

BOARD OF REGENTS  
BANKING COMMITTEE

September 19, 2002

The Banking Committee of the Board of Regents met on Thursday, September 19, 2002, at the University of Iowa, Iowa City, Iowa.

Those present were:

Banking Committee members: Regents David Fisher (chair), Amir Arbisser, Mary Ellen Becker, David Neil, and Owen Newlin.

Others in attendance were:

Institutional representatives: Douglas True, Ann Madden Rice, Carol Senneff, Herb Musser, Cynthia Bartels, Mark Mills, Gregory Geoffroy, Warren Madden, Mark Chidister, Joan Thompson, Brad Dye, Robert Koob, Tom Schellhardt, Gary Shontz, Jim Heuer and Luann Woodward;

Barry Fick, Springsted, Inc.;

Ken Haynie and Ed Bittle, Ahlers law firm;

Mark Brubaker, Wilshire Associates; and

Board Office: Pamela Elliott, Joan Racki, Deb Hendrickson and Barb Briggie.

Regent Fisher called the meeting to order at 7:30 a.m.

**APPROVE MINUTES OF THE JULY 2002 BANKING COMMITTEE MEETING.**

MOTION: Regent Neil moved to approve the minutes of the July 18, 2002, Banking Committee meeting, as written. Regent Becker seconded the motion. MOTION CARRIED UNANIMOUSLY.

**RESOLUTION AUTHORIZING AND PROVIDING FOR THE ISSUANCE OF UNIVERSITY OF IOWA FACILITIES CORPORATION (CARVER BIOMEDICAL RESEARCH FACILITY) REVENUE BONDS, SERIES 2002A AND SERIES 2002B.**

Vice President True stated that the project to be financed by the sale of University of Iowa Facilities Corporation bonds is the Carver Biomedical Research Facility. He said University officials have talked with the Board on six previous occasions regarding the project. The project is an extension of the Medical Education and Biomedical Research Facility and will form the north end of the quadrant in that complex. Of the \$48 million in bonds to be sold for the project, some would be taxable and some would not be taxable. This exciting facility will predominantly be used for research but there will also be facilities for the Dean of Medicine.

Mr. Fick stated that the bonds will be sold in two series. The \$17 million series will be single tax exempt and the \$8 million series will be taxable. He noted that there is strong interest from the underwriting community. Three bidders have signed up for the tax-exempt series and four

bidders have signed up for the taxable series. The bond sales will benefit from the current low interest rate environment and he expects a successful sale.

Mr. Haynie stated that the bond documentation is similar to what was approved in July for the final financing of the Medical Education and Biomedical Research Facility. One difference in the indenture had to do with private use and governmental use of the facility. A second difference is the insurance provision.

Regent Fisher asked if the revenue stream to pay the bonds is from lease rentals from the School of Medicine. Vice President True responded affirmatively, noting that the funds would be from indirect cost recoveries from sponsored research.

Regent Fisher asked if the indirect cost recovery is from research funds to the University. Vice President True responded affirmatively.

Regent Fisher noted that there were no guarantees on those sources of income. Vice President True responded that, while there are no guarantees, University officials have not projected any growth in sponsored research income.

Regent Neil asked if the Regent bond ratings are connected with the State of Iowa bond rating. Mr. Fick responded that the University has its own bond rating. He read the following from a publication of Standard & Poor's which indicated that state support is also a factor in the University's rating:

Other rating factors include the State University of Iowa's:

- Position as the flagship, comprehensive university in Iowa;
- Strong historical levels of state support;
- Sound financial performance at the overall university level, including hospital operations;
- Stable enrollment and demand;
- Relatively broad geographical draw for a public flagship institution, with approximately 37% of the students originating from outside of Iowa; and
- Low debt burden of less than 4%.

Mr. Haynie referred to the sponsored research that will take place in this facility. He stated that, under the Internal Revenue Code, sponsored research is generally considered private use if the sponsor is an agency of the U.S. government or is a private industry. He said much of the financing has to be taxable because the main use of the building is for research. He then described the process for approval of the University of Iowa Facilities Corporation and final approval of the Board of Regents.

Regent Neil asked the reason for the anticipated large number of bidders. Mr. Fick responded that the larger interest in the bonds was due to the continued poor performance of the equities market as well as the strong reputation of Board of Regents bonds. Mr. Haynie said there were also no Board of Regents taxable bonds in the market and the taxable market is a broader market.

MOTION: Regent Neil moved to recommend that the Board adopt A Resolution Authorizing and Approving the Execution and Delivery of the Ground Lease, the Lease, the Indenture, the Bond Purchase Agreement, the Tax Exemption Certificate and the Continuing Disclosure Certificate, and Authorizing and Providing for the Issuance of University of Iowa Facilities Corporation (Roy J. and Lucille A. Carver Biomedical Research Building Project) \$17,000,000 Revenue Bonds, Series 2002A, and \$8,000,000 Revenue Bonds, Series 2002B and Providing for the Payment Thereof. Regent Becker seconded the motion. MOTION CARRIED UNANIMOUSLY.

