructions regarding the implementation of the benefits into the budget process.

Other Employee Benefits – Employer contributions to the self-insured Unemployment Compensation Fund are based on an actuarial study. Workers' Compensation Insurance rates are experience rated for each component. The Chancellor will issue appropriate instructions regarding the implementation of Unemployment Compensation Fund and Workers' Compensation Insurance Benefits.

Other Operating Expenses Guidelines – Increases in Maintenance, Operation, Equipment, and Travel are to be justified by expanded workloads, for developing new programs, or for correcting past deferrals or deficiencies.

Budget Reductions and Limitations – The General Appropriations Act may contain provisions requiring budget reductions and budget restrictions which may impact the FY 2004 Operating Budget. Upon approval of this legislation, the Chancellor or other appropriate authority will issue instructions regarding the implementation of any of these reductions and limitations into the budgeting process.

2004 Operating Budget Calendar

May 8, 2003	U. T. Board of Regents approves budget policies
June 2-9, 2003	Budget goals and priorities/resource allocation hearings with System Administration
June 20, 2003	Draft copies of budgets, salary rosters, and supplemental data due to System Administration
June 30 – July 8, 2003	Technical budget hearings with System Administration
July 14, 2003	Final copies of budgets, salary rosters, and supplemental data due to System Administration
July 30, 2003	Operating Budget Summaries mailed to U. T. Board of Regents
August 6-7, 2003	U. T. Board of Regents approves Operating Budget
August 15, 2003	Approved budgets and salary rosters due to System Administration for copying and binding

BACKGROUND INFORMATION

The U. T. System FY 2004 Budget Preparation Policies will track the regulations and directives that will be included in the General Appropriations Act to be enacted by the 78th Texas Legislature. Following legislative approval of the General Appropriations Act, the Chancellor will issue detailed instructions regarding the implementation of these regulations and directives.

This item was presented to the Finance and Planning Committee in April 2003.

7. **U. T. System: Report on Investments for the Five Months Ended January 31, 2003**

REPORT

Pages 63 - 71 contain the Summary Reports on Investments for the five months ended January 31, 2003.

Item I on Pages 63 - 65 reports summary activity for the Permanent University Fund (PUF) investments. The PUF's net investment return for the five months was negative 1.61%. The PUF's net investment return for marketable securities for the five months was negative 1.08% versus its composite benchmark return of negative 2.16%. The PUF's net asset value decreased by $433.5 million since the beginning of the year to $6,304.8 million. This decrease reflects the annual distribution to the AUF made in September 2002 for $363.0 million.

Item II on Pages 66 - 69 reports summary activity for the General Endowment Fund (GEF), the Permanent Health Fund (PHF), and Long Term Fund (LTF). The GEF's net investment return for the five months was negative 1.52%. The GEF's net investment return for marketable securities for the five months was negative 1.09% versus its composite benchmark return of negative 2.16%. The GEF's net asset value decreased $32.6 million since the beginning of the year to $3,260.6 million.

Item III on Page 70 reports summary activity for the Short Intermediate Term Fund (SITF). Total net investment return on the SITF was 0.86% for the five months versus the SITF's performance benchmark of 1.71%. The SITF's net asset value increased by $83.7 million since the beginning of the year to $1,519.6 million.

Item IV on Page 71 presents book and market value of cash, fixed income, equity, and other securities held in funds outside of internal investment pools. Total cash and equivalents, consisting primarily of component operating funds held in the Dreyfus money market fund, increased by $519,781 thousand to $1,797,911 thousand during the three months. Market values for the remaining asset types were fixed income securities: $315,453 thousand versus $283,452 thousand at the beginning of the period; equities: $186,523 thousand versus $131,845 thousand at the beginning of the period; and other investments: $43 thousand versus $21 thousand at the beginning of the period.

This item was presented to the Finance and Planning Committee in April 2003.

