

Financial Statements  
and Independent Auditors' Report  
The University of Texas System  
Long Term Fund  
*Years Ended August 31, 2012 and 2011*

# The University of Texas System Long Term Fund

## Financial Statements

Years Ended August 31, 2012 and 2011

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## INDEPENDENT AUDITORS' REPORT

The Board of Regents of The University of Texas System  
The Board of Directors of The University of Texas Investment Management Company

We have audited the accompanying Statements of Fiduciary Net Assets of The University of Texas System Long Term Fund (the "Fund"), as of August 31, 2012 and August 31, 2011, and the related Statements of Changes in Fiduciary Net Assets for the years then ended. These financial statements are the responsibility of The University of Texas Investment Management Company ("UTIMCO" or "management"). Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing the audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements of the Fund are intended only to present the financial position of the Fund as of August 31, 2012 and August 31, 2011, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States and do not purport to, and do not, present the financial position of UTIMCO or The University of Texas System as of August 31, 2012 or August 31, 2011, or the changes in its financial position for the years then ended.

As discussed in Note 3, the financial statements include an investment in The University of Texas System General Endowment Fund (the "GEF"), valued at \$6,128,367,681 and \$6,056,577,496 as of August 31, 2012 and August 31, 2011, respectively. The GEF has 69.4% and 68.3% of its net assets as of August 31, 2012 and August 31, 2011, respectively, invested in assets whose fair value has been estimated by management in the absence of readily determinable fair values. Management's estimate of the value of the Fund is based on the net asset value per unit of GEF, which is also calculated by UTIMCO.

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Fund as of August 31, 2012 and August 31, 2011, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Management's discussion and analysis on pages 3 through 6 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental schedule referred to in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements. This supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the audit procedures applied in our audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, such information is fairly stated in all material respects in relation to the financial statements taken as a whole.

*Deloitte & Touche LLP*

October 31, 2012

## **MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A) (Unaudited)**

Our discussion and analysis of The University of Texas System Long Term Fund's (Fund) financial performance provides an overview of its activities for the year ended August 31, 2012. This discussion was prepared by The University of Texas Investment Management Company (UTIMCO) and should be read in conjunction with the Fund's financial statements and notes. The Fund was established February 9, 1995, by The University of Texas System Board of Regents (UT Board) to succeed the Common Trust Fund pooled investment fund. The Fund is a pooled investment fund established for the collective investment of approximately 10,335 privately raised endowments and other long-term funds established to benefit the 15 institutions of the UT System. The Texas Constitution and various state statutes designate the UT Board as the fiduciary for the management of certain public endowment and operating funds. The UT Board has entered into an Investment Management Services Agreement delegating investment management responsibility for all investments to UTIMCO.

On March 1, 2001, the Fund purchased units in the General Endowment Fund (GEF) in exchange for the contribution of its investment assets. The GEF, established by the UT Board effective March 1, 2001, is a pooled fund for the collective investment of long-term funds under the control and management of the UT Board. The GEF has only two participants: the Fund and the Permanent Health Fund (PHF), which was also established by the UT Board. The GEF is organized as a pooled investment fund in which the Fund and the PHF purchase and redeem units quarterly. The GEF is under the fiduciary responsibility of the UT Board and is provided day-to-day operations by UTIMCO.

The purpose of the MD&A is to provide an objective and easily readable analysis of the Fund's financial statements based upon currently known facts, decisions and conditions.

### **Financial Highlights**

- The Fund's net fiduciary assets, after contributions, withdrawals and distributions, increased by \$71.8 million from \$6,056.6 million to \$6,128.4 million or approximately 1.2% for the year ended August 31, 2012, compared to an increase of \$926.3 million from \$5,130.3 million to \$6,056.6 million or approximately 18.1% for the year ended August 31, 2011. The change in net fiduciary assets from year to year is mainly attributable to the following:
  1. The Fund posted a net investment gain of 3.13% for the year ended August 31, 2012, calculated using the Modified Dietz Method as described by the CFA Institute. The net investment return of the Fund is dependent on the results of the investments held in the GEF. The GEF's investments in developed country equities, credit-related fixed income and real estate were the biggest contributors to the 2012 return. Investments in natural resources, developed country equities and credit-related fixed income were the biggest contributors to the net investment gain of 14.77% for August 31, 2011.
  2. Participant contributions to the Fund decreased by 53.4% from fiscal year 2011 to 2012. Fiscal year 2012 contributions of \$211.4 million represented 3.5% of the

## THE UNIVERSITY OF TEXAS SYSTEM LONG TERM FUND

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average value of the Fund assets during the year. From fiscal year 2010 to 2011, participant contributions to the Fund increased by 50.7%. Contributions for fiscal year 2011 totaled \$453.5 million and represented 7.8% of the average value of the Fund assets during the year. Participant contributions consist of endowment and other long-term funds that have been forwarded to the Fund for management by UTIMCO.

3. The Fund's distribution rate per unit was increased by 1.4%, approximately the three-year average rate of inflation, for the year ended August 31, 2012. This equated to an increase in the 2012 rate to \$.3215 per unit from the 2011 rate of \$.3172 per unit. The 2011 rate represented an increase of 2.4% over the fiscal year 2010 rate of \$.3098 per unit. Fiscal year 2012 distributions represented 4.96% of the Fund's average net asset value during the year, compared to the fiscal year 2011 distributions which represented 4.87% of the Fund's average net asset value for the year.

### **Use of Financial Statements and Notes**

The Fund's financial statements were prepared in accordance with standards issued by the Governmental Accounting Standards Board (GASB). Two financial statements are required under GASB: the statement of fiduciary net assets and the statement of changes in fiduciary net assets.

The notes to the financial statements contain supplemental information that is essential for the fair presentation of the financial statements.

### **Statements of Fiduciary Net Assets**

The statements of fiduciary net assets present assets, liabilities, and net assets of the Fund as of the end of the fiscal year. These statements, along with all of the Fund's financial statements, are prepared using the accrual basis of accounting, whereby Fund investment income is recognized when earned and Fund expenses are recognized when incurred.

Since the Fund invests in only GEF units and a negligible amount of cash, the majority of the Fund's net assets represent investment in GEF units.

As of August 31, 2012, the Fund owned 30,233,803 GEF units representing an ownership percentage of 86.26%, compared to 30,840,825 GEF units representing an ownership percentage of 85.92% as of August 31, 2011. As of August 31, 2012 and 2011, the fair value of the GEF units was \$6,128.4 million and \$6,056.6 million, respectively.

The GEF invests in a broad mix of investments and is actively managed to its benchmark, the Endowment Policy Portfolio. The Endowment Policy Portfolio is the index or benchmark for the endowment funds that UTIMCO manages. The return of the Endowment Policy Portfolio is the sum of the weighted benchmark returns for each asset class. UTIMCO allocates GEF's assets to internally and externally managed portfolios in accordance with approved asset allocation policies, and attempts to supplement the original endowment corpus by increasing purchasing power over time. In doing so, UTIMCO increases the endowment resources available to fund the teaching, research, and health care programs specified by the various donors.

