

Chapter 09 - - Investments and Endowments

09.00 Chapter definitions.

- 09.00.1 "ADV" means the Advisor Registration Form.
- 09.00.2 "CMOs" means collateralized mortgage obligations.
- 09.00.3 "IAC" means the Investment Advisory Committee.
- 09.00.4 "LTIF" means the Long Term Investment Fund.
- 09.00.5 "NAV" means the Net Asset Value.
- 09.00.6 "S&P" means Standard and Poors.
- 09.00.7 "SEC" means the Securities and Exchange Commission.
- 09.00.8 "SITIF" means the Short/Intermediate Term Investment Fund.
- 09.00.9 "UMIFA" means the Uniform Management of Institutional Funds Act.

09.01 **Institutional funds investment.** This policy statement shall guide the investment of the subset of institutional funds, known as the SITIF, of the TTU system. The SITIF is the principal cash fund of the TTU system. Balances in individual accounting funds are to be maintained as cash available for withdrawal without prior notice. All institutional funds not invested in the LTIF in accordance with Section 09.02, *Regents' Rules*, will be invested in accordance with this policy section.

This policy does not preclude the acceptance and retention of securities as gifts to the TTU system. The TTU system shall manage and safeguard such securities in original form, in accordance with the donor's written instructions. Upon the partial or total disposition of the original investment, the proceeds will be invested in accordance with this policy.

- 09.01.1 Investment authority. The *Texas Education Code* provides that the TTU system shall invest all funds in accordance with the prudent person standard. The prudent person standard requires making

investments that prudent investors, exercising reasonable care, skill, and caution, would acquire or retain in light of the purposes, terms, distribution requirements, and other circumstances of the fund then prevailing, taking into consideration the investment of all the assets of the fund rather than a single investment.

09.01.2 Investment objectives.

- a. The investment of funds for the SITIF shall provide incremental return to assist in meeting the operating needs of the TTU system. The investment will be accomplished by having three components of the SITIF:

	<u>Range</u>
(1) Bank deposits and eligible investment pools	25-40%
(2) Fixed income securities	25-40%
(3) Fixed income index mutual fund and government agency securities	30-40%

- b. The investment of funds shall consider asset diversification, total return, suitability, and the experience, quality, and capability of investment personnel. It will be governed by the following investment objectives, in the following order of priority:

- (1) preservation and safety of principal;
- (2) liquidity; and
- (3) yield.

In determining whether the above objective has been met, the following shall be taken into consideration:

- (1) the investment of all funds rather than a consideration as to the prudence of a single investment; and

(2) whether the investment decision was consistent with this written policy.

c. The total return goal of each fixed earnings manager is to exceed the total return of the Lehman Brothers Aggregate Bond Index or the Lehman Brothers Intermediate Government/Corporate Bond Index.

(1) Each fixed earnings manager will be evaluated versus a fixed earnings universe and should rank above the median of that universe over a moving three-year period.

(2) Each fixed earnings manager should maintain a volatility (beta) no greater than 1.20 versus the Lehman Brothers Aggregate Index or the Lehman Brothers Intermediate Government/Corporate Bond Index.

(3) The risk-adjusted performance (alpha) should be positive.

(4) Total return is defined as the sum of earned interest and dividends, realized and unrealized gains or losses, less all investment management costs.

(5) Investment managers will be reviewed on an on-going basis and evaluated based upon the following criteria:

(a) adherence to the philosophy and style that was articulated at, or subsequent to, the time the investment manager was retained; and

(b) continuity of personnel and practices at the firm.

09.01.3 Investment concept. The SITIF shall employ a total return philosophy. Under such a concept, realized gains and losses will be recorded.

09.01.4 Performance goals and objectives. The SITIF will be comprised primarily of collateralized bank accounts, money market mutual funds, eligible fixed income securities, and index mutual funds.

The SITIF's annual performance will be compared to the indices of comparable securities.

- a. The first component, deposits and investment pools, will be evaluated against the 90-day T-Bill.
- b. The fixed income securities component will be evaluated against either the 2-year T-Note or the Lehman Brothers Intermediate Term Government Index, depending upon the types of securities held.
- c. The fixed income mutual index fund component will be compared to the Lehman Brothers Intermediate Term Government Index or its equivalent.