I. PERMANENT UNIVERSITY FUND (1)

a.) Summary Investment Report at January 31, 2003 (2)

($ millions)

	FY01-02	FY02-03		
	Full Year	Two Months Ending October 31, 2002	Three Months Ending January 31, 2003	Year-to-Date
Beginning Net Assets	7,540.1	6,738.3	6,272.6	6,738.3
PUF Lands Receipts (3)	80.5	14.2	23.1	37.3
Investment Return	(522.9)	(113.8)	13.8	(100.0)
Expenses	(21.0)	(3.1)	(4.7)	(7.8)
Distributions to AUF	(338.4)	(363.0)	-	(363.0)
Ending Net Assets	6,738.3	6,272.6	6,304.8	6,304.8
AUF Distribution:				
From PUF Investments	338.4	363.0		363.0
From Surface Income	8.1	0.6	2.0	2.6
Total	346.5	363.6	2.0	365.6
Total Net Investment Return	-7.35%	-1.79%	0.18%	-1.61%

(1) Report prepared in accordance with Texas Education Code Sec. 51.0032.

(2) General - The Investment Summary Report excludes PUF Lands mineral and surface interests with estimated August 31, 2002 values of $639.8 million and $161.1 million, respectively.

(3) PUF Lands Receipts - As of January 31, 2003: 1,158,086 acres under lease; 522,319 producing acres; 3,134 active leases; and 2,076 producing leases.

I. PERMANENT UNIVERSITY FUND (continued)

b.) Comparison of Asset Allocation Versus Endowment Neutral Policy Portfolio and Net Investment Return for the five months ended January 31, 2003
(Asset Allocation and Benchmarks Approved by the UTIMCO Board)

	Asset Allocation	Endowment Neutral Policy Portfolio	Actual Net Investment Return	Endowment Neutral Policy Portfolio Return (1)	Benchmark
Cash and Cash Equivalents	0.7%	0.0%	0.65%	0.69%	90 Day T-Bills Average Yield
Domestic Public Equities					Wilshire 5000 U.S. Equities Index
Passive Management	13.9%		-5.66%	-5.44%	
Active Management	10.7%		-4.17%	-5.44%	
Hedge and Structured Active Management	6.0%		-1.97%	-5.44%	
Total Domestic Public Equities	30.6%	31.0%	-4.66%	-5.44%	
International Public Equities					Morgan Stanley Capital International - All Country World Free ex U.S.
Passive Management	6.4%		-7.81%	-7.81%	
Active Management	8.4%		-5.91%	-7.81%	
Hedge and Structured Active Management	0.6%		4.00%	-7.81%	
Total International Public Equities	15.4%	19.0%	-6.39%	-7.81%	
Absolute Return	8.1%	10.0%	6.78%	2.37%	90 Day T-Bills Average Yield plus 4%
Inflation Hedging	9.5%	10.0%	2.36%	4.32%	(25% Goldman Sachs Commodity Index minus 100 basis points) plus (25% Treasury Inflation Protected Securities) plus (25% National Commercial Real Estate Index Fund) plus (25% Wilshire Associates Real Estate Securities Index)
Fixed Income	21.2%	15.0%	4.19%	3.08%	(33% Lehman Brothers Aggregate Bond Index ex U.S. Governments) plus (67% Lehman Brothers Government Bond Index)
Total Marketable Securities	85.5%	85.0%	-1.06%	-2.16%	
Private Capital	14.5%	15.0%	-4.61%	-3.84%	Wilshire 5000 U.S. Equities Index plus 4% (2)
Total	100.0%	100.0%	-1.61%	-2.38%	

(1) The benchmark return for the endowment neutral policy portfolio is calculated by summing the neutrally weighted index return (% weight for the asset class multiplied by the benchmark return for the asset class) for the various asset classes in the endowment portfolio for the period reported.
(2) Due to valuation and liquidity characteristics associated with Private Capital, short-term benchmark comparisons are not appropriate.