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The following table summarizes the statements of fiduciary net assets (in millions):

	<b>2012</b>	<b>2011</b>	<b>2010</b>
<b>Assets</b>			
GEF Units, at Fair Value	\$ 6,128.4	\$ 6,056.6	\$ 5,130.3
Receivable for GEF Units Sold	11.9	4.6	6.7
<b>Total Assets</b>	<b>6,140.3</b>	<b>6,061.2</b>	<b>5,137.0</b>
<b>Liabilities</b>			
Payable to Participants	11.9	4.6	6.7
<b>Total Liabilities</b>	<b>11.9</b>	<b>4.6</b>	<b>6.7</b>
<b>Net Assets Held in Trust</b>	<b>\$ 6,128.4</b>	<b>\$ 6,056.6</b>	<b>\$ 5,130.3</b>

**Statements of Changes in Fiduciary Net Assets**

Changes in fiduciary net assets as presented on the statements of changes in fiduciary net assets are based on activity of the Fund. The purpose of these statements is to present additions to the Fund resulting from net investment income and participant contributions and to present deductions from the Fund resulting from administrative and investment expenses and participant distributions.

The net increase in investments of the Fund was \$148.0 million during the year compared to the net increase in investments of \$733.9 million for the year ended August 31, 2011. The Fund's investment expenses totaled \$5.3 million, \$4.9 million and \$3.1 million, respectively, for the years ended August 31, 2012, 2011, and 2010.

Distributions to participants totaled \$297.8 million, \$282.1 million and \$253.4 million, respectively, for the years ended August 31, 2012, 2011, and 2010. The increase in distributions is a result of the UT Board increasing the distribution rate from \$0.3172 per unit to \$0.3215 per unit for fiscal year 2012, and additional contributions into the Fund. The increase for fiscal year 2011 is a result of the UT Board's increase of the distribution rate from \$0.3098 per unit to \$0.3172 per unit, and additional contributions to the Fund. The Fund is structured as a pooled investment fund in which each endowment or account purchases units at the Fund's fair value or net asset value per unit. Cash distributions are paid quarterly, on a per unit basis, directly to the UT System institution of record.

The Fund's objectives are:

- Provide for current beneficiaries by increasing the annual distribution rate at least equal to the rate of inflation so that real purchasing power is maintained, and
- Provide for future beneficiaries by increasing the market value of endowment funds after the annual distribution at a rate at least equal to the rate of inflation so that future distributions maintain purchasing power as well.

Fund distributions are controlled by a spending policy approved by the UT Board. The key to preservation of endowment purchasing power over the long-term is control of spending through a

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target distribution rate. This target rate should not exceed the endowment's average annual investment return after fund expenses and inflation. The Fund distributions are increased annually at the three year average rate of inflation provided that the distribution rate remains within a range of 3.5% to 5.5% of the Fund's net asset value. As reported on the financial highlights statement in the supplemental schedules, the ratio of distributions to average net assets (12-quarter average) has remained between 3.5% to 5.5%.

The following table summarizes the statements of changes in fiduciary net assets (in millions):

	<b>2012</b>	<b>2011</b>	<b>2010</b>
Investment Income	\$ 192.6	\$ 787.1	\$ 591.8
Less Investment Expenses	(5.3)	(4.8)	(3.1)
Net Investment Income	187.3	782.3	588.7
Participant Contributions	211.4	453.5	301.0
Total Additions	398.7	1,235.8	889.7
Administrative Expenses	12.6	12.2	12.4
Participant Withdrawals	16.5	15.2	10.4
Participant Distributions	297.8	282.1	253.4
Total Deductions	326.9	309.5	276.2
Change in Fiduciary Net Assets	71.8	926.3	613.5
Net Assets Held in Trust, Beginning of Year	6,056.6	5,130.3	4,516.8
Net Assets Held in Trust, End of Year	\$ 6,128.4	\$ 6,056.6	\$ 5,130.3

**Contacting UTIMCO**

The above financial highlights are designed to provide a general overview of the Fund's investment results and insight into the following financial statements. Additional information may be found on our website and inquiries may be directed to UTIMCO via [www.utimco.org](http://www.utimco.org).



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**Statements of Fiduciary Net Assets**

*August 31, 2012 and 2011*

*(Dollars in thousands, except per unit amounts)*

	<u>2012</u>	<u>2011</u>
<b>Assets</b>		
GEF Units, at Fair Value	\$ 6,128,367	\$ 6,056,577
Receivable for GEF Units Sold	11,874	4,647
Other	<u>9</u>	<u>1</u>
<b>Total Assets</b>	<u>6,140,250</u>	<u>6,061,225</u>
<b>Liabilities</b>		
Payable to Participants	<u>11,874</u>	<u>4,647</u>
<b>Total Liabilities</b>	<u>11,874</u>	<u>4,647</u>
<b>Net Assets Held in Trust</b> (937,912,196 Units and 907,954,363 Units, respectively)	<u>\$ 6,128,376</u>	<u>\$ 6,056,578</u>
<b>Net Asset Value Held in Trust Per Unit</b>	<u>\$6.534</u>	<u>\$6.671</u>

*The accompanying notes are an integral  
part of these financial statements.*

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**Statements of Changes in Fiduciary Net Assets**

*Years Ended August 31, 2012 and 2011*

*(in thousands)*

	<u>2012</u>	<u>2011</u>
<b>Additions</b>		
Investment Income:		
Net Increase in Investments	\$ 148,034	\$ 733,906
Allocation of GEF Net Investment Income	44,559	53,226
Other Income	-	1
Total Investment Income	<u>192,593</u>	<u>787,133</u>
Less Investment Expenses:		
UTIMCO Management Fee	5,275	4,821
Other Expenses	20	33
Total Investment Expenses	<u>5,295</u>	<u>4,854</u>
Net Investment Income	187,298	782,279
Participant Contributions	<u>211,365</u>	<u>453,490</u>
<b>Total Additions</b>	<u>398,663</u>	<u>1,235,769</u>
<b>Deductions</b>		
Administrative Expenses:		
Fee for Endowment Administration and Management	12,502	12,074
Fee for UT System Oversight	98	122
Total Administrative Expenses	<u>12,600</u>	<u>12,196</u>
Participant Withdrawals	16,416	15,177
Participant Distributions	<u>297,849</u>	<u>282,094</u>
<b>Total Deductions</b>	<u>326,865</u>	<u>309,467</u>
<b>Change in Fiduciary Net Assets</b>	71,798	926,302
Net Assets Held in Trust, Beginning of Year	<u>6,056,578</u>	<u>5,130,276</u>
<b>Net Assets Held in Trust, End of Year</b>	<u>\$ 6,128,376</u>	<u>\$ 6,056,578</u>

*The accompanying notes are an integral  
part of these financial statements.*

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## LONG TERM FUND

*Notes to Financial Statements*

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### **Note 1 – Organization and Basis of Presentation**

The University of Texas System Long Term Fund (Fund) is a pooled fund established for the collective investment of private endowments and other long-term funds supporting various programs and purposes of the 15 institutions comprising The University of Texas System (UT System). The Fund was formerly known as the Common Trust Fund. The Long Term Fund was established February 9, 1995, by the Board of Regents of The University of Texas System (UT Board) to succeed the Common Trust Fund pooled investment fund. Fiduciary responsibility for the Fund rests with the UT Board. The day-to-day operational responsibilities of the Fund are delegated to The University of Texas Investment Management Company (UTIMCO), pursuant to an Investment Management Services Agreement with the UT Board.

