MINUTES OF MEETING OF
THE AUDIT AND ETHICS COMMITTEE OF
THE UNIVERSITY OF TEXAS INVESTMENT MANAGEMENT COMPANY

The Audit and Ethics Committee of The University of Texas Investment Management Company (the "Committee") convened on the 10th day of June, 1996, in the offices of Hicks, Muse, Tate & Furst, 200 Crescent Court, Suite 1600, Dallas, Texas, said meeting having been called by the Committee Chairman, with notice provided to each member in accordance with the Bylaws. Participating in the meeting were the following members of the Committee:

Robert H. Allen
Susan M. Byrne

thus, constituting a majority and quorum of the Committee. Also, participating in the meeting was Bernard Rapoport, Chairman of the Board of Regents (the "U. T. Board") of The University of Texas System (the "System"); Thomas G. Ricks, President of The University of Texas Investment Management Company (the "Corporation"); Jerry E. Turner, Secretary of the Corporation; and Cathy Iberg, Vice-President - Investment Operations of the Corporation. Mr. Allen, in the absence of Donald L. Evans, Chairman, called the meeting to order at 11:15 a.m.

Approval of Committee Mandate

The first matter to come before the Committee was approval of the Audit and Ethics Committee Mandate (the "Mandate"). Mr. Ricks reviewed the responsibilities of the Committee as contained in the Mandate. Mr. Allen inquired as to whether the Mandate had been approved by the Corporation's Board of Directors (the "Board"). Mr. Ricks replied that the Mandate was presented in the draft UTIMCO Business Plan dated October 5, 1995 and was the basis for the adoption of a resolution on February 22, 1996 by the Board (then consisting of Messrs. Hicks, Cunningham, Evans and Loeffler) to create the Committee. However, the Mandate itself had not been adopted by the Board pursuant to a formal resolution. Mr. Allen stated that he approved of the Mandate but that he believed the delegations of authority to the Committee under the Mandate warranted a formal adoption of the Mandate by the Board. Ms. Byrne agreed with Mr. Allen's statement. Mr. Ricks committed to prepare a resolution for adoption by the Board approving the Mandate prior to the Committee's selection of an independent auditor in late July, 1996.

In reviewing the Mandate, Ms. Byrne inquired whether management would receive the management letter prior to receipt by the Committee. Mr. Ricks responded that management's responses were generally included in the management letter. Ms. Byrne also inquired as to whether the auditors would understand that they were being hired by the Board as opposed to UTIMCO management ("Management") or the System. Mr. Ricks responded that the Mandate and the audit plan to be presented later in the meeting assumed the Committee's primary role in the auditor selection process. Mr. Rapoport stated that although the

Corporation would be engaging its own auditors, it was important for outside parties to understand that the Corporation was ultimately a Board controlled enterprise.

At this point in the meeting, Mr. Rapoport was called away and did not return to the meeting.

Review of UTIMCO Financial Statements

Ms. Iberg distributed financial statements which included footnotes. Mr. Ricks stated that Management had installed a Salomon accounting system from which the Corporation's financial statements were prepared. He reviewed the Corporation's most recent statement of financial position, statement of activities and statement of cash flows as of April 30, 1996 and for the two month period since inception on March 1, 1996. He stated that the statements were prepared in accordance with FAS 117 Financial Statements of Not for Profit Organizations which differed slightly from presentation standards of for profit organizations.

The two major assets of the Corporation were cash of approximately $1 million representing advance payments of quarterly management fees and furniture and equipment of approximately $600,000. The Corporation's revenues for the relevant two months period consisted of management fees of $922,000, directors fees of $7,250 and interest on invested cash of $5,000. Mr. Ricks stated that certain members of Management serve on the boards of directors of approximately five portfolio companies for which they receive directors fees. Although they served in an individual capacity, they were nominated in recognition of the U. T. Board's ownership interest in the portfolio company. As a result, they were required to turn over all compensation received for such services to the Corporation. The Corporation's expenses for the period were approximately $550,000 comprised primarily salaries resulting in a "net surplus" of $380,000. Mr. Ricks further stated that the expenses were below budget due to the deferral of either new or replacement hires for three positions. Since the Corporation was a not for profit corporation, any surpluses generated by the Corporation at the end of the fiscal year would be credited against the management fee in the succeeding year. From a cash standpoint, the Corporation ended the period with a roughly $1,000,000 balance which was invested in a Dreyfus Money Market Fund by Bank One as holder of the Corporation's operating account.

Mr. Ricks also presented a supplemental schedule showing expenses as allocated by major fund group. Mr. Allen inquired as to whether future statements would include revenues by fund. Mr. Ricks responded affirmatively stating that the footnotes would be refined as well in preparation for fiscal year end August 31 statements.

At this point in the meeting, Mr. Evans arrived.