UTIMCO 4/4/2003

c.) Comparison of Asset Allocation Versus Endowment Neutral Policy Portfolio and Net Investment Return for the five months ended January 31, 2003
(Prior Asset Allocation)

	Asset Allocation	Endowment Neutral Policy Portfolio	Endowment Neutral Policy Portfolio Return (1)	Benchmark
Cash	0.7%	0.0%	0.69%	90 Day T-Bills Average Yield
Domestic Common Stocks:				
Large/Medium Capitalization Equities	17.0%	25.0%	-5.88%	Standard and Poor's 500 Index
Small Capitalization Equities	7.5%	7.5%	-4.19%	Russell 2000 Index
Total Domestic Common Stocks	24.5%	32.5%		
International Common Stocks:				
Established Markets	10.6%	12.0%	-8.95%	Morgan Stanley Capital International Europe, Asia, Far East Index (net)
Emerging Markets	4.3%	3.0%	-2.83%	Morgan Stanley Capital International Emerging Markets Free
Total International Common Stocks	14.9%	15.0%		
Inflation Hedging	9.5%	7.5%	7.53%	33% (Goldman Sachs Commodity Index minus 100 basis points) plus 67% (*National* Commercial Real Estate Index Fund)
Fixed Income:				
Domestic	16.7%	15.0%	3.31%	Lehman Brothers Aggregate Bond Index
International	4.5%	5.0%	8.70%	Salomon Non-U.S. World Government Bond Index, Unhedged
Total Fixed Income	21.2%	20.0%		
Marketable Alternative Equities	14.7%	10.0%	3.65%	90 Day T-Bills Average Yield plus 7%
Total Marketable Securities	85.5%	85.0%	-1.04%	
Non-Marketable Alternative Equities	14.5%	15.0%	-3.84%	Wilshire 5000 U.S. Equities Index plus 4%
Total	100.0%	100.0%	-1.42%	

(1) The benchmark return for the endowment neutral policy portfolio is calculated by summing the neutrally weighted index return (% weight for the asset class multiplied by the benchmark return for the asset class) for the various asset classes in the endowment portfolio for the period reported.

II. GENERAL ENDOWMENT FUND (1)

a.) Summary Investment Report at January 31, 2003

($ millions)

	FY01-02		FY02-03					
	Full Year		Two Months Ending October 31, 2002		Three Months Ending January 31, 2003		Year-to-Date	
Beginning Net Assets	3,723.9		3,293.2		3,259.5		3,293.2	
Net Contributions	(230.7)		(7.9)		(23.0)		(30.9)	
Investment Return	(245.3)		(65.4)		16.0		(49.4)	
Expenses	(7.2)		(0.7)		(1.3)		(2.0)	
Allocations (2)	52.5		40.3		9.4		49.7	
Ending Net Assets	**3,293.2**		**3,259.5**		**3,260.6**		**3,260.6**	
Net Asset Value per Unit	**90.932**		**89.124**		**89.519**		**89.519**	
Units and Percentage Ownership (End of Period):								
PHF	7,676,762	21.2%	7,676,762	21.0%	7,569,273	20.8%	7,569,273	20.8%
LTF	28,539,389	78.8%	28,895,452	79.0%	28,853,799	79.2%	28,853,799	79.2%
Total	**36,216,151**	**100.0%**	**36,572,214**	**100.0%**	**36,423,072**	**100.0%**	**36,423,072**	**100.0%**
Total Net Investment Return	**-6.96%**		**-1.97%**		**0.46%**		**-1.52%**	

(1) Report prepared in accordance with Texas Education Code Sec. 51.0032.

(2) The GEF allocates its net investment income and realized gain or loss to its unitholders at month end. The allocated investment income and realized gain amounts are considered reinvested as GEF contributions. Any allocated realized losses reduce the cost basis of the units in the GEF. Since the allocation is proportional to the percentage of ownership by the unitholders, no additional units are purchased.

II. GENERAL ENDOWMENT FUND (continued)

b.) Unitholders' Summary Investment Report at January 31, 2003 (1)

($ millions)