On March 1, 2001, the Fund purchased units in the General Endowment Fund (GEF) in exchange for the contribution of its investment assets. The GEF, established by the UT Board effective March 1, 2001, is a pooled fund for the collective investment of long-term funds under the control and management of the UT Board. The performance of the Fund is significantly impacted by the performance of the GEF. The GEF has only two participants: the Fund and the Permanent Health Fund (PHF) which was also established by the UT Board. The GEF is organized as a pooled investment fund in which the Fund and the PHF purchase and redeem units quarterly. The GEF is under the fiduciary responsibility of the UT Board and is provided day-to-day operations by UTIMCO.

The activities of the Fund are accounted for as a fiduciary fund. The financial statements of the Fund use an economic resources measurement focus and the accrual basis of accounting, whereby revenues are recorded when earned and expenses are recorded when a liability is incurred regardless of the timing of cash flows. The financial statements of the Fund are prepared in accordance with the requirements of the Governmental Accounting Standards Board (GASB).

The annual combined financial statements of UT System are prepared in accordance with the Texas Comptroller of Public Accounts' Annual Financial Reporting Requirements and include information related to the Fund. The accompanying financial statements may differ in presentation from the Texas Comptroller of Public Accounts' Annual Financial Reporting Requirements.

Management has evaluated subsequent events through October 31, 2012, the date the financial statements were available to be issued. No subsequent events requiring adjustment to, or disclosure in, the financial statements were identified as a result of this evaluation.

### **Note 2 – Investment in GEF**

The Fund only invests in GEF units and a negligible amount of cash. The Fund also continues to receive securities as proceeds in class action suits from the securities the Fund previously owned. These securities are normally sold when received, but from time to time will be reflected as a Fund investment. Subsequent participant contributions received by the Fund are also used to purchase GEF units. At August 31, 2012, the Fund is the majority participant in the GEF, with ownership of 30,233,803 units, which represents 86.26% of the GEF. At August 31, 2011, the Fund held 30,840,825 units, which represented 85.92% of the GEF.

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## LONG TERM FUND

*Notes to Financial Statements (cont.)*

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The GEF and the Fund have identical investment objectives. Additionally, the GEF's accounting policies follow the Fund's, as described in Note 3, except for the distributions to participants. On a monthly basis for accounting purposes, the GEF allocates its net investment income and realized gain or loss to the Fund based on its ownership of GEF units at month end. The allocated investment income and realized gain amounts increase the cost basis of the units in the GEF, and any allocated realized losses reduce the cost basis of the units in the GEF. Since the allocation is proportional to the percentage of ownership by the unitholders, no additional units are purchased. The Fund redeems GEF units quarterly to meet its distribution requirements to its unitholders.

### Note 3 – Significant Accounting Policies

(A) **Security Valuation** -- The Fund's investment in GEF units is valued at the net asset value per unit reported by the GEF. Investment assets which are held in the GEF that have readily determinable fair values are primarily valued on the basis of market valuations provided by independent pricing services. The GEF's investments in private investment funds, hedge funds, U.S. equity, non-U.S. equity, emerging market and fixed income investment funds and certain other equity securities are fair valued by management using the investments' capital balances and net asset value information provided by the investment managers as well as other considerations as described in the GEF financial statements. The Fund's investment in the GEF is valued at \$6,128,367,681 and \$6,056,577,496, as of August 31, 2012 and 2011, respectively.

(B) **Investment Income** -- Interest income is accrued as earned.

(C) **Security Transactions** -- A gain or loss is recognized on GEF unit sales on the basis of average cost.

(D) **Distributions to Participants** -- Cash distributions to participants are paid quarterly based on a per unit payout established by the UT Board. For the year ended August 31, 2012, the quarterly rate was \$0.080375 which equates to an annual rate of \$0.3215 per unit. For the year ended August 31, 2011, the quarterly distribution rate was \$0.07930 which equated to an annual rate of \$0.3172 per unit. The ratio of distributions to average net assets (12-quarter average) was 4.93% as of August 31, 2012. The investment policy provides that the annual payout will be adjusted by the average consumer price index of the prior 36 months subject to a maximum distribution of 5.5% of the Fund's average market value and a minimum distribution of 3.5% of the Fund's average market value.

(E) **Fund Valuation** -- Valuation of the Fund's units occurs on a quarterly basis. Unit values are determined by dividing the value of the Fund's net assets by the number of units outstanding on the valuation date.

(F) **Purchases and Redemption of Units** -- Unit purchases occur on the first business day of each fiscal quarter. Unit redemptions occur on the last business day of each fiscal quarter. The value of participating units, upon admission to the Fund, is based upon the market value of net assets held as of the quarterly valuation date. Redemptions from the Fund will also be made at the market value price per unit at the quarterly valuation date at the time of the redemption. There are no transaction costs incurred by participants for the purchase or redemption of units.

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*Notes to Financial Statements (cont.)*

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(G) **Participants' Net Assets** -- All participants in the Fund have a proportionate interest in the Fund's net assets.

(H) **Use of Estimates** -- The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

(I) **Cash and Cash Equivalents** -- Cash and Cash Equivalents consist of money market investments and other overnight funds.

### **Note 4 – Investment Risk**

The investment risk disclosure that follows relates to the GEF's investments before securities lending transactions and the investment of cash collateral. Disclosures relating to the GEF's securities lending are provided in Note 5. Values presented are the Fund's pro-rata share of GEF investments based on its unit ownership in the GEF.

#### **(A) Credit Risk**

Article VII, Section 11b of the Texas Constitution authorizes the UT Board, subject to procedures and restrictions it establishes, to invest the Permanent University Fund (the "PUF") in any kind of investment and in amounts it considers appropriate, provided that it adheres to the prudent investor standard. This standard provides that the UT Board, in making investments, may acquire, exchange, sell, supervise, manage, or retain, through procedures and subject to restrictions it establishes and in amounts it considers appropriate, any kind of investment 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 of the assets of the Fund rather than a single investment. Pursuant to Section 51.0031(c) of the Texas Education Code, the UT Board has elected the prudent investor standard to govern its management of the Fund.

