BOARD OF REGENTS
BANKING COMMITTEE

January 16, 2002

The Banking Committee of the Board of Regents met on Wednesday, January 16, 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:

Regent Sue Nieland;

Institutional representatives: Mary Sue Coleman, Douglas True, Cynthia Bartels, Ann Madden Rice, Carol Senneff, Terry Johnson, Deb Schott, Gregory Geoffroy, Mark Chidister, Margaret Pickett, Joan Thompson, Brad Dye, Robert Koob, Gary Shontz, William Johnson, Jim Heuer, Luann Woodward;

Ken Haynie and Ed Bittle, Ahlers law firm;

Barry Fick, Springsted;

Mark Brubaker and Marc Friedberg, Wilshire Associates;

Board Office: Greg Nichols, Pamela Elliott, Joan Racki, Deb Hendrickson, and Barb Briggle.

Regent Fisher called the meeting to order at 10:08 a.m.

APPROVE MINUTES OF THE NOVEMBER 2001 BANKING COMMITTEE MEETING.

MOTION: Regent Neil moved to approve the minutes of the November 14, 2001, Banking Committee meeting, as written. Regent Becker seconded the motion. MOTION CARRIED UNANIMOUSLY.

ASSET ALLOCATION OF ENDOWMENT FUNDS.

Associate Director Hendrickson reviewed with the Banking Committee members the information that was provided in the meeting materials. She stated that, in November 2001, the Board established an endowment for the expected significant proceeds pursuant to the Principal demutualization. Wilshire Associates reviewed the Board's asset allocation policy and provided the following recommendations:

> Discontinue the use of balanced portfolio management at INVESCO and split the INVESCO accounts into two separate accounts: U.S. equity and U.S. fixed income;
>
> Introduce a new S&P 500 index fund manager;
>
> Introduce a new active small capitalization value manager;
>
> Add Reams Asset Management as a second fixed income manager for the endowment funds; and
>
> Adjust the manager weightings and shorten the rebalancing target ranges as identified below.

Asset Allocation Policy

	Current Range	Proposed Range
Domestic Stocks (US equities)	+/–10%	+/–5%
Domestic Bonds (US fixed income)	+/–10%	+/–5%
International Stocks (foreign equities)	+/–3%	+/–3%

> The Board authorizes institutional officials to maintain the appropriate portfolio asset allocations, and if, at the end of a quarter, rebalancing is required, the institutional officials are to rebalance the portfolio during the following quarter.

Mr. Brubaker stated that the two primary goals of any endowment fund, since it is a perpetual fund, are to maintain the inflation-adjusted assets over time and to maintain real spending levels at current levels. The asset allocation policy is the best tool in managing those goals. He said the receipt of $103 million from Principal will enable the Board to broaden diversification without disrupting the current portfolios. In the last six weeks, the Board's fund managers have reevaluated the Board's asset allocation policy and investment structure. He discussed Wilshire Associates' recommendation to broaden diversification across the market. There was a gap in the small cap value component of the portfolio. Three recommendations were being made with regard to fund manager selection, which he described. He stated that, with the addition of the Principal proceeds, it makes sense to further diversify the portfolio.

Mr. Brubaker proceeded to review Wilshire's report on its asset allocation recommendations. Information discussed included the asset allocation process, current asset allocation policy versus the NACUBO universe, efficient portfolio alternatives, asset allocation recommendations, investment structure recommendations, manager weighting policy recommendations, structure recommendations, and manager recommendations.

Regent Becker referred to the statement in the materials that the funds are not as broadly diversified as most of the universities' peers because the funds do not include less liquid asset classes, such a real estate. She asked if the Banking Committee made the decision not to invest in real estate. President Newlin responded affirmatively. Regent Fisher stated that if Regent Becker ever wished to have further discussion of the matter, it could be included on the Banking Committee's agenda. He noted that the Banking Committee had a lengthy discussion of asset allocation 1-1/2 to 2 years ago.

With regard to efficient portfolio alternatives, Mr. Brubaker stated that the current mix strikes a balance in achieving the Board's goals. He reviewed in detail Wilshire's asset allocation and investment structure recommendation. He noted that Invesco had the freedom to make allocation decisions between stocks and bonds. Wilshire discourages use of that strategy because market timing is difficult to do. He reviewed the investment structure recommendation which included retaining Invesco, but eliminating its ability to make tactical decisions between stocks and bonds. Invesco officials indicated that the change would have no impact on fees.

Regent Fisher discussed the rigorous interview process that was undertaken for selecting the fund managers. He believed that, through that process, very good fund managers were selected. Regent Neil noted that all of the Regent institutions were represented at the meetings where the interviews took place, as was the Board Office.

Mr. Brubaker reviewed Wilshire's recommended manager weighting policy.

Mr. Friedberg presented Wilshire's new manager recommendations. He stated that, as a result of interviews of small cap value managers that were held the previous week, there was a unanimous recommendation to hire LSV Asset Management. The recommendation for the S&P 500 index portion of the portfolio was to hire Barclays Global Investors with Reams as the fixed income manager.