	FY01-02	FY02-03		
	Full Year	Two Months Ending October 31, 2002	Three Months Ending January 31, 2003	Year-to-Date
PERMANENT HEALTH FUND				
Beginning Net Assets	881.4	698.2	677.8	698.2
Withdrawals	(88.2)	-	-	-
Investment Return	(52.6)	(13.9)	3.3	(10.6)
Expenses	(0.6)	(0.1)	(0.2)	(0.3)
Distributions (Payout) (2)	(41.8)	(6.4)	(9.6)	(16.0)
Ending Net Assets	**698.2**	**677.8**	**671.3**	**671.3**
Net Asset Value per Unit (3)	0.851524	0.826627	0.818610	0.818610
No. of Units (End of Period)	820,000,000	820,000,000	820,000,000	820,000,000
Distribution Rate per Unit	**0.04700**	**0.00783**	**0.01175**	**0.01958**
Total Net Investment Return	**-7.05%**	**-2.01%**	**0.42%**	**-1.60%**
LONG TERM FUND				
Beginning Net Assets	2,843.3	2,595.1	2,551.6	2,595.1
Net Contributions	89.3	34.9	31.8	66.7
Investment Return	(199.7)	(52.2)	11.5	(40.7)
Expenses	(3.0)	(2.6)	(0.1)	(2.7)
Distributions (Payout) (2)	(134.8)	(23.6)	(35.8)	(59.4)
Ending Net Assets	**2,595.1**	**2,551.6**	**2,559.0**	**2,559.0**
Net Asset Value per Unit (3)	4.788	4.645	4.602	4.602
No. of Units (End of Period)	542,049,359	549,346,011	556,060,529	556,060,529
Distribution Rate per Unit	**0.25100**	**0.04300**	**0.06450**	**0.10750**
Total Net Investment Return	**-6.97%**	**-1.96%**	**0.45%**	**-1.52%**

(1) The Permanent Health Fund (PHF) and Long Term Fund (LTF) are internal mutual funds for the pooled investment of endowment funds. The PHF is comprised of endowments for health-related institutions of higher **education and the LTF is comprised of privately raised endowments and other long term funds of UT System components.**

(2) The PHF and LTF accrue for their respective quarterly distributions on a monthly basis. In order to generate the **cash** for the distributions, the PHF and LTF sell units at quarter end. Therefore, the **total PHF and LTF net assets will be less than the GEF net assets on month ends other than fiscal quarter ends.**

(3) The asset allocation of the PHF and LTF is representative of the asset allocation for the GEF.
A nominal amount of cash is held in PHF and LTF to pay expenses incurred separately by these funds.

II. GENERAL ENDOWMENT FUND (continued)

c.) Comparison of Asset Allocation Versus Endowment Neutral Policy Portfolio and Net Investment Return for the five months ended January 31, 2003
(Asset Allocation and Benchmarks Approved by the UTIMCO Board)

	Asset Allocation	Endowment Neutral Policy Portfolio	Actual Net Investment Return	Endowment Neutral Policy Portfolio Return (1)	Benchmark
Cash and Cash Equivalents	0.4%	0.0%	0.65%	0.69%	90 Day T-Bills Average Yield
Domestic Public Equities					Wilshire 5000 U.S. Equities Index
Passive Management	14.6%		-5.50%	-5.44%	
Active Management	11.4%		-5.04%	-5.44%	
Hedge and Structured Active Management	6.4%		-1.92%	-5.44%	
Total Domestic Public Equities	32.4%	31.0%	-4.82%	-5.44%	
International Public Equities					Morgan Stanley Capital International - All Country World Free ex
Passive Management	7.0%		-7.71%	-7.81%	
Active Management	8.4%		-5.96%	-7.81%	
Hedge and Structured Active Management	0.6%		4.00%	-7.81%	
Total International Public Equities	16.0%	19.0%	-6.43%	-7.81%	
Absolute Return	8.7%	10.0%	6.75%	2.37%	90 Day T-Bills Average Yield plus 4%
Inflation Hedging	9.6%	10.0%	2.47%	4.32%	(25% Goldman Sachs Commodity Index minus 100 basis points) plus (25% Treasury Inflation Protected Securities) plus (25% National Commercial Real Estate Index Fund) plus (25% Wilshire Associates Real Estate Securities Index)
Fixed Income	21.2%	15.0%	4.46%	3.08%	(33% Lehman Brothers Aggregate Bond Index ex U.S. Governments) plus (67% Lehman Brothers Government Bond
Total Marketable Securities	88.3%	85.0%	-1.09%	-2.16%	
Private Capital	11.7%	15.0%	-4.68%	-3.84%	Wilshire 5000 U.S. Equities Index plus 4% (2)
Total	100.0%	100.0%	-1.52%	-2.38%	

(1) The benchmark return for the endowment neutral policy portfolio is calculated by summing the neutrally weighted index return (% weight for the asset class multiplied by the benchmark return for the asset class) for the various asset classes in the endowment portfolio for the period reported.
(2) Due to valuation and liquidity characteristics associated with Private Capital, short-term benchmark comparisons are not appropriate.