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization (NRSRO). The GEF's investment policy does not provide specific limitations or requirements regarding investment ratings. Per GASB Statement No. 40 (GASB 40), *Deposit and Investment Risk Disclosures, an amendment to GASB Statement No. 3*, unless there is information to the contrary, obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. GASB 40 also provides that securities with split ratings, or a different rating assignment between NRSROs, are disclosed using the rating indicative of the greatest degree of risk. The following table presents the Fund's pro-rata share of each applicable GEF investment type grouped by rating as of August 31, 2012 and 2011:

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Notes to Financial Statements (cont.)

GEF Investment Type	August 31,		Rating
	2012	2011	
<b>Investments:</b>			
U.S. Government Guaranteed	\$ 52,766,394	\$ 69,870,345	AA
U.S. Government Non-Guaranteed:			
U.S. Agency	1,710,062	1,622,677	AA
U.S. Agency Asset Backed	-	8,897,889	AAA
U.S. Agency Asset Backed	34,810,277	33,672,080	AA
Total U.S. Government Non-Guaranteed	36,520,339	44,192,646	
Total U.S. Government	89,286,733	114,062,991	
Corporate Obligations:			
Domestic	7,047,390	10,234,407	AAA
Domestic	2,885,566	4,199,548	AA
Domestic	29,623,446	32,735,660	A
Domestic	29,651,066	23,144,354	BAA/BBB
Domestic	5,023,867	3,516,533	BA/BB
Domestic	3,557,925	2,500,881	B
Domestic	2,873,164	3,614,881	CAA/CCC
Domestic	1,153,770	1,367,846	CA/CC
Domestic	-	145,939	C
Domestic	368,867	255,548	D
Domestic	536,846	702,469	Not Rated
Foreign	20,976,305	23,937,499	AAA
Foreign	7,531,859	6,468,227	AA
Foreign	8,736,045	12,666,744	A
Foreign	10,929,930	8,559,822	BAA/BBB
Foreign	2,052,266	1,435,432	BA/BB
Foreign	668,169	644,977	B
Foreign	405,234	-	CAA/CCC
Foreign	124,160	-	Not Rated
Total Corporate Obligations	134,145,875	136,130,767	
Foreign Government and Provincial Obligations	71,496,342	90,833,759	AAA
Foreign Government and Provincial Obligations	30,101,486	15,127,936	AA
Foreign Government and Provincial Obligations	47,303,472	22,645,498	A
Foreign Government and Provincial Obligations	57,664,439	67,380,768	BAA/BBB
Foreign Government and Provincial Obligations	10,343,347	4,066,120	BA/BB
Foreign Government and Provincial Obligations	34,073,443	9,776,506	Not Rated
Total Foreign Government and Provincial Obligations	250,982,529	209,830,587	
Other Debt Securities	392,922	350,303	AAA
Other Debt Securities	928,320	1,080,677	AA
Other Debt Securities	3,374,756	3,588,953	A
Other Debt Securities	106,144	293,311	BAA/BBB
Other Debt Securities	-	606,910	BA/BB
Other Debt Securities	890,727	-	B
Total Other Debt Securities	5,692,869	5,920,154	
Total Debt Securities	\$ 480,108,006	\$ 465,944,499	
Convertible Securities	\$ 266,621	\$ -	B
Convertible Securities	-	1,759,748	Not Rated
Total Convertible Securities	\$ 266,621	\$ 1,759,748	
Other Investment Funds - Debt	\$ 6,949,585	5,944,755	BA/BB
Cash and Cash Equivalents - Money Market Funds	\$ 287,112,931	\$ 242,677,731	AAA
Cash and Cash Equivalents	9,938,307	8,868,461	Not Rated
Total Cash and Cash Equivalents	\$ 297,051,238	\$ 251,546,192	
<b>Net Deposit with Brokers for Derivative Contracts:</b>			
U.S. Government Guaranteed	\$ 309,359	\$ 701,056	AA
Foreign Government and Provincial Obligations	9,033,940	13,312,551	BAA/BBB
Foreign Government and Provincial Obligations	8,589,285	919,918	Not Rated
Cash	8,694,823	9,752,127	Not Rated
<b>Total Net Deposit with Brokers for Derivative Contracts</b>	<b>\$ 26,627,407</b>	<b>\$ 24,685,652</b>	

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## LONG TERM FUND

*Notes to Financial Statements (cont.)*

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### **(B) Concentrations of Credit Risk**

The GEF's investment policy statement contains the limitation that no more than 5% of the market value of fixed income securities may be invested in corporate or municipal bonds of a single issuer. The GEF does not hold any direct investments in any one issuer that is 5% or more of the market value of the GEF's fixed income investments.

### **(C) Custodial Credit Risk**

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the GEF will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the GEF will not be able to recover the value of its investment or collateral securities that are in the possession of another party. Texas State Statutes and the GEF's investment policy statements do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments. As of August 31, 2012 and 2011, the GEF does not have any deposits or investments that are exposed to custodial credit risk.

### **(D) Interest Rate Risk**

Interest rate risk is the risk that changes in market interest rates will adversely affect the value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its value to changes in market interest rates. Interest rate risk inherent in the GEF is measured by monitoring the modified duration of the overall investment portfolio. Modified duration estimates the sensitivity of the GEF's investments to changes in interest rates. The GEF has no specific policy statement limitations with respect to its overall modified duration. The following table summarizes the GEF's modified duration and the Fund's pro-rata share of the GEF investment value by investment type as of August 31, 2012 and 2011:

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## LONG TERM FUND

Notes to Financial Statements (cont.)

GEF Investment Type	August 31,			
	2012		2011	
	Value	Modified Duration	Value	Modified Duration
<b>Investments:</b>				
U.S. Government Guaranteed:				
U.S. Treasury Bonds and Notes	\$ 41,301,964	7.96	\$ 68,539,907	10.47
U.S. Treasury Bills	10,487,385	0.53	706,945	0.50
U.S. Treasury Inflation Protected	414,733	7.15	-	-
U.S. Agency Asset Backed	562,312	4.18	623,493	3.47
Total U.S. Government Guaranteed	<u>52,766,394</u>	6.44	<u>69,870,345</u>	10.31
U.S. Government Non-Guaranteed:				
U.S. Agency	1,710,062	7.06	1,622,677	9.11
U.S. Agency Asset Backed	34,810,277	2.65	42,569,969	2.83
Total U.S. Government Non-Guaranteed	<u>36,520,339</u>	2.85	<u>44,192,646</u>	3.06
Total U.S. Government	<u>89,286,733</u>	4.97	<u>114,062,991</u>	7.50
Corporate Obligations:				
Domestic	82,721,907	6.37	82,418,066	6.33
Foreign	51,423,968	5.37	53,712,701	5.10
Total Corporate Obligations	<u>134,145,875</u>	5.98	<u>136,130,767</u>	5.84
Foreign Government and Provincial Obligations	<u>250,982,529</u>	6.44	<u>209,830,587</u>	6.76
Other Debt Securities	<u>5,692,869</u>	12.77	<u>5,920,154</u>	11.87
Total Debt Securities	<u>480,108,006</u>	6.12	<u>465,944,499</u>	6.74
Convertible Securities	<u>266,621</u>	29.03	<u>1,759,748</u>	2.37
Other Investment Funds - Debt	<u>6,949,585</u>	6.90	<u>5,944,755</u>	7.50
Cash and Cash Equivalents	<u>297,051,238</u>	0.06	<u>251,546,192</u>	0.08
Total	<u>\$ 784,375,450</u>	3.84	<u>\$ 725,195,194</u>	4.42
<b>Net Deposit with Brokers for Derivative Contracts:</b>				
U.S. Government Guaranteed:				
U.S. Treasury Bills	\$ 80,969	0.67	\$ 701,056	0.28
U.S. Treasury Bonds and Notes	228,390	18.28	-	-
Total U.S. Government Guaranteed	<u>309,359</u>	13.67	<u>701,056</u>	0.28
Foreign Government and Provincial Obligations	<u>17,623,225</u>	5.49	<u>14,232,469</u>	6.91
Cash	<u>8,694,823</u>	-	<u>9,752,127</u>	-
<b>Total Net Deposit with Brokers for Derivative Contracts</b>	<u>\$ 26,627,407</u>	3.79	<u>\$ 24,685,652</u>	3.99