09.01.5 Authorized investment officers. The chief financial officer is the authorized investment officer. At each August meeting, the board will delegate its authority, as necessary, to authorize and approve the sale, purchase, and transfer of stocks, bonds, and other securities that are owned or controlled by the TTU system provided such action is approved by any two of the officers listed below:

- a. chief financial officer;
- b. associate chief financial officer;
- c. assistant vice chancellor for investments; or
- d. chief fiscal officers of the component institutions.

One of the two officers named as follows must approve the sale of all instruments contributed to the TTU system: vice chancellor for institutional advancement; or legal counsel for institutional advancement.

09.01.6 Potential conflicts of interest. An investment officer referenced in Section 09.01.5, *Regents' Rules*, will not be permitted to have a personal business relationship with an entity seeking to sell an investment to the TTU system. An investment officer who is related within the second degree of affinity or third degree

of consanguinity (see the chart in Section 03.01.8, *Regents' Rules*), to an individual seeking to sell an investment to the TTU system shall file a statement disclosing that relationship. A statement required under this section of the policy statement must be filed with the board and the Texas Ethics Commission.

- 09.01.7 Authorized investments. The following are authorized investments:
- a. Obligations of, or guaranteed by, domestic governmental entities:
 - (1) obligations of the United States or its agencies and instrumentalities;
 - (2) CMOs directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States; and
 - (3) other obligations, such as mortgage-backed securities, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, the state of Texas or the United States or their respective agencies and instrumentalities.
 - b. The following are limitations on authorized investments:
 - (1) obligations of the United States or its agencies and instrumentalities:
 - (a) maximum term -- 7 years;
 - (b) maximum single purchase -- without limitation; or
 - (c) maximum aggregate position -- no limit;
 - (2) CMOs directly issued by a federal agency or instrumentality of the United States, the underlying security for

which is guaranteed by an agency or instrumentality of the United States:

- (a) maximum term -- 7 years weighted average life, at time of purchase;
- (b) maximum single purchase -- 3% of portfolio; and
- (c) maximum aggregate position -- not to exceed 75% of portfolio.

The purchase of any security in the CMO category is to be considered on an individual basis with emphasis on credit quality, marketability, liquidity, and legality.

- (3) other obligations, such as mortgage-backed securities, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, the state of Texas or the United States or their respective agencies and instrumentalities:
 - (a) maximum weighted average life -- 7 years, at time of purchase;
 - (b) maximum single purchase -- 3% of portfolio; or
 - (c) maximum aggregate position -- 25% of portfolio.

c. Bank deposits and certificates of deposit:

- (1) Funds shall be deposited into those depositories consistent with Section 07.08, *Regents' Rules*, on Selection of Primary and Secondary Depositories for the TTU system.

On any given day, no depository bank shall have institutional funds on deposit in an amount that exceeds any one of the following limits:

- (a) 25% of the total funds available for investment by the TTU system; or

- (b) based upon the bank's latest regularly published statement of financial condition: 15% of its total deposits; or an amount equal to the sum of its capital, permanent surplus, retained earnings, and reserves.

The above limitations shall not be construed to establish a commitment and/or guarantee on the part of the TTU system to deposit any particular amount in any one bank. The TTU system may develop additional institutional guidelines that may employ other criteria to establish limits on the total amount of deposits in any bank. Such guidelines, however, shall not allow the total deposits in any bank to exceed the limits otherwise established under this policy.

- (2) Certificates of deposit if issued by a state or national bank or a savings and loan association domiciled in the state of Texas shall have the following limitations:
 - (a) maximum term -- 7 years;
 - (b) maximum single purchase -- 3% of portfolio; and
 - (c) maximum aggregate position -- same as bank deposits (see Section 9.01.7.c(1), *Regents' Rules*).
- (3) For both bank deposits and certificates of deposit identified in Section 9.01.7.c.(1)-(2), *Regents' Rules*, the following provisions apply:
 - (a) All cash instruments, including certificates of deposit, must be fully collateralized as required in the *Texas Education Code* and with the Public Funds Investment Act, as amended, except that surety bonds are not authorized as collateral. The pledged collateral shall be placed in a custodian bank or banks named by the TTU system. In no

event will the custodian be affiliated with the depository bank.

- (b) Deposits and certificates of deposits must be guaranteed or insured by the Federal Deposit Insurance Corporation or its successor or be secured by eligible obligations that are described in Section 09.01.7.a., *Regents' Rules*, including mortgage backed securities directly issued by a federal agency or instrumentality that have a market value of not less than the principal amount of the deposits and/or certificates.