Mr. Friedberg said the LSV Asset Management firm is expected to outperform the market consistently over time.

Mr. Brubaker stated that, of the three small cap value management firms interviewed, LSV Asset Management is the best complement to Seneca, the Board's mid cap growth manager.

Vice President True stated that University of Iowa officials support the recommendation and agree with Wilshire Associates that the University's Quasi I fund be embedded in its endowment fund. He suggested that the motion include approval to merge the Quasi I into the endowment fund.

MOTION: Regent Neil moved to recommend that the Board (1) maintain the current allocation of 63 percent domestic equities, 7 percent international equities, and 30 percent fixed income; (2) add three additional fund managers for the Regent endowment portfolios; (3) adopt the specific investment manager asset allocations, as presented; (4) adopt target ranges, as presented; and (5) merge the University of Iowa Quasi I into the endowment fund. Regent Newlin seconded the motion. MOTION CARRIED UNANIMOUSLY.

SELECTION OF FUND MANAGERS.

MOTION: Regent Becker moved, for the Regent endowment funds, to recommend the Board (1) approve the selection of LSV Asset Management as small capitalization value fund manager; (2) approve the selection of BGI as large capitalization index fund manager; and (3) allow the institutions to utilize Reams Asset Management as a second fixed income fund manager. Regent Neil seconded the motion. MOTION CARRIED UNANIMOUSLY.

RESOLUTIONS FOR THE SALE AND AWARD OF $14,980,000 DORMITORY REVENUE BONDS, SERIES ISU 2002.

Controller Pickett stated that the proposed bond sale was the second bond issue related to Iowa State University's Union Drive Neighborhood. The proceeds would fund construction of the community center.

Mr. Haynie stated that this was the first bond sale for which bids were accepted through PARITY® ("the Internet Bid System"). Two bids were received by that system. He said it was a very interesting process and the system worked great. For this sale, all avenues of submitting bids were accepted. He may recommend utilizing only this procedure for receipt of bids in the future. This process would work great in a refunding because re-offering information would instantly be available.

Regent Fisher asked if an individual with substantial assets could bid on a bond sale through this Internet process. Mr. Haynie responded affirmatively. The individual would have to register with the PARITY system and provide bid security.

Mr. Fick stated that two bids were received that morning for the dormitory bonds for Iowa State University. The first bid was received from a group led by Bank of America Securities for a true interest rate of 5.0098 percent. The second bid was received from a group led by U.S. Bancorp Piper Jaffray for a true interest rate of 4.947 percent. He said the U.S. Bancorp Piper Jaffray bid was one of the more favorable bids he has seen in a while. The bid was approximately 20 basis points below the market. The bid included three term bonds.

Regent Fisher asked if dormitory revenue bonds carry a higher interest rate than do academic building revenue bonds. Mr. Fick responded that dormitory revenue bonds do have a slightly higher rate than academic building revenue bonds because the bond rating is slightly lower. The dormitory bonds have a little longer maturity than most issues of academic building revenue bonds.

MOTION: Regent Newlin moved to recommend that the Board adopt the following resolutions: (1) A Resolution providing for the sale and award of $14,980,000 Dormitory Revenue Bonds, Series I.S.U. 2002, and approving and authorizing the agreement of such sale and award. (2) A Resolution authorizing and providing for the issuance and securing the payment of $14,980,000 Dormitory Revenue Bonds, Series I.S.U. 2002, for the purpose of constructing and equipping a community center and related facilities and making other necessary improvements to existing residence halls and related facilities, all located on the campus of Iowa State University of Science and Technology, including funding the debt service reserve fund and paying costs of issuing the Bonds. Regent Arbisser seconded the motion. MOTION CARRIED UNANIMOUSLY.

PRELIMINARY RESOLUTION FOR THE SALE OF UP TO $15,000,000 UTILITY SYSTEM REVENUE BONDS, SERIES SUI 2002.

Vice President True stated that the proposed utility system bond sale would occur in February. The University of Iowa has a number of projects that would be financed by the sale. The University will also be reimbursed for funds already spent. He noted that the utility system projects were a major undertaking.

Regent Fisher, noting that the utility system is self supporting, asked if the University departments pay the cost to the utility system for their buildings. Vice President True responded affirmatively, noting that each department is billed according to usage.

Regent Fisher asked if student fees are also a revenue stream. Vice President True responded that student fees are not a direct revenue stream. The utility system is supported by charges to users.

Regent Fisher asked for clarification regarding the following statement that was included in the meeting materials:

> Principal on the bonds would be repaid over a period of 20 years, with debt service of approximately $1,183,400 annually to be paid from utility system charges and the proceeds of any utility system student fees which the Board may establish in the future.

Associate Director Racki responded that adding the statement about student fees which the Board may establish in the future was done to improve the bond rating because it improves the security of the bonds. The Board could implement a student fee if the charges to the users of the utility system are insufficient to fund debt service.

President Newlin asked if any of the three universities have ever instituted student fees for the utility system. Representatives of the University of Iowa and Iowa State University responded that had not been done. The University of Northern Iowa does not have a separate utility system.