The GEF has purchased options on ten year constant maturity swaps, with expirations ranging from five to seven years, as insurance against possible future increases in inflation. As of August 31, 2012 the Fund's pro-rata share of these options had a notional value of \$2,896,580,518 and a fair value of \$4,099,431. As of August 31, 2011 the Fund's pro-rata share of these options had a notional value of \$2,390,294,400 and a fair value of \$10,709,394. The risk of loss on these options is limited to the Fund's pro-rata share of the premiums paid by the GEF upon the purchase of the options, which totaled \$16,265,734 as of August 31, 2012 and \$13,083,926 as of August 31, 2011. The GEF also purchased both puts and swaptions on the Japanese Yen, with expirations ranging from one to two years, as insurance against the possibility of a downturn in the Japanese economy.



# THE UNIVERSITY OF TEXAS SYSTEM

## LONG TERM FUND

*Notes to Financial Statements (cont.)*

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As of August 31, 2012 the Fund's pro-rata share of these puts and swaptions had a notional value of \$1,750,300,303 with a fair value of \$1,594,812 and a loss limited to \$14,888,610 which represents the premiums paid. As of August 31, 2011 the Fund's pro-rata share of these puts and swaptions had a notional value of \$3,239,793,597 with a fair value of \$6,043,994 and a loss limited to \$17,437,900 which represents the premiums paid. It is estimated that these options would adjust the 2012 duration of total debt securities of 6.12 downward by approximately 0.47, and the total duration of 3.84 downward by approximately 0.48. It is estimated that these options would adjust the 2011 duration of total debt securities of 6.74 downward by approximately 1.04, and the total duration of 4.42 downward by approximately 1.17. One of the GEF's external managers also uses options and interest rate and credit default swaps to modify the duration of its portfolio in a cost efficient manner. It is estimated by management that these positions held by the external manager would not significantly adjust the modified duration as presented above.

### ***(E) Investments with Fair Values That Are Highly Sensitive to Interest Rate Changes***

The GEF may invest in various mortgage backed securities, such as collateralized mortgage backed obligations. The GEF also may invest in investments that have floating rates with periodic coupon changes in market rates, zero coupon bonds and stripped Treasury and Agency securities created from coupon securities. No percentage of holdings limitations are specified in the investment policy statements regarding these types of securities. As of August 31, 2012 and 2011, the GEF's investments include the following investments that are highly sensitive to interest rate changes.

Collateralized mortgage obligations which are subject to early payment in a period of declining interest rates. The resultant reduction in expected total cash flows will affect the fair value of these securities. The Fund's pro-rata share of these securities amounted to \$29,053,093 and \$39,993,632 as of August 31, 2012 and 2011, respectively.

Mortgage backed securities which are subject to early payment in a period of declining interest rates. The resultant reduction in expected total cash flows will affect the fair value of these securities. The Fund's pro-rata share of these securities amounted to \$21,323,010 and \$21,364,612 as of August 31, 2012 and 2011, respectively.

Asset backed securities which are backed by home equity loans, auto loans, equipment loans and credit card receivables. Prepayments by the obligees of the underlying assets in periods of decreasing interest rates could reduce or eliminate the stream of income that would have been received. The Fund's pro-rata share of these securities amounted to \$2,802,497 and \$4,837,146, as of August 31, 2012 and 2011, respectively.

### ***(F) Foreign Currency Risk***

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of the GEF's non-U.S. dollar investments. There are no limitations on investments in non-U.S. denominated bonds or common stocks in relation to the GEF's total fixed income and developed country equity exposures in the GEF's investment policy statement.

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*Notes to Financial Statements (cont.)*

The following table summarizes the Fund's pro-rata exposure of the GEF's non-U.S. dollar investments at August 31, 2012 and 2011:

GEF Investment Type	August 31,	
	2012	2011
<b>Foreign Common Stock:</b>		
Australian Dollar	\$ 14,685,765	\$ 19,945,718
Brazilian Real	41,112,191	28,486,813
Canadian Dollar	13,992,023	19,962,071
Chilean Peso	1,271,395	1,223,006
Czech Koruna	651,821	818,199
Danish Krone	1,818,149	1,541,634
Egyptian Pound	500,833	583,685
Euro	30,696,487	38,425,520
Hong Kong Dollar	71,050,405	62,554,288
Hungarian Forint	514,093	640,173
Indian Rupee	7,995,955	11,903,946
Indonesian Rupian	7,361,464	6,359,478
Israeli Shekel	-	32,576
Japanese Yen	19,055,052	22,620,872
Malaysian Ringgit	10,051,456	9,096,012
Mexican Peso	7,755,239	8,036,825
Moroccan Dirham	200,236	295,937
Norwegian Kroner	561,524	1,529,628
Pakistani Rupee	354,476	293,236
Peruvian Nuevo Sol	2,401	41,968
Philippine Peso	5,366,751	1,760,228
Polish Zloty	3,119,427	4,576,046
Russian Ruble	-	839,853
Singapore Dollar	8,327,239	7,185,723
South African Rand	10,547,486	14,564,611
South Korean Won	29,499,460	41,709,518
Swedish Krona	7,583,268	8,032,760
Swiss Franc	5,744,706	7,957,313
Taiwan Dollar	18,228,430	16,161,655
Thai Baht	10,019,366	8,758,827
Turkish Lira	5,852,715	6,246,789
UK Pound	54,522,016	59,256,171
United Arab Emirates Dirham	595,561	689,401
Total Foreign Common Stock	<u>389,037,390</u>	<u>412,130,480</u>
<b>Other - Equity Securities:</b>		
Canadian Dollar	-	76
Chilean Peso	365	-
Malaysian Ringgit	-	744
Thai Baht	38,652	-
UK Pound	18	-
Total Other - Equity Securities	<u>39,035</u>	<u>820</u>
<b>Foreign Preferred Stock:</b>		
Brazilian Real	15,122,003	19,150,292
South African Rand	-	32,878
South Korean Won	305,171	119,248
Total Foreign Preferred Stock	<u>15,427,174</u>	<u>19,302,418</u>
<b>Foreign Government and Provincial Obligations:</b>		
Australian Dollar	16,599,760	10,317,021
Brazilian Real	76,950,290	80,885,350
Canadian Dollar	5,258,017	8,519,442
Colombian Peso	1,172,309	-
Euro	58,348,825	39,965,690
Hong Kong Dollar	359,400	499,985

# THE UNIVERSITY OF TEXAS SYSTEM

## LONG TERM FUND

Notes to Financial Statements (cont.)