- d. For the purpose of this policy, a repurchase agreement is a simultaneous agreement to buy, hold for a specified time, and sell back at a future date obligations described in Section 09.01.7.a., *Regents' Rules*, at a market value at the time the funds are disbursed of not less than the principal amount of the funds disbursed. A fully collateralized repurchase agreement is an authorized investment if the repurchase agreement is secured by obligations described in Section 09.01.7.a., *Regents' Rules*, and requires the securities being purchased to be pledged to the TTU system and deposited at the time the investment is made with a third party selected and approved by the TTU system. Repurchase agreements must be placed through a primary government securities dealer, as defined by the Federal Reserve, or a financial institution doing business in Texas.

Limitations are the same as for bank deposits (see Section 9.01.7.c(1), *Regents' Rules*). Reverse repurchase agreements are not permitted.

- e. A no-load money market mutual fund is an authorized investment if it:
 - (1) is regulated by the SEC; and
 - (2) includes in its investment objective the maintenance of a stable net asset value of \$1 for each share.

- f. Eligible investment pools are authorized investments:
- (1) To be considered an eligible investment pool, the investment pool must furnish an offering circular or other similar disclosure instrument that contains, at a minimum, the following information:
 - (a) the types of investments in which money is allowed to be invested, including the amount and type of investments in foreign securities;
 - (b) the maximum average dollar-weighted maturity allowed, based on the stated maturity date, of the pool;
 - (c) the maximum stated maturity date of any investment security within the portfolio;
 - (d) the objectives of the pool;
 - (e) the size of the pool;
 - (f) the names of the members of the advisory board of the pool and the dates their terms expire;
 - (g) the custodian bank that will safe-keep the pool's assets;
 - (h) whether the intent of the pool is to maintain a net asset value of one dollar and the risk of market price fluctuation;
 - (i) whether the only source of payment is the assets of the pool at market value or whether there is a secondary source of payment, such as insurance or guarantees, and a description of the secondary source of payment;

- (j) the name and address of the independent auditor of the pool;
 - (k) the requirements to be satisfied for the TTU system to deposit funds in and withdraw funds from the pool and any deadlines or other operating policies required for the TTU system to invest funds in and withdraw funds from the pool; and
 - (l) the performance history of the pool, including yield, average dollar-weighted maturities, and expense ratios.
- (2) To maintain eligibility, the investment pool must furnish the following:
- (a) investment transaction confirmations; and
 - (b) a monthly report that contains, at a minimum, the following:
 - i. the types and percentage breakdown of securities in which the pool is invested;
 - ii. the current average dollar-weighted maturity of the pool, based on the stated maturity date;
 - iii. the current percentage of the pool's portfolio in investments that have stated maturities of more than one year;
 - iv. the book value versus the market value of the pool's portfolio, using amortized cost valuation;
 - v. the size of the pool;
 - vi. the number of participants in the pool;

- vii. the custodian bank that is safekeeping the assets of the pool;
 - viii. a listing of daily transaction activity of the TTU system;
 - ix. the yield and expense ratio of the pool;
 - x. the portfolio managers of the pool; and
 - xi. any changes or addenda to the offering circular.
- (c) In addition to the eligibility requirements set forth above, the investment pool must mark its portfolio to market daily and, to the extent reasonably possible, stabilized at a \$1 net asset value. If the ratio of the market value of the portfolio divided by the book value of the portfolio is less than 0.995 or greater than 1.005, portfolio holdings shall be sold by the pool as necessary to maintain the ratio between 0.995 and 1.005. Further, the investment pool must be continuously rated no lower than AAA or AAA-m, or at an equivalent rating by at least one nationally recognized rating service.
- (d) Corporate bonds, debentures, or similar obligations are eligible investments if rated BBB (or equivalent) or above and the weighted average of all corporate bonds does not exceed 4 years.

09.01.8 Securities dealer selection.

- a. The TTU system may rely on the information and advice of securities sales representatives concerning proposed investments, investment timing and pricing. It is essential that the TTU system have sufficient knowledge about the securities firms and personnel with whom they are doing business. Firms that are unwilling to provide complete and timely disclosure of their financial conditions will not be utilized.

