

**MINUTES OF  
JOINT MEETING OF THE  
POLICY COMMITTEE AND AUDIT AND ETHICS COMMITTEE OF  
THE UNIVERSITY OF TEXAS INVESTMENT MANAGEMENT COMPANY**

The Policy Committee and the Audit and Ethics Committee of The University of Texas Investment Management Company (the "Corporation") convened in a joint open session on **May 16, 2006**, by means of conference telephone enabling all persons participating in the meeting to hear each other, at the offices of the TXU Corporation, 1601 Bryan Street, Dallas, Texas, said meeting having been called by the Committee Chairs, Robert Rowling and Erle Nye, with notice provided to each member in accordance with the Corporation's Bylaws. The audio portion of the meeting was electronically recorded. Participating in the meeting were the following members of the Policy Committee:

Colleen McHugh  
Erle Nye

Also participating in the meeting were the following members of the Audit and Ethics Committee:

Erle Nye, Chairman  
Woody Hunt

Mr. Hunt joined the meeting as a member of the Audit and Ethics Committee at the time noted, at which time a majority and quorum of the Audit and Ethics Committee were present. Policy Committee Chairman Robert Rowling was not present at the meeting. Also attending the meeting were H. Scott Caven, Jr., Chairman of the Board; Bob Boldt, President of the Corporation; Cathy Iberg, Managing Director, Marketable Alternative Investments/Deputy CIO; Christy Wallace, Assistant Secretary of the Corporation; Bill Edwards, Managing Director of Information Technology; Andrea Reed, Risk Manager; Gary Hill, Manager, Investment Reporting; Debbie Childers, Manager, Portfolio Accounting and Operations; Greg Lee, Manager, Finance and Administration; Jerry Turner, legal counsel for the Corporation; Keith Brown of the McCombs School of Business at UT Austin; and Philip Aldridge, Amy Barrett, Barry Burgdorf, Charlie Chaffin and Cathy Swain of UT System Administration.

In the absence of a quorum of the Audit and Ethics Committee, Mr. Nye called the Policy Committee meeting to order at 1:33 p.m. with Mr. Nye and Ms. McHugh constituting a majority and quorum of the Policy Committee. Copies of materials supporting the Policy Committee meeting agenda were previously furnished to each Director.

**Amendments to the Code of Ethics**

Mr. Nye explained that the Code of Ethics ("Code") sets forth the basic principles and guidelines for directors and employees of The University of Texas Investment Management Company ("UTIMCO"). Both the Audit and Ethics Committee and the Policy Committee have responsibilities related to the Code of Ethics. The Audit and Ethics Committee, as mandated by the Audit Charter of the Audit and Ethics Committee, is responsible for reviewing the Code policy annually and recommending any changes to the UTIMCO Board for approval. In addition, the Policy Committee, as mandated by the Policy Committee Charter, is responsible for reviewing proposed amendments to the Code and providing recommendations to the UTIMCO Board with respect to such amendments. Further, the Texas Education Code, Section

66.08, requires, among other things, that the Board of Regents approve the Code. Mr. Nye reported that Code has been rewritten by UT System's Office of General Counsel and reviewed by UTIMCO Staff, Vinson & Elkins and Baker Botts. Section 1.01 of the Code, General Principles, was expanded to conform to the wording that the UTIMCO Board approved in July, 2005 giving a broad general outline of guiding principles. At this point, Mr. Hunt joined the meeting, thereby providing a majority and quorum for the Audit and Ethics Committee; whereupon the Audit and Ethics Committee meeting was convened.