GEF Investment Type	August 31,	
	2012	2011
<b>Foreign Government and Provincial Obligations (continued):</b>		
Hungarian Forint	\$ 4,177,391	\$ 2,907,456
Indonesian Rupian	-	4,066,119
Japanese Yen	23,102,385	8,625,091
Malaysian Ringgit	4,437,206	5,565,622
Mexican Peso	14,652,190	7,596,939
New Zealand Dollar	12,809,270	9,096,325
Norwegian Kroner	-	5,260,171
Polish Zloty	11,712,919	6,676,254
Singapore Dollar	1,688,425	4,377,861
South African Rand	5,824,812	5,076,308
South Korean Won	4,683,656	5,242,414
UK Pound	24,631,192	17,946,841
Total Foreign Government and Provincial Obligations	266,408,047	222,624,889
<b>Corporate Obligations:</b>		
Australian Dollar	7,152,187	8,479,141
Canadian Dollar	835,791	1,901,097
Euro	20,937,710	25,682,603
Japanese Yen	1,135,154	1,398,209
New Zealand Dollar	598,521	-
UK Pound	6,434,833	4,910,750
Total Corporate Obligations	37,094,196	42,371,800
<b>Convertible Securities:</b>		
Brazilian Real	-	1,759,748
<b>Purchased Options:</b>		
Australian Dollar	2,208,777	34,053,600
Brazilian Real	242,309	-
Euro	3,997	1,905,053
Japanese Yen	1,594,812	6,043,859
South Korean Won	8,940,342	26,963,075
Total Purchased Options	12,990,237	68,965,587
<b>Private Investment Funds:</b>		
Canadian Dollar	11,398,874	6,326,686
Euro	94,519,646	97,897,494
UK Pound	10,661,316	4,934,223
Total Private Investment Funds	116,579,836	109,158,403
<b>Investment Funds - Emerging Markets:</b>		
Brazilian Real	3,084,710	3,115,855
Canadian Dollar	490,556	-
Euro	1,842,737	-
Hong Kong Dollar	585,998	-
Swedish Krona	360,477	-
Taiwan Dollar	34,684	-
UK Pound	23,693,521	-
Total Investment Funds - Emerging Markets	30,092,683	3,115,855
<b>Investment Funds - Natural Resources:</b>		
UK Pound	1,398,955	-
<b>Cash and Cash Equivalents:</b>		
Australian Dollar	511,067	1,084,437
Brazilian Real	715,270	817,623
Canadian Dollar	31,417	65,147
Chilean Peso	5,807	1,010
Czech Koruna	18,360	12
Danish Krone	4,479	423
Egyptian Pound	360	-
Euro	1,320,241	916,443
Hong Kong Dollar	455,758	210,222
Hungarian Forint	2,044	41

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LONG TERM FUND

Notes to Financial Statements (cont.)

GEF Investment Type	August 31,	
	2012	2011
<b>Cash and Cash Equivalents (continued):</b>		
Indian Rupee	\$ 158,312	\$ 295,260
Indonesian Rupian	23,496	10,370
Israeli Shekel	2,256	1,235
Japanese Yen	59,891	5,127
Malaysian Ringgit	94,829	118,783
Mexican Peso	24,589	14,542
Moroccan Dirham	2,945	10,241
New Zealand Dollar	487	509
Norwegian Kroner	169	86,640
Pakistani Rupee	23	-
Peruvian Nuevo Sol	206	17,003
Philippine Peso	4,289	19,265
Polish Zloty	47,453	9,610
Singapore Dollar	176,626	2,075
South African Rand	36,829	12,101
South Korean Won	200,969	109,454
Swedish Krona	6,751	923
Swiss Franc	178	3
Taiwan Dollar	554,787	492,313
Thai Baht	23,561	8,874
Turkish Lira	53,066	117
UK Pound	280,180	4,039,126
Total Cash and Cash Equivalents	<u>4,816,695</u>	<u>8,348,929</u>
<b>Written Options:</b>		
Australian Dollar	(1,124,600)	(20,833,192)
Euro	-	(15,971)
South Korean Won	(4,451,660)	(17,501,314)
Total Written Options	<u>(5,576,260)</u>	<u>(38,350,477)</u>
<b>Swaps:</b>		
Australian Dollar	17,920	(967)
Brazilian Real	-	22,261
Euro	1,636	(11,669)
Japanese Yen	(790,525)	16,183
Mexican Peso	229,121	420,599
UK Pound	(84,805)	(194,317)
Total Swaps	<u>(626,653)</u>	<u>252,090</u>
<b>Futures:</b>		
Australian Dollar	(16,694)	25,394
Brazilian Real	(592,264)	-
Canadian Dollar	(3,505)	(25,463)
Euro	(227)	248,295
Japanese Yen	4,617	-
UK Pound	(4,950)	(70,131)
Total Futures	<u>(613,023)</u>	<u>178,095</u>
Total	<u>\$ 867,068,312</u>	<u>\$ 849,858,637</u>

(G) **Counterparty (Credit) Risk**

The derivative instruments utilized by the GEF, contain varying degrees of off-balance sheet risk whereby changes in the fair values of securities underlying the financial instruments may exceed the amounts recognized in the statement of changes in fiduciary net assets. The GEF manages these risks on an aggregate basis along with the risks associated with its other investments as part of its overall risk management process.