- b. The following will be considered in the selection of securities firms:
 - (1) The ability of the securities dealer to fulfill commitments as evidenced by capital strength, liquidity and operating results. This evidence shall be gathered from current financial data, annual reports, credit reports, and other sources of financial information. The securities dealer will exhibit a minimum capital requirement of \$50 million.
 - (2) The dealers' general reputation for financial stability and fair and honest dealings with customers.
 - (3) Information available from state or federal securities regulators and securities industry self-regulatory organizations, such as the National Association of Securities Dealers, concerning any formal enforcement actions against the dealer, its affiliates or associated personnel.
 - (4) A review of the background of the sales representative with whom business will be conducted in order to determine experience and expertise.
- c. A copy of this policy statement is to be provided to all securities dealers seeking to conduct securities transactions with the TTU system.
- d. The TTU system shall make reasonable, good faith efforts to include woman-owned and minority-owned businesses in its investment process. For purposes of this policy, a minority-owned business is a business entity in which 51% of the ownership interests in the entity are held by one or more minority group members, and a woman-owned business is a business entity in which at least 51% of the ownership interests in the entity are held by one or more women.

09.01.9 Investment training. The officers identified in Section 09.01.5, *Regents' Rules*, shall attend at least one training session per year that addresses the responsibilities of the investment officers. The train-

ing should include education in investment controls, security risks, strategy risks, market risks, and compliance with certain state statutes and this policy statement. The chief financial officer shall be notified of the completion of the required training by the investment officers.

09.01.10 Internal management reports. Not less than quarterly, the chief financial officer shall prepare and submit to the chair of the Finance and Administration Committee, the chancellor, and to the presidents of the component institutions a written report of the status of investments.

a. The report shall:

- (1) describe the investment position of the SITIF; and
- (2) contain a summary of:
 - (a) the beginning market value of the reporting period;
 - (b) additions and changes to the market value during the period;
 - (c) ending market value for the period;
 - (d) state the book value and market value of investments at the beginning and the end of the reporting period by type of asset invested;
 - (e) the weighted average maturity of each asset type; and
 - (f) the compliance of the SITIF investments as they relate to this policy statement.

b. The chief financial officer shall, at the beginning of each fiscal year, present a report to the board of the investments of the TTU system during the preceding fiscal year. The report will summarize all investment activity for the year, including total investment income and annual investment rate of return.

09.02 **Endowment and certain long-term institutional funds investment policy.**

09.02.1 Policy statement purpose. This policy statement shall guide the investment of endowment and long-term institutional funds.

09.02.2 Endowment funds investment.

- a. Endowment funds are funds given to the TTU system with a donor-imposed restriction that the corpus is not to be expended but is to be invested for the purpose of producing earnings.

Endowment funds may also include: term endowment funds for which the donor stipulates that the principal may be expended after a stated period or upon the occurrence of a certain event; and funds functioning as endowments (quasi-endowments).

- b. Funds functioning as endowments. The board delegates to the chancellor, or his/her designee, the authority to establish a quasi-endowment fund (a fund functioning as an endowment) when such a fund totals less than \$250,000.

09.02.3 Investment of non-endowment institutional funds in the LTIF. Institutional funds are defined in Section 51.002, *Texas Education Code*, (as amended or modified). Long-term institutional funds are all non-endowment institutional funds approved, for investment purposes, for inclusion in the LTIF.

09.02.4 Fiduciary responsibility. The board recognizes its fiduciary responsibility to comply with the restrictions imposed by the donors of endowment funds. The board acknowledges its legal responsibility to ensure that the management of endowment and other institutional funds is in compliance with state law, including UMIFA (Section 163, *Texas Property Code*, as amended or modified).

09.02.5 Investment philosophy -- management procedures.

- a. No endowment or other institutional fund shall be considered for management under this policy unless it is under the sole

control of the TTU system, with full discretion as to investment of principal and expenditure of spendable earnings. The vice chancellor for institutional advancement shall ensure there are no donor-imposed restrictions preventing the use of the LTIF, including restrictions against both investment in equity securities or corporate debt, and expenditure of net realized appreciation of existing endowment funds. Future donors shall be advised of the investment policy at the times their gifts are made. Funds excluded from consideration from this policy statement will be invested in the SITIF, as authorized by Section 09.01, *Regents' Rules*, or, if instructed by the donor, will be managed and safeguarded in their original form.

- b. The commingled endowment/institutional fund is the LTIF. The LTIF shall be unitized and each new endowment gift added to the fund shall receive units in the fund based upon the market value of the gift and the unit value of the fund at the latest month end preceding the date of receipt of the gift. The unit value of the LTIF shall be determined at least monthly. Earnings determined under the policy statement's spending policy shall be calculated on a unit basis for distribution purposes.
- c. The LTIF may be invested in such securities and investments as permitted by state law. The LTIF may be further limited to such eligible investments as directed by the board (see Section 09.02.11, *Regents' Rules*).
- d. In addition, the LTIF may retain, with the approval of the board, the professional services (investment advisors) deemed appropriate for the management and investment of the fund. All investment managers employed shall be registered under the Investment Act of 1940 and provide the most recent ADV filed with the SEC.