#### **REVISED BOND ISSUANCE SCHEDULE – OCTOBER AND NOVEMBER 2002.**

Associate Director Racki stated that last November, when the Board adopted the bond issuance schedule for calendar year 2002, staff indicated that the schedule would be continually reviewed and recommendations for changes would be made, if necessary. She said University of Iowa officials have indicated that the Athletics, Parking and Pomerantz Center projects were delayed sufficiently that there was no need to sell bonds this calendar year. With the bond market being in a favorable position, a review was undertaken of refunding opportunities. The revised bond issuance schedule includes refunding of University of Northern Iowa Dormitory Bonds in October and the sale of University of Iowa Hospital Revenue Bonds in November.

MOTION: Regent Arbisser moved to recommend that the Board establish a revised schedule for the issuance of bonds for October and November 2002, as detailed. Regent Neil seconded the motion. MOTION CARRIED UNANIMOUSLY.

#### **PRELIMINARY RESOLUTION FOR THE SALE OF UP TO \$9,800,000 DORMITORY REVENUE REFUNDING BONDS, SERIES UNI 2002.**

Controller Shontz stated that, in 1992, bonds were sold to finance construction of the Residence on the Hill (ROTH) and the bonds that remain have 3.7 percent and 3.0 percent coupon rates. Those bonds can now be called and can be replaced with bonds with lower coupon rates. The replacement bonds would also have less restrictive bond covenants. He said the net present value savings would be 8.4 percent for refunding of three series of bonds.

Mr. Fick stated that the interest rate market is very favorable.

Mr. Bittle stated that removing the old bond covenants will make these bonds a little “cleaner”.

Mr. Haynie pointed out that the bond market index is at a 31-year low.

MOTION: Regent Becker moved to recommend that the Board adopt A Resolution authorizing the Executive Director to fix the date or dates for the sale of up to \$9,800,000 Dormitory Revenue Refunding Bonds, Series U.N.I. 2002. Regent Neil seconded the motion. MOTION CARRIED UNANIMOUSLY.

### **COSTS OF BOND ISSUANCE.**

Associate Director Racki stated that this was a continuing report that is presented to the Banking Committee as final costs of bond issues are received. She referred the members to the location in the meeting materials of the summary of estimated and actual costs.

ACTION: Regent Fisher stated the Banking Committee received the report on the issuance costs related to Academic Building Revenue Refunding Bonds, Series S.U.I 2002 and U.N.I. 2002; Parking System Revenue Bonds, Series I.S.U. 2002; and University of Iowa Facilities Corporation Bonds, Series 2002 (Medical Education and Biomedical Research Facility – Building A), by general consent.

### **QUARTERLY INVESTMENT AND CASH MANAGEMENT REPORT.**

Director Elliott referred to the “implementation issues” section of the materials for this item. She stated that in January 2002, because of the proceeds of the Principal demutualization, the Board’s investment policy was modified and called for additional fund managers. Following an appropriate solicitation and selection process, Barclays Global Investors was selected as the new large index manager. Because of provisions of Iowa law, the institutions were unable to sign the investment agreement with Barclays. She said that, to implement the Board’s investment policy, a new manager will need to be hired.

Regent Fisher recognized Mark Brubaker, Wilshire Associates.

Mr. Brubaker presented an overview of the performance review as prepared by Wilshire Associates. He stated that equity markets had a rough second quarter of 2002. Through the previous day, the S&P was down 23.1 percent for the year. International stocks have underperformed U.S. markets and were down roughly 15-1/2 percent. For the first time, emerging markets outperformed developed markets and U.S. markets. The S&P is down 9 percent/year for the last three years, which coincides with bursting of the technology bubble. He said there has been the most dramatic out-performance of bonds over stocks since 1940. The disparities between large and small cap stocks and growth versus value stocks is driving the U.S. equities market at unprecedented levels.

With regard to fixed income, Mr. Brubaker referred to earlier comments regarding the market for taxable bonds. He said he agreed with the reason given for the expectation of a good response. He then referred to the exhibit which showed international index returns.

President Newlin asked if there are any "Enrons" in Europe or Japan. Mr. Brubaker responded that one of the primary rationales that is argued in avoiding international stocks is lack of consistent accounting standards; there are apples-to-apples comparisons in the U.S. He noted that many overseas investors have been pulling money out of the U.S. equities market, as have many U.S. investors because of recent accounting problems with various companies. He believes there is no longer the feeling that U.S. accounting is far superior to accounting in other countries.

Mr. Brubaker next presented highlights of the endowment performance. He said the slight overweight to U.S. equities for the quarter hurt results. The longer term numbers remain excellent -- 3.3 percent ahead of the index. The performance of the University of Iowa endowment was slightly better than the results of the Iowa State University endowment because of Iowa State University's slightly longer-than-policy allocation to U.S. equities. He said the cash flows in the two endowment funds were another reason for the slight difference in performance between the two endowments.

Wilshire Associates created a new composite of total fund results for the University of Iowa and for the Iowa State University endowment portfolios to coincide with the investment policy change. With regard to the fixed income composite, Mr. Brubaker said the most active fixed income managers attempt to add value by taking prudent credit risk. With regard to the international equities composite, Mr. Brubaker stated that Sanford Bernstein was the top-performing equities manager over the past three years. He said he did not have any concerns with Seneca's short-term numbers.