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*Notes to Financial Statements (cont.)*

The Fund's pro-rata share of the GEF's gross counterparty exposure as of August 31, 2012 for options, swaps, and foreign currency exchange contracts is shown in the table below:

<b>Options</b>				
<u>Assets</u>	<u>Liabilities</u>	<u>Assets</u>	<u>Liabilities</u>	
<u>Notional</u>	<u>Notional</u>	<u>Fair Value as of August 31, 2012</u>	<u>Fair Value as of August 31, 2012</u>	<u>Counterparty Rating</u>
\$ 5,583,075,638	\$ 808,331,404	\$ 16,847,359	\$ 5,822,282	A
<b>Swaps</b>				
<u>Assets</u>	<u>Liabilities</u>	<u>Assets</u>	<u>Liabilities</u>	
<u>Notional</u>	<u>Notional</u>	<u>Fair Value as of August 31, 2012</u>	<u>Fair Value as of August 31, 2012</u>	<u>Counterparty Rating</u>
\$ 79,286,790	\$ 116,701,111	\$ 1,285,166	\$ 639,972	A
2,977,100	792,277	778,828	791,877	AA
\$ 82,263,890	\$ 117,493,388	\$ 2,063,994	\$ 1,431,849	
<b>Foreign Currency Exchange Contracts</b>				
<u>Assets</u>	<u>Liabilities</u>	<u>Assets</u>	<u>Liabilities</u>	
<u>Notional</u>	<u>Notional</u>	<u>Fair Value as of August 31, 2012</u>	<u>Fair Value as of August 31, 2012</u>	<u>Counterparty Rating</u>
\$ 150,792,372	\$ 268,456,596	\$ 3,396,021	\$ 5,677,761	A
5,007,480	4,069,871	79,503	88,224	AA
\$ 155,799,852	\$ 272,526,467	\$ 3,475,524	\$ 5,765,985	

The Fund's pro-rata share of the GEF's gross counterparty exposure as of August 31, 2011 for options, swaps, and foreign currency exchange contracts is shown in the following table:

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*Notes to Financial Statements (cont.)*

<b>Options</b>				
<u>Assets</u>	<u>Liabilities</u>	<u>Assets</u>	<u>Liabilities</u>	
<u>Notional</u>	<u>Notional</u>	<u>Fair Value as of August 31, 2011</u>	<u>Fair Value as of August 31, 2011</u>	<u>Counterparty Rating</u>
\$ 4,045,345,503	\$ 1,018,340,684	\$ 57,966,968	\$ 33,546,543	A
2,745,390,487	216,090,035	21,774,618	9,497,541	AA
<u>\$ 6,790,735,990</u>	<u>\$ 1,234,430,719</u>	<u>\$ 79,741,586</u>	<u>\$ 43,044,084</u>	

  

<b>Swaps</b>				
<u>Assets</u>	<u>Liabilities</u>	<u>Assets</u>	<u>Liabilities</u>	
<u>Notional</u>	<u>Notional</u>	<u>Fair Value as of August 31, 2011</u>	<u>Fair Value as of August 31, 2011</u>	<u>Counterparty Rating</u>
\$ 34,226,472	\$ 238,512,132	\$ 1,080,666	\$ 18,387,551	A
829,710,700	2,062,033	584,404	43,422	AA
<u>\$ 863,937,172</u>	<u>\$ 240,574,165</u>	<u>\$ 1,665,070</u>	<u>\$ 18,430,973</u>	

  

<b>Foreign Currency Exchange Contracts</b>				
<u>Assets</u>	<u>Liabilities</u>	<u>Assets</u>	<u>Liabilities</u>	
<u>Notional</u>	<u>Notional</u>	<u>Fair Value as of August 31, 2011</u>	<u>Fair Value as of August 31, 2011</u>	<u>Counterparty Rating</u>
\$ 269,696,145	\$ 231,384,752	\$ 3,020,769	\$ 1,755,065	A
113,183,486	101,875,788	1,005,143	5,922,053	AA
<u>\$ 382,879,631</u>	<u>\$ 333,260,540</u>	<u>\$ 4,025,912</u>	<u>\$ 7,677,118</u>	

As of August 31, 2012 and 2011, the GEF also had investments in futures contracts, options on future contracts and exchange-cleared swaps. Futures contracts, options on future contracts and exchange-cleared swaps expose the GEF to minimal counterparty credit risk since they are exchange traded and the exchange's clearinghouse, as counterparty to all exchange traded futures, guarantees them against default, and therefore they are not presented in the table above.

Counterparty risk for swaps, options and foreign currency exchange contracts which are traded over-the-counter is mitigated by having master netting arrangements between the GEF and its counterparties, and by the posting of collateral on a daily basis by the counterparty to the GEF to cover the GEF's exposure to a counterparty above the limits set in place in each master netting agreement. Collateral posted by counterparties is held by the GEF in one of its accounts at the GEF's custodian bank. As of August 31, 2012 and 2011, the Fund's pro-rata share was \$10,765,135 and \$42,675,500 respectively, of collateral held by the GEF related to derivative instruments other than futures. As of August 31, 2012 and 2011, the Fund's pro-rata share was \$17,984,145 and \$41,648,922, respectively, of collateral posted with brokers by the GEF related to derivative instruments other than futures.

**Note 5 – Securities Lending**

In accordance with the prudent investor investment standards, the GEF loans securities to certain brokers who pay the GEF negotiated lenders' fees. These fees are included in the GEF's investment income, and related expenses, net of rebates paid to borrowers. The GEF receives qualified

**THE UNIVERSITY OF TEXAS SYSTEM**  
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*Notes to Financial Statements (cont.)*

securities and/or cash as collateral against the loaned securities. The collateral, when received, will have a market value of 102% of loaned securities of U.S. issuers and a market value of 105% for loaned securities of non-U.S. issuers. If the market value of the collateral held in connection with loans of securities of U.S. issuers is less than 100% at the close of trading on any business day, the borrower is required to deliver additional collateral by the close of the next business day to equal 102% of the market value. For non-U.S. issuers, the collateral should remain at 105% of the market value of the loaned securities at the close of any business day. If it falls below 105%, the borrower must deliver additional collateral by the close of the following business day. The Fund's pro-rata share of the value of the GEF's securities loaned and the value of collateral held are as follows at August 31, 2012 and 2011:

<b>GEF Securities on Loan</b>	<b>2012 Value</b>	<b>2011 Value</b>	<b>Type of Collateral</b>	<b>2012 Value of Collateral</b>	<b>2011 Value of Collateral</b>
U.S. Government	\$ 12,436,354	\$ 2,798,693	Cash	\$ 12,692,255	\$ 2,856,153
Foreign					
Government	2,487,196	7,029,082	Cash	2,605,874	7,371,790
Corporate Bonds	5,742,392	7,201,971	Cash	5,901,165	7,381,971
Common Stock	91,109,702	58,806,122	Cash	95,799,495	61,003,258
<b>Total</b>	<b>\$ 111,775,644</b>	<b>\$ 75,835,868</b>	<b>Total</b>	<b>\$ 116,998,789</b>	<b>\$ 78,613,172</b>
U.S. Government	\$ 23,431,011	\$ 696,728	Non-Cash	\$ 23,915,199	\$ 739,306
Corporate Bonds	-	123,812	Non-Cash	-	131,379
	<b>\$ 23,431,011</b>	<b>\$ 820,540</b>		<b>\$ 23,915,199</b>	<b>\$ 870,685</b>

Cash received as collateral for securities lending activities is invested and reinvested in a commingled pool managed exclusively for the benefit of the GEF, the PUF, the Intermediate Term Fund and other UT Board accounts that participate in securities lending activities. The pool is managed in accordance with investment guidelines established in the securities lending contract between the GEF and its securities lending agent. The maturities of the investments in the pool do not necessarily match the term of the loans, rather the pool is managed to maintain a maximum dollar-weighted average maturity of 60 days and an overnight liquidity of 20%. Lending income is earned if the returns on those investments exceed the rebate paid to borrowers of the securities. The income remaining after the borrower rebates is then shared with the lending agent on a contractually negotiated split. If the investment of the cash collateral does not provide a return exceeding the rebate or if the investment incurs a loss of principal, the payment of the shortfall to the borrower would come from the GEF and the securities lending agent in the same proportion as the split of income.