Review of 1996 Audit Plan

Mr. Ricks stated that he had met with representatives of the System to devise an audit plan for the financial statements of the funds under management and the Corporation itself. Mr. Ricks then reviewed the proposed audit plan stating that an external accounting firm would be used to audit the PUF because of the precedent established in the previous year, the AAA status of the fund's bonds and the amount of PUF indebtedness outstanding. An external accounting firm would also perform an audit of the Corporation's books because it was a separate legal entity from the System. However, the Board would rely on an internal audit of the Long Term Fund and Short Intermediate Term Fund by the U. T. internal audit staff. Mr. Ricks also stated that although the State Auditors Office had yet to be consulted on the plan, it assumed some degree of reliance on the field work of the internal and external auditors. U. T. System would coordinate with the State Auditors Office upon approval of the plan by the Committee. Mr. Evans stated that he wanted the Long Term fund and the Short Intermediate Term Fund to be audited by an outside auditor as well in order to provide assurance to the Board of the performance of its fiduciary responsibilities. His opinion was supported by both Mr. Allen and Ms. Byrne.

Ms. Byrne then inquired as to the audit trail for alternative assets. Mr. Ricks stated that the transaction procedures for alternative assets did not conform to those of publicly traded securities. The investments were generally in the form of limited partnership interests purchased directly from general partners rather than through brokers in book entry form and with confirmation. In addition, valuations were not provided by pricing services but were taken from the audited financial statements of the partnership. Underlying portfolio company valuations were generally approved annually or semi-annually by an advisory committee of limited partners and verified by the partnership audits. Reviews of the private investments since the mid-1980s by the U. T. internal auditors had not identified any problems.

Review of UTIMCO Compliance

Mr. Ricks referred the Committee to Tab 4 of the meeting book and stated that a preliminary finding of the State Auditor's Office review of investment practices was the need to improve documentation and reporting of compliance. Compliance by the Corporation was required in five major areas: federal statutes; state statutes; the Investment Management Services Agreement; investment policies; and the UTIMCO Code of Ethics. Compliance regarding federal and state tax issues involved compliance with Internal Revenue Code Section 501(c)(3). The Corporation had received its 501(c)(3) exemption from the Internal Revenue Service and was required to file a Form 990 annually. The Corporation had also received an exemption from state franchise, sales, excise and use taxes by the State Comptroller.

Mr. Ricks also reviewed statutory requirements under state statutes. He reviewed the major requirements of Section 66.08 of the Education Code, Article VII, Section 11b of the State Constitution governing investment of the PUF, Chapter 51 of the Education Code and, finally, Section 163 of the Property Code, a.k.a. the Uniform Management of Institutional Funds Act.

Mr. Ricks then reviewed with the Committee the primary obligations required to be performed under the Investment Management Services Agreement. He also stated that the investment policies pursuant to which the Corporation was authorized to invest funds were to be reviewed by the Corporation and presented for annual approval by the U. T. Board. He reported that only the PUF investment policy had been amended concurrent with the delegation of investment management authority to the Corporation. No additional changes to policies had been submitted for U. T. Board approval at the request of the Secretary to the U. T. Board due to the size of the agenda item authorizing the contract with the Corporation. The understanding was that the current investment policies should be reviewed by the Board and submitted to the U. T. Board within the year for approval at the conclusion of this process. Mr. Ricks also stated that the PUF and LTF policies would be reviewed at the August 30 meeting when a representative from Cambridge Associates would update its asset allocation study for the LTF. In addition, Mr. Ricks stated that he had prepared and distributed to the Board the Analysis and Proposed Amendment to the Texas Constitution for the PUF as an introduction to a Board discussion on PUF investment policy.

Mr. Ricks then referred the Committee to the UTIMCO Code of Ethics. He stated that the Code applied to directors, officers and employees all of whom would be required to sign a Certificate of Receipt and Acceptance. He added that he was considering adding the AIMR Standards of Professional Conduct which were directed specifically at investment professionals, were updated on a regular basis and were the industry standard. All of the company's CFAs were already required to comply with the Standards.

Mr. Ricks then referred to the UTIMCO Financial Disclosure and Conflict of Interest Statement. This form was based on the System form and had been signed by all employees. Mr. Ricks stated that concerns had been raised as to whether the required disclosure of personal financial information by voluntary outside directors would be subject to public dissemination. Also, to what degree would it serve as a disincentive for qualified persons to serve on the Board. Given these concerns, it was agreed that the financial Disclosure Form would be addressed at the next meeting of the Committee. Mr. Evans remarked that he already filed a form as a System regent but he could see where it could serve as a disincentive for some people particularly given the lack of compensation. Mr. Allen responded that the only true way to determine this was to circulate the form to directors prior to the next meeting. Mr. Ricks agreed to do so.

Report on State Auditors Investment Practices Review of U. T. System

Mr. Ricks summarized the objectives of the review stating that the auditors had been in their offices since October of the preceding year. He stated that the staff had received preliminary audit points on January 4 and March 4. While the audit had turned up some valid recommendations, the staff had a strong disagreement with respect to other recommendations as well as the materiality of some findings. The auditors findings were due on May 15 but had not been received by the June 10 meeting date. He would report on the findings and management's responses at the next meeting.

There being no further items to come before the Committee, the meeting was adjourned at 12:25 p.m.

Donald L. Evans
Chairman
Audit and Ethics Committee