d.) Comparison of Asset Allocation Versus Endowment Neutral Policy Portfolio and Net Investment Return for the five months ended January 31, 2003.
(Prior Asset Allocation)

	Asset Allocation	Endowment Neutral Policy Portfolio	Endowment Neutral Policy Portfolio Return (1)	Benchmark
Cash	0.4%	0.0%	0.69%	90 Day T-Bills Average Yield
Domestic Common Stocks:				
Large/Medium Capitalization Equities	17.8%	25.0%	-5.88%	Standard and Poor's 500 Index
Small Capitalization Equities	8.2%	7.5%	-4.19%	Russell 2000 Index
Total Domestic Common Stocks	26.0%	32.5%		
International Common Stocks:				
Established Markets	10.9%	12.0%	-8.95%	Morgan Stanley Capital International Europe, Asia, Far East Index (net)
Emerging Markets	4.6%	3.0%	-2.83%	Morgan Stanley Capital International Emerging Markets Free
Total International Common Stocks	15.5%	15.0%		
Inflation Hedging	9.6%	7.5%	7.53%	33% (Goldman Sachs Commodity Index minus 100 basis points) plus 67% (National Commercial Real Estate Index Fund)
Fixed Income:				
Domestic	16.2%	15.0%	3.31%	Lehman Brothers Aggregate Bond Index
International	4.9%	5.0%	8.70%	Salomon Non-U.S. World Government Bond Index, Unhedged
Total Fixed Income	21.1%	20.0%		
Marketable Alternative Equities	15.7%	10.0%	3.65%	90 Day T-Bills Average Yield + 7%
Total Marketable Securities	88.3%	85.0%	-1.04%	
Non-Marketable Alternative Equities	11.7%	15.0%	-3.84%	Wilshire 5000 U.S. Equities Index + 4%
Total	100.0%	100.0%	-1.42%	

(1) The benchmark return for the endowment neutral policy portfolio is calculated by summing the neutrally weighted index return (% weight for the asset class multiplied by the benchmark return for the asset class) for the various asset classes in the endowment portfolio for the period reported.

III. SHORT INTERMEDIATE TERM FUND (1)

Summary Investment Report at January 31, 2003

($ millions)

	FY01-02	FY02-03		
	Full Year	Two Months Ending October 31, 2002	Three Months Ending January 31, 2003	Year-to-Date
Beginning Net Assets	1,704.6	1,435.9	1,476.3	1,435.9
Net Contributions	(261.0)	45.1	51.6	96.7
Investment Return	60.3	5.4	7.3	12.7
Expenses	(0.7)	(0.1)	(0.1)	(0.2)
Distributions of Income	(67.3)	(10.0)	(15.5)	(25.5)
Ending Net Assets	**1,435.9**	**1,476.3**	**1,519.6**	**1,519.6**
Net Asset Value per Unit	10.099	10.066	10.010	10.010
No. of Units (End of Period)	**142,184,975**	**146,653,309**	**151,802,526**	**151,802,526**
Total Net Investment Return	**3.75%**	**0.36%**	**0.49%**	**0.86%**

(1) Report prepared in accordance with Texas Education Code Sec. 51.0032.

IV. SEPARATELY INVESTED ASSETS

Summary Investment Report at January 31, 2003

($ thousands)

