UNIVERSITY OF MINNESOTA

BOARD OF REGENTS

Finance and Operations Committee

March 10, 2005

A meeting of the Finance and Operations Committee of the Board of Regents was held on Thursday, March 10, 2005, at 9:30 a.m. in the East Committee Room, 600 McNamara Alumni Center.

Regents present: Clyde Allen, Presiding; Anthony Baraga, Dallas Bohnsack, John Frobenius, Steven Hunter, and David Larson.

Staff present: Executive Director Ann Cieslak; Associate Vice Presidents Steve Cawley, Stuart Mason, and Michael Volna.

Student Representatives present: Joshua Jacobsen and Abu Jalal (alternate).

Regent Allen welcomed recently elected Regents Hunter and Larson to the committee.

BOARD OF REGENTS POLICY: *PURCHASING*

Associate Vice President Volna led the discussion on proposed amendments to Board of Regents Policy: *Purchasing*. The proposed new language reflects the revised delegations of authority and current practices and has been structured for clarity and consistency with other Board policies.

Volna reported that the committee reviewed the policy in June 2004, at which time a number of recommendations were made. The policy was redrafted and reviewed by the committee at its February 2005 meeting. Volna referred the committee to the summary of proposed amendments as contained in the docket materials, noting that the new language addresses purchasing activities covered in Board or administrative policies, competitive purchasing, and the institution's commitment to certain core values in the conduct of purchasing activities.

A motion was made and seconded, and the committee voted unanimously to recommend adoption of amendments to Board of Regents Policy: *Purchasing.*

BOARD OF REGENTS POLICY: *ENDOWMENT FUND*

Associate Vice President Mason presented proposed amendments to Board of Regents Policy: *Endowment Fund.* Mason stated that the Office of Asset Management is recommending a reduction in payout rate and an extension in spending policy to improve the strategic positioning of the Consolidated Endowment Fund (CEF). This change in policy will yield increases in annual distribution, albeit at a somewhat slower pace than continuation of current spending levels. The purpose of the changes is to create a stable and growing source of funding to support the University's mission and preserve the inflation-adjusted value of the CEF.

Mason summarized the recommendations, which call for gradually lowering the CEF payout rate from 5% to 4.5% and gradually increasing the number of months in the market value averaging period from 12 quarters to 20 quarters.

The committee engaged in a lengthy discussion. In response to questions, Mason explained that the lower payout rate is not expected to negatively impact the budget or tuition as slightly smaller initial dollars in early years will be followed by larger dollar payouts in later years.

The proposed amendments will return for action at a future meeting of the committee.

RESOLUTION RELATED TO BOARD OF REGENTS POLICY: *ENDOWMENT FUND*

Associate Vice President Mason presented a proposed resolution related to Board of Regents Policy: *Endowment Fund.* The resolution specifies the schedule for distributions, the target distribution rate and schedule of reductions, and the schedule for adjusting the number of month-end market values to be included in the month-end average.

The resolution will return for action at a future meeting of the committee.

ANNUAL INVESTMENT CONSULTANTS REPORT: CAMBRIDGE ASSOCIATES

Associate Vice President Mason introduced Stephen Symchych, Senior Partner at Cambridge Associates, to present the annual report regarding the Consolidated Endowment Fund (CEF) investment performance review and to discuss asset allocation strategies versus peer college and university endowments. A copy of the report is on file in the Board Office.

Symchych reported that in 2004, the University's one-year return on investments was 19.5% compared to a 13.3% return for 135 Cambridge Associates colleges and universities. The three-year return was 8.5% versus 8.4% for the same group. He offered a comparison of asset allocation performance in similarly sized colleges and universities and the fifteen best-performing institutions, noting that the best-performing institutions have more assets to invest and a higher allocation of funds to alternative investments.

Symchych briefly discussed the new asset allocation targets and stated that Cambridge is working with the Office of Asset Management to project long-term returns based on various combinations of asset allocations. The new targets illustrate projected returns with increased allocations in alternative asset classes. The projections show increases in most areas, and Cambridge Associates believes that the return on the CEF will not be lowered materially in any way. The compounded return is expected to increase over time, largely due to reduction in volatility, but Symchych reminded the committee that these are projections, and not absolutes.