09.02.6 Long-term institutional funds authorized withdrawal. Upon the approval of the chief financial officer and the appropriate chief fiscal officer, long-term institutional funds may be withdrawn from their investment in the LTIF. This withdrawal/reallocation will be

made one year from the date of approval by the chief financial officer. The dollar amount of the withdrawal will equal the number of units withdrawn times the NAV as of the end of the most recent valuation of the LTIF. Because of changes in the NAV from the time of initial deposit, the dollar amount of withdrawal may be more or less than the original investment.

- 09.02.7 Administration and management of the LTIF. The board, IAC, and institutional personnel shall exercise ordinary business care and prudence under the facts and circumstances prevailing at the time of the action or decision. The board, IAC, and institutional personnel shall consider both the long-term and short-term needs of the TTU system in carrying out educational purposes, present and anticipated financial requirements, the expected return on endowment investments, price level trends, and general economic conditions.
- 09.02.8 Financial goal. The financial goal for management of endowment and long-term institutional funds is to preserve the real (i.e., inflation-adjusted) purchasing power of principal and earnings after accounting for endowment spending, inflation, and costs of investment management. Performance of the LTIF against this objective is to be measured over rolling five-year periods.
- 09.02.9 Investment objectives.
- a. The total return goal for the LTIF is to exceed the Consumer Price Index plus 5% and a balanced index that replicates the target asset allocation of the LTIF. These objectives shall be measured over rolling five-year periods.
 - b. The total return goal for each equity manager is to exceed the total return of its respective equity benchmark, such as the S&P 500 Stock Index or the Russell 2000 Index.
 - (1) Each equity investment manager will be evaluated versus an equity investment manager universe and should rank above the median over a moving three-year period of investment managers with a similar investment style

(for example, large cap value, small cap growth, and so forth).

- (2) Each equity investment manager should maintain a volatility (beta) no greater than 1.20 versus its respective equity benchmark.
- (3) The risk-adjusted performance (alpha) should be positive.

09.02.10 Spending policy.

- a. The TTU system recognizes the need for spendable earnings by the beneficiaries of the endowment and long-term institutional funds under its custodianship. The following spending policy reflects an objective to distribute as much total return as is consistent with overall investment objectives defined herein while protecting the inflation-adjusted value of the endowment principal.
- b. The following definitions are used:
 - (1) total return is defined as the sum of total interest and dividends and realized and unrealized gains and losses, less all investment management costs;
 - (2) net current yield is defined as the sum of total interest and dividends earned, less all investment management costs; and
 - (3) spendable earnings is defined as that portion of total return allocated for spending as discussed below.
- c. The distribution of spendable earnings to each unit of the LTIF shall not exceed 6% nor be less than 4% of the average market value of a unit of the LTIF for the 12 quarters just ended. The target annual distribution rate shall be 4.5% of the average unit market value for the 12 quarters just ended. Distribution shall be made quarterly, as soon as practicable after the last calendar day of November, February, May, and August.

- d. The target annual distribution rate shall be reviewed annually with any recommended changes submitted to the board for approval.
- e. If total return since inception of the LTIF, measured at the end of the quarter, does not exceed spendable distributions since inception plus the target distribution for that quarter, the actual distribution shall be limited to the net current yield, not to exceed 4.5%. To minimize the potential effect of year-to-year fluctuations of annual distribution rates, the use of a revenue stabilization reserve may be utilized.

09.02.11 Asset allocation.

- a. To achieve the goal and objectives of the LTIF, the fund's assets may be invested in the categories listed below. The LTIF shall be diversified both by asset class and, within asset classes, by economic sector, industry, and market capitalization (size). The purpose of diversification is to limit the risk associated with any single security or class of securities. The asset allocation of the LTIF shall be structured as follows:

<u>Type of Securities</u>	<u>Range</u>
Equity	30-60%
Domestic Large Cap	10-30%
Domestic Mid Cap	0-10%
Domestic Small Cap.....	0-15%
International.....	10-30%
Real Estate.....	5-15%
Alternative Asset Class.....	15-34%
Hedge Funds.....	10-17%
Private Equity	5-17%
Fixed Earnings	10-30%
Cash	0-10%