Regent Neil asked if the projects to be funded from the bond issuance include building a new chiller. Vice President True responded that a portion of the funding from Utility

System Revenue Bonds would be used to connect the arts campus with the current chiller facility ($3.1 million).

Mr. Haynie noted that part of the bond proceeds will reimburse the University for costs already incurred.

MOTION: Regent Neil 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 $15,000,000 Utility System Revenue Bonds (The State University of Iowa), Series S.U.I. 2002. Regent Arbisser seconded the motion. MOTION CARRIED UNANIMOUSLY.

PRELIMINARY RESOLUTION FOR THE SALE OF UP TO $12,900,000 STUDENT UNION BONDS, SERIES UNI 2002.

Controller Shontz stated that the proposal was for a March sale of bonds for the Maucker Union project that has a $13 million project cost.

Regent Arbisser referred to the last time the University of Northern Iowa utilized student fees to support repayment of student union bonds. He asked if the University stopped charging the fees at the conclusion of the project. Controller Shontz responded that the fees were not discontinued but were reprogrammed.

MOTION: Regent Neil 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 $12,900,000 University of Northern Iowa Student Union Revenue Bonds, Series U.N.I. 2002. Regent Arbisser seconded the motion. MOTION CARRIED UNANIMOUSLY.

COST OF BOND ISSUANCE.

Associate Director Racki reported on issuance costs for the October 2001 sale of University of Iowa $13,735,000 Dormitory Revenue Bonds.

Regent Fisher asked that, in the future, the report itemize the actual costs between the Ahlers law firm, Springsted and miscellaneous.

Regent Arbisser noted the report showed that the estimates and costs sometimes varied quite a bit. Mr. Haynie responded that some of the costs are difficult to predict. Charges from the rating agencies are sometimes erratic. It is hard to predict what Moody's and Standard and Poors will charge. The complexity of the financing can affect some of the other costs. He said the prediction of costs is made about one-half way into the bond sale process; therefore, an educated guess is made as to the costs. He noted that when two bond issues are undertaken close together, some efficiencies are attained.

ACTION: Regent Fisher stated the Banking Committee received the report on the issuance costs related to Dormitory Revenue Bonds, Series S.U.I. 2001, by general consent.

EXTERNAL AUDIT REPORT – QUAD-CITIES GRADUATE STUDY CENTER.

Director Elliott presented the report on the FY 2001 financial audit of the Quad-Cities Graduate Study Center. She said there were no reported findings.

ACTION: Regent Fisher stated the Banking Committee received the Quad-Cities Graduate Study Center audit report for the fiscal year ended June 30, 2001, by general consent.

REVENUE BOND FUND AUDIT REPORTS.

Vice President True stated that no findings were reported regarding financial or compliance issues with the revenue bond resolutions.

ACTION: Regent Fisher stated the Banking Committee, by general consent, received the following University of Iowa Revenue Bond Fund audit reports for the fiscal year ended June 30, 2001: 1. Academic Building, 2. Athletics Facilities, 3. Center for University Advancement, 4. Department of Residence, 5. Iowa Memorial Union, 6. Parking System, 7. Recreation Building, 8. Student Health Facility, 9. Telecommunications Facilities and 10. Utility System.

INTERNAL AUDITS REPORT.

Director Elliott stated that there were approximately 13 new audits and 11 follow-up audits. There are very few audits left that need to be closed. She noted that the Board Office had redesigned the report.

Director Senneff introduced Deb Schott of her office. She then presented an overview of the internal audit reports. She said University of Iowa internal auditors have now looked at all of the box offices on campus.

Regent Fisher stated that the University of Iowa had come "light years" in completing outstanding internal audits. He expressed appreciation to Director Senneff for the good work.

Regent Neil asked if an external audit is due from the University of Iowa Hospitals and Clinics. Director Elliott responded affirmatively. She said the Board Office received the report last week, which would be brought to the Board during the next University of Iowa Hospitals and Clinics quarterly report.

ACTION: Regent Fisher stated the Banking Committee, by general consent, (1) received the following thirteen internal audit reports from the University of Iowa: Athletic Ticket Office, Cash Collection Activities, College of Dentistry – Business Office Cash Handling, College of Dentistry – Business System Security & Access, College of Medicine Departmental Audit – Otolaryngology, Conflict of Interest, Hancher Box Office, Human Resources – Family Medical Leave Act, Intercollegiate Athletics – Home Game Ticket Revenue, FY 2000-2001 NCAA Compliance Audit – Student Athlete Employment, NCAA Representative of Athletics Interest (Boosters), Registrars – Audit of In-State Tuition, and Summary of Internal Audit Review Activity for Regent Investment Policy Compliance FY 2000-01; and (2) received the report on the Status of the Internal Audit Follow-up reports, including eleven follow-up reports.

ADJOURNMENT.

The meeting of the Regents Banking Committee adjourned at 11:00 a.m. on January 16, 2002.

Pamela M. Elliott
Director, Business and Finance

Robert J. Barak
Interim Executive Director

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