Mr. Nye asked Mr. Turner to present the changes to Section 1.03 and 1.12 of the Code that are being suggested to clarify and explain the definition of "Control" and "Nepotism," respectively. Mr. Nye asked Mr. Burgdorf to explain the suggested addition of Section 2.10 of the code, which contains language relative to referrals to be consistent with the Regents' Rules and Regulations. Mr. Nye asked Mr. Turner to continue by discussing Sections 3.03 and 3.06 of the Code related to private investments. Mr. Turner explained that Section 3.06 has been added to state that a director, director entity, employee, or employee entity may retain a private investment in a business entity in which UTIMCO also has a private investment, provided the director, director entity, employee, or employee entity acquired its private investment prior to the time that the related director or employee assumed a position with UTIMCO. Consistent with Section 3.06, Section 3.02 would allow UTIMCO or a UTIMCO entity to invest in a private entity in which a director, director entity, employee or employee entity owned a private investment acquired prior to the time that the related director or employee assumed a position with UTIMCO. Mr. Nye asked Mr. Boldt for his opinion on new language of Section 3.03. Mr. Boldt said this language is essential to allow appointment of new Board members and employees without penalizing UTIMCO or the new director or employee; provided that in Mr. Boldt's opinion, the director, director entity, employee or employee entity would not be entitled to make any additional private investment in the same private entity in which it was an investor before the related director or employee assumed a position with UTIMCO, they would still be slightly disadvantaged by Section 3.03. Ms. McHugh asked for comments from the UT System. Mr. Burgdorf stated that he approved the language of Section 3.06 and agreed that no divestment should be required under the circumstance described therein. However, Mr. Burgdorf did state his understanding that some members of the Board of Regents and the Chancellor had concerns with the language of Section 3.03. Ms. McHugh asked to defer consideration of the changes to the Code by the Policy Committee to give time for further review. Mr. Nye suggested additional language to Section 3.03 of the Code requiring Board approval of any such investment by UTIMCO or a UTIMCO entity after full disclosure in an open meeting of the relevant facts and a finding by the Board that the investment will not benefit the director, director entity, employee, or employee entity then owning a private investment. After discussion, Mr. Turner and Mr. Burgdorf were asked to provide new language following Mr. Nye's suggestion for review at the next Policy Committee meeting.

### **Approval of the Minutes**

The next matter to come before the Policy Committee was approval of the Policy Committee minutes of the March 7, 2006 meeting. By motion duly made and seconded, the following resolution was unanimously adopted:

RESOLVED, that the minutes of the Meeting of the Policy Committee of the Board of Directors held on March 7, 2006, be, and are hereby, approved.

### **Amendments to the Bylaws**

Mr. Nye asked Mr. Turner to present the proposed amendments to the Corporation's Bylaws. Mr. Turner gave background information on past amendments made to the Texas Education Code, Section 66.08, and noted that some of the recommended changes of the Bylaws proposed by the Staff were to adjust language to agree with these amendments. In addition, minor changes were made to agree with the Code, to reflect an address change, and to include language to be consistent with the Investment Management Services Agreement. Upon motion duly made and seconded, the following resolution was unanimously adopted by the Policy Committee:

RESOLVED, that amendments to the Bylaws of the Corporation as presented be, and are hereby by the Policy Committee, approved, subject to approval by the Corporation's Board of Directors.

At approximately 2:45 p.m., the Policy Committee meeting was recessed.

Whereupon, Chairman Nye announced that a quorum of the Audit and Ethics Committee was still in attendance and that such Committee would continue with its meeting. Copies of materials supporting the Audit and Ethics Committee meeting agenda were previously furnished to each Director.

### **Approval of the Minutes**

The first matter to come before the Audit and Ethics Committee was approval of the Audit and Ethics Committee minutes of the January 16, 2006 meeting. By motion duly made and seconded, the following resolution was unanimously adopted:

RESOLVED, that the minutes of the Meeting of the Audit and Ethics Committee of the Board of Directors held on January 16, 2006, be, and are hereby, approved.

### **Custodian Selection**

Mr. Nye stated that he had been involved with the Custodian Search from beginning to end and noted that the Staff had performed the search using a very thorough and thoughtful process. Mr. Nye stated that he felt confident that the selection recommended by the Staff was the custodian that had the most competent service with the lowest cost. He asked Mr. Hill to review the process with the Audit and Ethics Committee and discuss the reasons for Staff's recommendation to select Mellon Trust as the custodian. After discussion, upon motion duly made and seconded, the following resolution was unanimously adopted:

RESOLVED, that the Audit and Ethics Committee approves the selection of Mellon Trust as the master custodian for the UT System Funds and directs staff to negotiate the contract with Mellon Trust, subject to approval of the UTIMCO Board.