- b. The asset allocation shall be monitored on an ongoing basis and rebalanced as needed.
- c. The equity investment component shall include readily marketable, domestic and international common stocks and convertible and preferred stocks. Established equity mutual funds may also be considered in the equity component. The investment purpose for equity securities is to provide high real total rates of return and to provide both long-term capital appreciation and growth in current earnings that exceed the rate of inflation.
- d. Each equity manager should stay fully invested in equities. In general, cash or cash equivalents should not exceed 5% of the market value of each equity portfolio.
- e. Alternative Asset Class. This component of investments will be considered on an individual investment basis. The purpose of this asset class is to provide diversification of the portfolio through high real total rates of return, long-term capital appreciation, and growth in earnings exceeding the rate of inflation at a lower overall risk to the portfolio as a whole. Each investment will be approved by the Board of Regents upon the recommendation of the Investment Advisory Committee. In addition, each investment in this class must have a due diligence report on file prior to the investment.
- f. Real Estate. This component may include both Real Estate Investment Trusts (REITS) and direct investments in real estate. These investments should provide high real total rates of return, long-term capital appreciation, and growth in current earnings that exceed the rate of inflation.
- g. In the event of severe economic/market conditions or strong liquidity needs, the investment managers may elect to establish a portfolio with a significant amount of cash. Any such decision arising from economic/market conditions must be explained in writing to the TTU system within 10 working days.

- h. Not more than 5% of the equity stock of any one corporation may be owned by the LTIF.
- i. At the time of purchase, no more than 10% of each manager's portfolio at market value may be invested in any one security, with the exception of securities issued by the United States government or its agencies.
- j. No more than 25% of the market value of each investment manager's portfolio may be invested in any one industry without prior approval by the board.
- k. Not more than \$500,000 of an investment manager's portfolio may be invested in commercial paper of any one issuer. The credit quality of any commercial paper investment must be A-1/P-1.
- l. Not more than \$100,000 of an investment manager's portfolio may be invested in bank certificates of deposit of any single issuer.
- m. The fixed-earnings investment component shall include marketable domestic and international government/government agency and corporate obligations. The fixed earnings portfolio must have an overall weighted average credit rating of "A" or better by Moody's and/or S & P's rating services. In addition, no more than 10% of the portfolio may be invested in bonds rated below investment grade "BBB/Baa."
- n. Investment grade bonds issued by foreign corporations or governments shall be eligible investments. Not more than 10% of the fixed earnings portfolio shall be invested in foreign securities.
- o. The use of established bond mutual funds may also be considered. The investment purpose for fixed-earnings securities is to provide a hedge against deflation or stock market downturns, to provide a high level of current earnings, to provide a stable source of revenue and to provide diversification of endowment assets.

- p. The manager guidelines, exclusions and prohibited activities stated in Sections 09.02.12 and 09.02.13, *Regents' Rules*, apply to investments in non-mutual and non-pooled funds, where the investment manager is able to construct a separate, discretionary account on behalf of the LTIF. Although policy cannot be dictated to pooled/mutual fund investment managers, the board's intent is to select and retain only pooled/mutual funds with policies that are similar to this policy statement. All managers should achieve the performance objectives of this policy.

09.02.12 Investment manager guidelines.

- a. Each investment manager must satisfy the performance objectives and asset allocation guidelines.
- b. Each investment manager shall have the full investment discretion with regard to market timing and security selection, consistent with this policy.
- c. Each investment manager shall handle the voting of proxies and tendering of shares in a manner that is in the best interest of the LTIF and consistent with the investment objectives contained herein.
- d. All purchases and sales transactions shall be conducted to obtain the best net execution.
- e. Specific guidelines may be established with each individual outside equity investment manager.

09.02.13 Exclusions and prohibited activities.

- a. In addition to the limitations discussed above, the following activities are not authorized by the board:
 - (1) Domestic Equity Managers;
 - (2) the purchase of unregistered or restricted stock; and

- (3) activities that are prohibited by limitations imposed by state law.