The Fund's pro-rata share of the GEF's portion of the collateral pool investments, rating by NRSRO, and weighted average maturity as of August 31, 2012 and 2011 is shown in the following table:

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Notes to Financial Statements (cont.)

Description	August 31,					
	2012			2011		
	Fair Value	Rating	Weighted Average Maturity In Days	Fair Value	Rating	Weighted Average Maturity In Days
Repurchase Agreements	\$ 57,262,812	No Rating	4	\$ 27,891,884	No Rating	1
Treasuries	1,626,780	AA	169	-	-	-
Agencies	3,192,938	P	36	-	-	-
Commercial Paper	25,205,648	P	57	27,436,937	P	28
Floating Rate Notes	14,007,138	AA		6,749,288	AA	
Floating Rate Notes	3,918,330	A		8,113,357	A	
Total Floating Rate Notes	<u>17,925,468</u>		40	<u>14,862,645</u>		33
Interest Bearing Notes	-		-	371,364	AA	76
Certificates of Deposit	10,980,283	P	68	8,040,917	P	33
Time Deposits	813,546	P	24	-	-	-
Other Receivables/Payables	(8,686)	Not Rated	-	9,427	Not Rated	-
Total Collateral Pool Investment	<u>\$ 116,998,789</u>		30	<u>\$ 78,613,174</u>		20

Collateral pool investments are uninsured, and are held by the securities lending agent, in its name, on behalf of the GEF, except for the investments in repurchase agreements which are held in the securities lending agent's name by a third party custodian not affiliated with the GEF or the borrower of the associated loaned securities. Therefore, the collateral pool is not exposed to custodial credit risk because the pool investments are not held by counterparties to the lending transactions or the counterparties' trust department or agent.

Cash collateral is recorded as an asset with an equal and offsetting liability to return the collateral on the statements of fiduciary net assets. Pool investments are valued at amortized cost which is indicative of fair value. Investments received as collateral for securities lending activities are not recorded as assets because the investments remain under the control of the transferor, except in the event of default.

In the event of default, where the borrower is unable to return the securities loaned, the GEF has authorized the securities lending agent to seize the collateral held. The collateral is then used to replace the borrowed securities where possible. Due to some market conditions, it is possible that the original securities cannot be replaced. If the collateral is insufficient to replace the securities, the securities lending agent has indemnified the GEF from any loss due to borrower default.

As of August 31, 2012 and 2011, the GEF had no credit risk exposure to borrowers because the amounts the GEF owed to borrowers exceeded the amounts the borrowers owed the GEF.

There were no significant violations of legal or contractual provisions, no borrower or securities lending agent default losses, and no recoveries of prior period losses during the years ended August 31, 2012 and 2011.



**THE UNIVERSITY OF TEXAS SYSTEM**  
**LONG TERM FUND**

*Notes to Financial Statements (cont.)*

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**Note 6 – Fees and Expenses**

The Fund is assessed a management fee by UTIMCO to cover the costs of managing the Fund and providing day-to-day operations. These fees are based on a budget prepared by management and approved by the UT Board. The fees assessed for the years ending August 31, 2012 and 2011, were \$5,274,701 and \$4,821,311, respectively.

The Fund is assessed an annual administrative fee on behalf of UT System and UT System institutions for the support of endowment administration and management efforts. This fee is assessed and paid at the beginning of each fiscal year. The fees assessed for the years ending August 31, 2012 and 2011, were \$12,502,195 and \$12,074,085, respectively.

The Fund is assessed a fee to cover costs associated with UT System personnel in their efforts to provide assistance to the UT Board and the Chancellor of the UT System in their oversight responsibilities of UTIMCO. The fees assessed for the years ended August 31, 2012 and 2011, were \$98,040 and \$122,050, respectively.

The Fund incurs other expenses related to its operations primarily consisting of audit fees, legal, and custodial fees.

**THE UNIVERSITY OF TEXAS SYSTEM**  
**LONG TERM FUND**  
*Supplemental Schedule*

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**Financial Highlights**  
*Years Ended August 31,*

	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>
<b>Selected Per Unit Data</b>					
Net Asset Value, Beginning of Year	\$ 6.671	\$ 6.107	\$ 5.706	\$ 6.976	\$ 7.503
Income from Investment Operations					
Net Investment Income (A)	0.029	0.040	0.035	0.043	0.090
Net Realized and Unrealized Gains (Losses) on Investments	<u>0.156</u>	<u>0.841</u>	<u>0.676</u>	<u>(1.011)</u>	<u>(0.324)</u>
Total Income (Loss) from Investment Operations	<u>0.185</u>	<u>0.881</u>	<u>0.711</u>	<u>(0.968)</u>	<u>(0.234)</u>
Less Distributions					
From Net Investment Income	0.029	0.040	0.035	0.043	0.090
From Net Realized Gains	<u>0.293</u>	<u>0.277</u>	<u>0.275</u>	<u>0.259</u>	<u>0.203</u>
Total Distributions	<u>0.322</u>	<u>0.317</u>	<u>0.310</u>	<u>0.302</u>	<u>0.293</u>
Net Asset Value, End of Year	<u>\$ 6.534</u>	<u>\$ 6.671</u>	<u>\$ 6.107</u>	<u>\$ 5.706</u>	<u>\$ 6.976</u>

**Ratios and Supplemental Data**

Net Assets, End of Year (in thousands)	\$6,128,376	\$6,056,578	\$5,130,276	\$4,516,800	\$5,285,011
Ratios to Average Net Assets					
Investment Expenses	0.27%	0.32%	0.31%	0.31%	0.26%
Total Expenses (A)	0.48%	0.53%	0.56%	0.59%	0.45%
Net Investment Income (B)	0.44%	0.62%	0.59%	0.77%	1.22%
Distributions (5-quarter average)	4.96%	4.87%	5.20%	5.38%	3.96%
Distributions (12-quarter average)	4.93%	5.12%	4.83%	4.41%	4.00%

(A) Total expenses include expenses and the expense component of the allocation of GEF net investment income balance on the statements of changes in fiduciary net assets.

(B) Net investment income is comprised of investment income (excluding the net increase in investments) and expenses as presented on the statements of changes in fiduciary net assets.