## **Audit Charter of the Audit and Ethics Committee**

Mr. Nye reviewed the background discussions held previously regarding proposed changes to the Audit Charter of the Audit and Ethics Committee. The Audit and Ethics Committee and the Risk Committee held a joint meeting on January 16, 2006, to discuss the oversight responsibility of the committees related to investment compliance, enterprise risk management, and investment risk management. The committees determined that the Risk Committee should be responsible for investment risk management and compliance. However, the Audit and Ethics Committee should still retain responsibility for reporting to the UTIMCO Board that an effective enterprise risk management is in place, which includes investment risk management and compliance. The Audit and Ethics Committee will look to the Risk Committee for assurance regarding investment risk management and compliance. The two committees requested that Staff delineate the responsibilities of the committees and describe the relationship. The Staff's recommendation included language to delineate the responsibilities of the Audit and Ethics Committee and Risk Committee. Upon motion duly made and seconded, the following resolution was unanimously adopted:

RESOLVED, that the revision of the Audit Charter of the Audit and Ethics Committee, be and is hereby approved, in the form submitted to the Audit and Ethics Committee, subject to approval by the Corporation's Board of Directors.

## **Engagement of Independent Auditor**

Mr. Nye stated that the next item for the Committee was to recommend appointment of Ernst & Young to serve as the Corporation's auditor for Fiscal Year 2006. The Staff's recommendation coincides with UT System's selection of Ernst & Young as external auditor for the investment funds. Mr. Boldt and Mr. Chaffin answered questions. Upon motion duly made and seconded, the following resolution was unanimously adopted:

RESOLVED, that the firm of Ernst & Young, LLP be, and is hereby, engaged as the independent auditor of the Corporation for the year ended August 31, 2006, subject to approval by the Corporation's Board of Directors.

## **Financial Statements**

Mr. Nye asked Mr. Hill to present the Unaudited Financial Statements for the six months ended February 28, 2006, for the Permanent University Fund (PUF), General Endowment Fund (GEF), Permanent Health Fund (PHF), Long Term Fund (LTF), Intermediate Term Fund (ITF), and UTIMCO as an information item. Mr. Lee also gave an explanation of a balance sheet change regarding reporting of office lease expense, rebates, and pricing due to advantages offered by the landlord. This and other budget comparison changes will be discussed in more detail during the budget process.

### **Audit and Ethics Committee's Self Assessment**

Mr. Nye asked Mr. Lee to hand out the results of the Audit and Ethics Committee Self Assessment. The Audit Charter of the Audit and Ethics Committee requires the Committee to evaluate its own performance, both of individual members and collectively, on a regular basis. This requirement was added to the charter in May, 2005. This is the first time that the Audit and Ethics Committee will have performed a self-assessment.

The Self-Assessment was mailed to the Audit and Ethics Committee members on Tuesday, May 2nd. The Staff tallied the responses and shared the findings with the Audit and Ethics Committee. Mr. Lee stated that the Staff will also request feedback from the Audit and Ethics Committee members concerning the adequacy of the questionnaire to improve the overall process. Mr. Nye charged the Staff to ask the Audit and Ethics Committee to perform a self-assessment on a regular basis.

### **Report by UT System Internal Audit Office**

Mr. Nye asked Mr. Chaffin of the UT System Internal Audit Office to provide the Audit and Ethics Committee with an update on their annual audit plan, review their report on the Client Participation and Client Management Systems for the Intermediate Term Fund, and discuss their report on the UTIMCO compliance program. Mr. Chaffin updated the Audit and Ethics Committee on the status of their internal audit plan for UTIMCO. In February 2006, the UT System Internal Audit Office conducted a review of the Client Participation and Client Management Systems for the Intermediate Term Fund. Ms. Barrett reviewed their report with the Audit and Ethics Committee. The audit went very well and noted that they suggested continued periodic use of the Denim Group to test for vulnerabilities. The UT System Internal Audit Office also recently conducted an audit of the UTIMCO compliance program (both the institutional compliance processes and the investment compliance processes). Ms. Chaffin and Ms. Barrett presented and discussed their compliance program audit report. The institutional compliance program adheres to the goals and objectives. The investment compliance activities have developed significantly and given the increased complexity of the portfolio and emerging guidance on effective compliance programs, the UT System Internal Audit Office recommended creating a new position for the compliance area. The Audit and Ethics Committee members concurred and noted the importance of having adequate staff to perform compliance processes.