09.02.14 Investment managers.

- a. The LTIF will be managed primarily by external investment management organizations. Each manager will be provided with a copy of this policy statement. Investment managers will be delegated with the discretion to manage the assigned assets to best achieve the goal and objectives of the LTIF. In addition, the manager will be informed of the expected spending pay-outs necessary for distribution to endowment recipients and the comparative benchmarks that will be used to evaluate performance.
- b. The selection of investment managers shall be approved by the board.
- c. Investment managers, members of the IAC, and advisors will disclose any relationship that might diminish the advisors' or managers' independence of judgment in their performance of the responsibilities to the university, utilizing the following Codes of Standards:
 - (1) Disclosure of conflicts. Managers, advisors, members of the IAC, and potential managers must make full and fair disclosure of all matters that could reasonably be expected to impair their independence and objectivity or interfere with their respective duties to the TTU system;
 - (2) Managers, advisors, members of the IAC, and potential managers must, on an annual basis, ensure that such disclosures are prominently set forth, are delivered in plain language, and communicate the relevant information effectively using the Texas State Auditor's Office Uniform Disclosure Form; and

- (3) Managers, advisors, members of the IAC, and potential managers will abide by the standards of conduct contained in Section 09.02.15, *Regents' Rules*.

09.02.15 Standards of conduct for investment managers and advisors.

- a. Code of Ethics. Investment managers and advisors employed by the TTU system shall:
 - (1) Act with integrity, competence, diligence, respect, and in an ethical manner with the public, clients, prospective clients, employers, employees, and colleagues in the investment profession and other participants in the global capital markets;
 - (2) Place the interest of clients, the interest of their employer, and the integrity of the investment profession above their own personal interest;
 - (3) Use reasonable care and exercise independent professional judgment when conducting investment analysis, making investment recommendations, taking investment actions, or engaging in other professional activities;
 - (4) Practice, and encourage others to practice, in a professional and ethical manner that will reflect credit on themselves and the profession;
 - (5) Promote the integrity of and uphold the rules governing global capital markets; and
 - (6) Maintain and improve their professional competence.
- b. Standards of professional conduct:
 - (1) Knowledge of the law. Investment managers and advisors must understand and comply with all applicable laws, rules, and regulations of any government agency, regulatory organization, licensing agency, or professional association governing their professional activities.

Investment managers and advisors must not knowingly participate or assist in any violation of such laws, rules, or regulations.

- (2) Independence and objectivity. Investment managers and advisors must use reasonable care and judgment to achieve and maintain independence and objectivity in their professional activities. Investment managers and advisors must not offer, solicit, or accept and gift, benefit, compensation, or consideration that could be reasonably expected to compromise their own or another's independence and objectivity.
 - (3) Misrepresentation. Investment managers and advisors must not knowingly make any statement that misrepresents facts relating to investment analysis, recommendations, actions, or other professional activities.
 - (4) Misconduct. Investment managers and advisors must not engage in any conduct involving dishonesty, fraud, deceit, or commit any act that reflects adversely on their integrity, trustworthiness, or professional competence.
- c. Investment analysis and recommendation. Investment managers and advisors shall:
- (1) Exercise diligence, independence, and thoroughness in conducting investment analysis, making investment recommendations, and taking investment actions; and
 - (2) Have a reasonable and adequate basis, supported by appropriate research and investigation, for any investment analysis, recommendation, and action.
- d. Disclosure and conflicts of interest:
- (1) Managers, advisors, and potential managers must make full and fair disclosure of all matters that could reasonably be expected to impair their independence and objec-

tivity or interfere with their respective duties to the Texas Tech University System; and

(2) Managers, advisors, and potential managers are investing public funds and are subject to the Texas Open Records Act.

e. The above standards of conduct are derived from the Association for Investment Management and Research code of ethics and standards of professional conduct.

09.02.16 Conflict of interest on investments; restrictions on investments.

The TTU system will not invest in any investment that creates a perceived conflict of interest between the investment and a member of the board, a member of the IAC, or an employee of the TTU system. A perceived conflict of interest exists when any of the following outside activities exist for either the member or TTUS employee, or members of their immediate family, with regards to the firm or partnership by:

- a. Investing in the firm or partnership where there exists a significant financial interest, as defined either by holding 5% or more of the stock, assets or other interests, or by investing 10% or more of the member's or TTUS employee's net assets;
- b. Acting as an employee, officer, director, partner, consultant, representative, agent, auditor, or advisor; or
- c. Engaging in any activity that could create the appearance of a conflict of interest, and thereby impair the reputation of the TTU system for impartiality and fair dealing.

As used herein, a member's or TTUS employee's "immediate family" includes any child, stepchild, parent, stepparent, spouse, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, sister-in-law and any other person sharing the household of a member or TTUS employee (other than a tenant or employee of the member or TTUS employee).