	FUND TYPE													
	CURRENT PURPOSE DESIGNATED		CURRENT PURPOSE RESTRICTED		ENDOWMENT & SIMILAR FUNDS		ANNUITY & LIFE INCOME FUNDS		AGENCY FUNDS		OPERATING FUNDS		TOTAL	
ASSET TYPES														
Cash & Equivalents:	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET	BOOK	MARKET
Beginning value 10/31/02	1,765	1,765	1,306	1,306	15,544	15,544	72	72	82	82	1,259,361	1,259,361	1,278,130	1,278,130
Increase/(Decrease)	(83)	(83)	1,006	1,006	2,348	2,348	134	134	(3)	(3)	516,379	516,379	519,781	519,781
Ending value 1/31/03	1,682	1,682	2,312	2,312	17,892	17,892	206	206	79	79	1,775,740	1,775,740	1,797,911	1,797,911
Debt Securities:														
Beginning value 10/31/02	-	-	263	189	40,314	42,814	14,482	15,227	-	-	251,461	225,222	306,520	283,452
Increase/(Decrease)	-	-	-	3	(1,136)	(1,035)	235	147	-	-	5,823	32,886	4,922	32,001
Ending value 1/31/03	-	-	263	192	39,178	41,779	14,717	15,374	-	-	257,284	258,108	311,442	315,453
Equity Securities:														
Beginning value 10/31/02	40	3,578	1,971	1,632	32,167	31,304	23,376	16,496	-	-	136,619	78,835	194,173	131,845
Increase/(Decrease)	-	933	25	21	5,963	5,434	418	41	-	-	49,164	48,249	55,570	54,678
Ending value 1/31/03	40	4,511	1,996	1,653	38,130	36,738	23,794	16,537	-	-	185,783	127,084	249,743	186,523
Other:														
Beginning value 10/31/02	-	-	-	-	-	-	125	21	-	-	-	-	125	21
Increase/(Decrease)	-	-	-	-	-	-	16	22	-	-	-	-	16	22
Ending value 1/31/03	-	-	-	-	-	-	141	43	-	-	-	-	141	43

Report prepared in accordance with Texas Education Code Sec. 51.0032.
Details of individual assets by account furnished upon request.

UTIMCO 4/4/2003

8. **U. T. System: Proposed Annual Distributions from the Permanent University Fund, Permanent Health Fund, and the Long Term Fund**

RECOMMENDATION

The Chancellor and the Executive Vice Chancellor for Business Affairs concur in the recommendation of The University of Texas Investment Management Company (UTIMCO) and the UTIMCO Board of Directors that:

a. The fiscal year distribution from the Permanent University Fund (PUF) to the Available University Fund (AUF) be decreased by 4.13% from $363,022,043 to $348,033,578 effective September 1, 2003. The distribution is an amount equal to 4.75% of the trailing 12-quarter average of the net asset value of the PUF for the quarter ending February of each fiscal year. The decline in the distribution is a direct result of the decline in the market value of the PUF, as reflected in the trailing 12-quarter average.

b. The distribution rate for the Permanent Health Fund (PHF) remain at its current rate per unit of $0.047.

c. The distribution rate for the U. T. System Long Term Fund (LTF) be increased from $0.258 per unit to $0.2645 per unit effective November 30, 2003.

BACKGROUND INFORMATION

For comparative purposes, the recommended distributions from the PUF, PHF, and LTF represent 5.52%, 5.78%, and 5.78% of the respective funds' market value as of February 28, 2003.

Background information on the PUF: The PUF Investment Policy states that the annual distribution from the PUF to the AUF shall be an amount equal to 4.75% of the trailing 12-quarter average of the net asset value of the Fund for the quarter ending February of each fiscal year. Per this formula, the amount to be distributed from the PUF for FY 2003-2004 is $348,033,578 as calculated below:

Quarter Ended	Net Asset Value
5/31/00	$ 7,910,907,663
8/31/00	8,452,335,867
11/30/00	7,652,556,843
2/28/01	7,686,874,230
5/31/01	7,749,573,154
8/31/01	7,540,148,091
11/30/01	7,079,157,437
2/28/02	7,114,025,229
5/31/02	7,303,322,636
8/31/02	6,738,274,515
11/30/02	6,397,124,818
02/28/03	6,299,971,921
	$ 87,924,272,404
Number of quarters	12
Average Net Asset Value	$ 7,327,022,700
Distribution Percentage	4.75%
FY 2003-04 Distribution	**$ 348,033,578**

Article VII, Section 18 of the Texas Constitution requires that the amount of distributions to the AUF be determined by the U. T. Board of Regents in a manner intended to provide the AUF with a stable and predictable stream of annual distributions and to maintain over time the purchasing power of PUF investments and annual distributions to the AUF. The Constitution further limits the U. T. Board of Regents' discretion to set annual PUF distributions to the satisfaction of three tests:

1. The amount of PUF distributions to the AUF in a fiscal year must be not less than the amount needed to pay the principal and interest due and owing in that fiscal year on PUF bonds and notes. The proposed distribution of $348,033,578 is substantially greater than PUF bonds debt service of $117,145,000 projected for FY 2003-2004.