Regent Fisher asked about the change of indexed manager. Mr. Brubaker said that matter was included in the next agenda item.

**ACTION:** Regent Fisher stated the Banking Committee received the investment and cash management reports for the quarter ended June 30, 2002, by general consent.

#### **SELECTION OF NEW FUND MANAGER.**

Mr. Brubaker stated that at a previous meeting of the Banking Committee, Wilshire Associates recommended hiring Barclays Global Investment as the new large index manager. Wilshire Associates views Barclays as the top indexer in the industry and, through the search process, it was determined that Barclays provided the lowest fee. After beginning the implementation process, outside counsel determined that the investment vehicle Barclays proposed to use was a commingled fund vehicle, which did not comply with the Iowa Code. Much time was spent trying to find an alternative vehicle but none was available with the same fee. A mutual fund investment vehicle was the only option and mutual funds typically involve higher fees. The firm of Vanguard was also interviewed during the selection process but its fees were higher. Subsequent discussions have taken place with Vanguard. Vanguard addressed the competitive

issue by lowering its mutual fund fee to 5 basis points. Therefore, Wilshire Associates recommended utilizing the services of Vanguard.

MOTION: Regent Newlin moved to recommend the Board approve the use of Vanguard, a large capitalization index fund manager, for the Regent endowment funds. Regent Arbisser seconded the motion. MOTION CARRIED UNANIMOUSLY.

Regent Arbisser asked if any of the vehicles just discussed are involved in managing retirement funds for any of the Regent universities. Vice President Madden responded that TIAA-CREF uses a number of fund managers. To the best of his recollection, none of the vehicles used by the Regent universities have been listed on TIAA-CREF's reports.

President Newlin referred to the upper right corner of page 7 of Wilshire's report which was entitled "asset allocation vs. policy", and asked that the totals be included. On page 9 of the report, there was no indication of what was meant by the "\*" in Iowa State University's table of total fund results.

Mr. Brubaker responded that totals would be included in future reports. He said the meaning of the asterisk should have been noted. The asterisk was to indicate that there was a change in benchmarks as of June 30, 2001.

Vice President True noted that the Principal proceeds are also a part of the endowment portfolios. Those proceeds have been in a money market account since December 2001.

Regent Fisher asked if \$30 million in Principal proceeds was transferred to the state. Vice President True responded affirmatively.

#### **MODIFICATION OF INSTITUTIONAL BANKING RELATIONSHIPS.**

Director Elliott stated that the Iowa Code requires that any change in institutional banking relationships be done so by Board of Regents resolution.

Regent Fisher noted that the University of Northern Iowa did not appear to have relationships with any Cedar Falls or Waterloo locally-owned banks. Controller Shontz responded that bids were taken two years ago. Locally-owned banks had an opportunity to present bids.

Regent Fisher asked for the length of the banking contracts. Controller Shontz responded that the contracts are for 5 years.

Regent Fisher suggested that the Regent institutions do business with the local banks as much as possible, providing those banks are competitive and sound.

MOTION: Regent Becker moved to recommend the Board approve the list of financial institutions, subject to the limitations specified as to purpose and maximum amount, as presented. Regent

Neil seconded the motion. MOTION CARRIED  
UNANIMOUSLY.

**MODIFICATION OF INSTITUTIONAL BROKERAGE SERVICES.**

Director Elliott stated that the current list of approved brokers includes 15 brokerage firms. The universities reported name changes to three firms and requested that nine firms be deleted from the list. The revised list would include six brokerage firms.

MOTION: Regent Neil moved to recommend the Board approve the changes to the list of brokers as detailed. Regent Newlin seconded the motion.  
MOTION CARRIED UNANIMOUSLY.

**INTERNAL AUDIT REPORTS – UNIVERSITY OF IOWA.**

Director Elliott stated that this month's report included four original audits and ten follow-up audits. All ten follow-up audits were closed, as noted.

Director Senneff introduced one of the University of Iowa's internal auditors, Herb Musser. She then made brief comments about the internal audit reports. She said four original audits were presented, as listed in the meeting materials. The Intercollegiate Athletics – Home Game Ticket Revenue internal audit is done every year. She said the audit information was included in the materials, and she offered to answer questions. There were none.

ACTION: Regent Fisher stated the Banking Committee, by general consent, (1) received the following four internal audit reports from the University of Iowa: UNIVERSITY OPERATIONS, Intercollegiate Athletics – Home Game Ticket Revenue FY 2001-02, and Internal Controls Relating to Student Activity Fees; HOSPITAL OPERATIONS, Scanned Signatures and UIHC Timekeeping/Payroll and (2) received the report on the status of internal audit follow-up reports, including ten follow-up reports.

**ADJOURNMENT .**

The meeting of the Regents Banking Committee adjourned at 8:23 a.m. on September 19, 2002.

  
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Pamela M. Elliott  
Director, Business and Finance

  
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Gregory S. Nichols  
Executive Director