Such restrictions on investments shall continue to apply for one year after the departure of a member of the board, a member of the IAC, or a TTUS employee from that person's office or position with the TTU system.

In no case shall the TTU system invest in any private entity in which a member of the IAC has any pecuniary interest.

09.02.17 Communications and reporting. The investment managers are responsible for frequent and open communication to the TTU system administration on all significant matters pertaining to the investment policies and the management of the LTIF assets. These reporting responsibilities include:

- a. communicating major changes in the investment managers' investment outlook, strategy, and portfolio structure;
- b. communicating significant changes in the ownership, organizational structure, financial condition, or personnel staffing;
- c. communicating, on a monthly basis, all investment activities during the preceding month – providing valuation reports of the month end portfolio holdings;
- d. communicating, on a quarterly basis, the performance of investment managers' activities;
- e. meeting at least semi-annually, to discuss the managers' performance, investment outlook, investment strategy and portfolio re-balancing strategies; and
- f. presenting at the beginning of each fiscal year, a report of the LTIF's investment activities for the preceding year together with a summary of each investment manager's performance.

09.02.18 Internal management reports. Not less than quarterly, the chief financial officer shall submit to the chair of the Finance and Administration Committee, the chancellor, and the presidents of the component institutions a written report of the status of the investments portfolio. The report shall:

- a. Provide an inventory of the investments of the LTIF; and
- b. Contain a summary of:
 - (1) asset balances, at book value, by asset class;
 - (2) asset balances, at market value, by asset class;
 - (3) performance measures;
 - (4) benchmarks; and
 - (5) beginning and ending market values for the quarter, with additions and changes.

09.02.19 Management fee.

- a. The TTU system will assess and retain an investment management fee at the annual rate of up to 0.5% of the average market value of the LTIF. The fee shall be calculated in the same manner as spendable income and will be recorded quarterly.
- b. The fee shall be used to offset the costs of managing long-term investments and to offset a portion of the costs of fundraising.
- c. The management fee rate shall be reviewed annually with any recommended changes submitted to the board for approval.

09.03 **Mineral leases.** It is the intent of the board to lease oil, gas, sulfur, ore, water, and other mineral interests of the TTU system for development whenever there is a demand that will reasonably ensure that they may be leased advantageously and it is in the best interest of the TTU system. All leases will be executed in accordance with the applicable laws and with rules and regulations adopted by the board that are not inconsistent with the provisions of law. The reason for leasing minerals is to obtain additional income to be used by the board for the administration of the TTU system, for payment of principal of and interest on revenue bonds and notes issued by the board, and for

any other purpose that in the judgment of the board may be for the good of the TTU system.

09.03.1 Lands under exclusive control of the board and owned by the state of Texas.

- a. Leases will be negotiated with prospective lessees to obtain their best offer above the minimum outlined in Section 09.03.1.c, *Regents' Rules*.
- b. Leases normally will be for oil and gas production only. Separate leases will be required for other mineral production, whether strip-mined or not.
- c. The board may not sell a lease for less than the royalty and rental terms demanded at that time by the General Land Office of the State of Texas in connection with the sale of oil, gas, and other mineral leases of the public lands of this state. In addition, no bid or proposal shall be accepted that offers a royalty of less than one-quarter of production, a primary term greater than five years or a delay rental of less than \$5 per acre per year.
- d. No state lands shall be sold unless the mineral rights are retained by the state, unless impractical.
- e. Use of TTU system standardized oil and gas lease or oil and gas and mineral lease forms will be required for all leases.
- f. Use of TTU system standardized division order forms will be required for all division orders.

09.03.2 Mineral and royalty interests derived from trusts and gifts.

- a. Leases will be negotiated with prospective lessees to obtain their best offer above the minimums outlined in Section 09.03.2.c, *Regents' Rules*.

- b. Leases will normally be for oil and gas production only. Separate leases will be required for other mineral production, whether strip-mined or not.
- c. No proposal shall be accepted that offers a royalty of less than one-quarter of production, a primary term of more than five years or a delay rental of less than \$5 per year per mineral acre, beginning with the second year of the lease.
- d. Use of TTU system standardized oil and gas lease or oil and gas and mineral lease forms will be required for all leases.
- e. Use of TTU system standardized division order forms will be required for all division orders.

09.03.3 Approval. All leases and other documents relating to leasing will be approved by the Finance and Administration Committee, by the board as a ratification item, and signed by the chancellor.