### **Reconvene Joint Meeting**

Mr. Nye reconvened the Joint Meeting of the Policy Committee and the Audit and Ethics Committee at approximately 3:30 p.m., with Mr. Nye, Ms. McHugh and Mr. Hunt constituting a majority and quorum of both Committees for purpose of considering the amendments of the Code. After a full and complete discussion of the proposed amendments to the Code earlier in the meeting, new language regarding the proposed changes to Section 3.03 of the Code, drafted by Mr. Turner and Mr. Burgdorf were presented as follows:

Section 3.03 (1) should read:

(UTIMCO or a UTIMCO entity may not) (1) invest in the private investments of a business entity if a direct

or, director entity, employee, or employee entity then owns a private investment in the same business entity unless:

(A) the director, director entity, employee, or employee entity acquired the private investment before the date on which the related director or employee assumed a position with UTIMCO;

(B) the related director's or employee's private investment does not constitute a pecuniary interest in a business entity as defined by Section 3.01 of this code; and;

(C) the Board approves the investment by UTIMCO or the UTIMCO entity after a full disclosure in an open meeting of the relevant facts and a finding by the Board that the investment will not benefit the director, director entity, employee, or employee entity;

Noting that the Policy Committee will not vote on the proposed amendments to the Code at this meeting, Mr. Nye called for a motion on behalf of the Audit and Ethics Committee. Upon motion duly made and seconded, the following resolution was unanimously adopted by the Audit and Ethics Committee:

RESOLVED, that amendments to the Code of Ethics of the Corporation as presented be, and are hereby, approved by the Audit and Ethics Committee, subject to approval by the Corporation's Board of Directors.

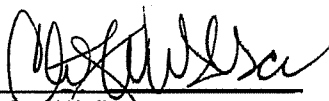
There being no further business to come before the Joint Meeting of the Policy Committee and the Audit and Ethics Committee, the meeting of the Policy Committee was adjourned at approximately 4:20 p.m. At this point, Ms. McHugh left the meeting.


The Audit and Ethics Committee continued in open session with Mr. Nye and Mr. Hunt constituting a majority and quorum of such Committee.

### **Update on Compliance, Reporting and Audit Issues**

Mr. Nye asked Mr. Boldt to present the final item on the agenda, which was an update on Compliance, Reporting and Audit Issues. At a joint meeting of the Risk Committee and Audit and Ethics Committee, members discussed the oversight responsibility of each committee as it related to investment compliance, enterprise risk management, and investment risk management. Based on the meetings, the Risk Charter was amended by the UTIMCO Board and the Audit Charter of the Audit and Ethics Charter has been presented to the Audit and Ethics Committee with proposed amendments. The Audit Charter has proposed language that states "With respect to 1) investment risk management and investment policies, 2) integrity of risk management procedures and controls, 3) integrity of risk models and modeling processes, and 4) liquidity of the PUF, GEF, and ITF, the Audit and Ethics Committee may rely on assurances from the Risk Committee in determining compliance." Mr. Boldt presented one report with color coding to show how the report will be divided into three separate reports. This new reporting will assist the Audit and Ethics Committee in understanding how staff has divided the responsibilities in the Compliance Report.

There being no further business to come before the Audit and Ethics Committee, the meeting was adjourned at approximately 4:25 p.m.

Assistant Secretary:   
Christy Wallace

Approved:   
Erle Nye, Chair

Date: 6-15-06

Audit & Ethics Committee of the Board of Directors of  
The University of Texas Investment Management Company