CONSENT REPORT

Associate Vice President Volna presented the Consent Report as detailed in the docket materials, including Purchase of Goods and Services over $250,000 to:

- ANDA, Inc. (Andx Corporation) for an estimated $300,000 to purchase generic pharmaceuticals to be stocked in the Boynton Health Service Pharmacy. This is the third year of a three-year contract. The renewal contract period is May 1, 2005 through April 30, 2006.

- Charles River Company for an estimated $1,225,000 for research rodents (mice and rats) as needed for the period January 1, 2005 through June 30, 2008, for the Research Animal Resources department.

- Coca-Cola Company and Coca-Cola Enterprises for an extension to the existing Exclusive Beverage and Sponsorship Agreement for the period July 1, 2006 through June 30, 2008. The value of this contract for the two-year extension is estimated at $5,247,794 (total beverage sales for two years), with an estimated value of $2,992,780 to the University of Minnesota.

- Enventis Telecom for $375,000 to provide annual Cisco Smartnet hardware and software support for the period April 1, 2005 through March 31, 2006, for Networking and Telecommunications Services, a division of the Office of Information Technology.

- FEI Company for $489,200 for one model 200 3D Focused Ion Beam System for the Nanofabrication Center.

- Minneapolis Department of Veterans Affairs Medical Center to increase the contract by $100,804, for a total of $309,013, for services through August 31, 2005 for the Department of Psychiatry.

- Office Max, a Boise Company, for an estimated $956,221 for Hewlett Packard laser toner and ink-jet printer cartridges to be stocked at the University Stores for use in University departments. The renewal contract period is from April 1, 2005 through March 31, 2006.

General Contingency

- Expenditure of $300,000 for Eastcliff Landscape Phase 7a and 7b.

Approval of New Investment Managers

The Office of Asset Management (OAM) proposes engaging two new investment managers to invest target allocations of the Consolidated Endowment Fund. The proposed investments have been reviewed and are recommended by the Investment Advisory Committee and Cambridge Associates.

Fixed Income: CMBS
Fidelity High Yield Real Estate Fund
- $20 million investment
- BBB-BB rated CMBS
- 7% cash yield & 6-year duration as of December 31, 2004
- Target return: 9-11%

International Equity: EAFE Small Cap
Acadian Capital
- $25 million investment
- Developed markets (EAFE) focus, small cap
- Higher returns & lower volatility than EAFE
- Target returns: EAFE + 2-4%

Change in Quasi Endowment F065

The Office of International Programs is requesting approval of a change in purpose of quasi endowment F065 from providing for the benefit of needy Norwegian students to benefiting students from the Nordic countries who wish to study at the University or participate in an approved education abroad program in one of the Nordic countries. The proposed change has been approved by the Office of the General Counsel in accordance with the donor's general intention of supporting student exchanges between the University and the Nordic countries.

A motion was made and seconded, and the committee voted unanimously to recommend approval of the Consent Report.

INFORMATION ITEMS

Associate Vice President Volna referred the committee to information items as detailed in the docket, and including:

- Quarterly Purchasing Report;
- Quarterly Asset Management Report;
- Quarterly Investment Advisory Committee Update;
- Semi-Annual Management Report.

Volna presented the Semi-Annual Management Report, an overview of the institution's unaudited financial statements. Committee members suggested that a report on actual monthly year-to-date expenditures would provide a useful current financial snapshot, even though the budget is prepared annually.

- State of Minnesota Economic Update

Volna reported that the February 2005 forecast anticipates Minnesota's FY2006-07 budget shortfall at $466 million, down from the November 2004 forecasted shortfall of $700 million.

- Semi-Annual Economic Development Report

Regent Allen introduced Craig Taylor, Director of the Office for Business and Community Economic Development. Taylor presented the Semi-Annual Economic Development Report for July-December 2004, a statistical overview of the University's expenditures with small, women, minority, and disabled-owned businesses. He reported that the share of the University's total expenditures with targeted businesses for the 2nd quarter of FY2004 was 3.2%, which is 10% below the previous year's 2nd quarter. The administration is considering strategies to reverse this decline. Committee members requested that any strategy include appropriate benchmarks.

The meeting adjourned at 11:00 a.m.

ANN D. CIESLAK
Executive Director and
Corporate Secretary