System	Debt Service
U. T.	$ 93,892,000
TAMU	23,253,000
Total	$ 117,145,000

Sources: U. T. System Office of Finance
Texas A&M University System
Office of Treasury Services

2. The U. T. Board of Regents may not increase annual PUF distributions to the AUF (except as necessary to pay PUF debt service) if the purchasing power of PUF investments for any rolling 10-year period has not been preserved. As the schedule below indicates, the average annual increase in the rate of growth of the value of PUF investments (net of expenses, inflation, and distributions) for the trailing 10-year period ended February 28, 2003, was 1.40%.

Average Annual	Percent
Rate of Total Return	7.70%
Mineral Interest Receipts	1.25%
Expense Rate	(0.08)% (1)
Inflation Rate	(2.46)%
Distribution Rate	(5.01)%
Net Real Return	**1.40%**

(1) Paid from AUF until 1/01/00

3. The annual distribution from the PUF to the AUF during any fiscal year made by the U. T. Board of Regents may not exceed an amount equal to 7% of the average net fair market value of PUF investment assets as determined by the U. T. Board of Regents, except as necessary to pay PUF bonds debt service. The annual distribution rate calculated using the trailing 12-quarter average value of the PUF is within the 7% maximum allowable distribution rate.

Value of PUF Investments (1)	Proposed Distribution	Proposed Distribution as a % of Value of PUF Investments	Maximum Allowed Rate
$7,327,022,700	$348,033,578	**4.75%**	7.00%

(1) Source: UTIMCO

Background information on the PHF and LTF: The spending policy objectives of the PHF and the LTF are to:

1. Provide a predictable stable stream of distributions over time;

2. Ensure that the inflation adjusted value of the distributions is maintained over the long term; and

3. Ensure that the inflation adjusted value of the assets of the PHF and the LTF, as appropriate, after distributions is maintained over the long term.

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

Unless otherwise established by UTIMCO and approved by the U. T. Board of Regents, the spending formula under the PHF Investment Policy and the LTF Investment Policy increases distributions at the rate of inflation subject to a distribution range of 3.5% to 5.5% of the average market value of the PHF assets and LTF assets for each Fund's respective trailing 12 fiscal quarters. The Investment Policies expressly reserve to the U. T. Board of Regents the ability to approve a per unit distribution amount for the PHF and the LTF, as appropriate, that, in the Board's judgment, would be more appropriate than the formula rate calculated by the spending policy provisions.

Because of significant negative returns in the global equity markets during the past three years, the PHF's net asset value of $690.2 million at November 30, 2002, is less than the original PHF contributions of $820.0 million. As a consequence, the recommendation is to depart from the spending formula and not to increase the PHF rate of $0.047 per unit for Fiscal Year 2004. The PHF's average distribution rate calculated using the prior 12-quarter average value of the PHF is 4.8%, within the range of 3.5% to 5.5% set forth in the PHF Investment Policy. The recommended distribution rate of $0.047 per unit was approved by the UTIMCO Board on February 18, 2003.

In addition to the spending policy objectives for the LTF (described above), the LTF Investment Policy expressly recognizes that, under the Uniform Management of Institutional Funds Act, the U. T. Board of Regents may distribute from the LTF the net appreciation, realized and unrealized, in the fair market value of LTF assets over the historic dollar value of the Fund. At November 30, 2002, the net asset value of the LTF was $2,597.6 million and the historic dollar value of the LTF was $1,831.4 million. The 2.5% increase in LTF distribution rate from $0.258 per unit to $0.2645 is recommended based on the investment policy to increase the distribution by the average rate of inflation for the trailing 12 quarters. The consumer price index for the prior three years as of November 30, 2002, was 2.5%. The LTF's average distribution rate calculated using the prior 12-quarter average value of the LTF is 4.50%, within the range of 3.5% to 5.5% set forth in the LTF Investment Policy. The recommended distribution rate of $.2645 per unit was approved by the UTIMCO Board on February 18, 2003.

This item was presented to the Finance and Planning Committee in April 2003.