

**BUDGET, FINANCE AND INVESTMENT COMMITTEE  
BOARD OF TRUSTEES  
UNIVERSITY OF VERMONT AND STATE AGRICULTURAL COLLEGE**

A meeting of the Budget, Finance and Investment Committee of the Board of Trustees of the University of Vermont State and Agricultural College was held on Friday, November 10, 2006 at 10:00 a.m., in room B308 Marsh Lounge, Billings Student Center.

**MEMBERS PRESENT:** Chair Deborah McAneny, Co-Vice Chair Robert Cioffi, Edwin Amidon Jr., Bill Botzow, Ian Boyce, Johannah Donovan, John Hilton Jr., Richard Hube Jr., Susan Hudson-Wilson, Raymond Pecor Jr., and Stirling Winder

**REPRESENTATIVES PRESENT:** Staff Representative Diane Trono, and Student Representatives Jessica Banks and Sean Haggerty

**ABSENT:** Co-Vice Chair Robert Young, Trustee Kathleen Hoyt, Faculty Representatives Albert Joy and Cory Teuscher, Alumni Representatives Samuel Bain and Meg Guzewicz, and Staff Representative Joan Kieran

**OTHER TRUSTEES PRESENT:** Board Chair Carl Lisman

**PERSONS ALSO PARTICIPATING:** President Daniel Fogel, Vice President for Finance and Administration J. Michael Gower, Associate Vice President for Budget and Resource Management Ted Winfield, LaRoy Brantley, Cambridge Associates, and Chris Cowen, Prager, Sealy & Co., LLC

Chair Deborah McAneny called the meeting to order at 10:05 a.m.

### **Committee Orientation**

Chair McAneny reviewed the overall responsibilities of the members of the newly formed Budget, Finance, and Investment Committee. The committee is charged with overseeing the development of strategic, long-range institutional financial plans and related plan objectives. Attention of the committee will be focused on strategic and policy issues.

### **Acceptance of Minutes**

A motion was made, seconded and voted to accept the minutes from the Debt Subcommittee meeting on September 7, 2006 and the Finance and Budget Committee and Investment Committee meetings held on September 8, 2006.

### **Strategic Financial Plan**

Chair McAneny facilitated a follow-up discussion of Version 5.0 of the Strategic Financial Plan (SFP), following a presentation made earlier today to the Committee of the Whole. A lengthy discussion took place on the impact of projected tuition rate increases from a financial and competitive standpoint. The committee questioned whether the 6.0% tuition increases projected for FY 2008, FY 2009, and FY 2010 were reasonable and appropriate. Concerns were also raised over the level of student debt at graduation. The committee discussed the impact of

tuition increases on in-state and out-of-state students in relation to levels of enrollment and increased financial aid needs. Currently, approximately 80% of Vermont students receive financial aid in the form of merit and need-based aid; a lesser percentage of out-of-state students receive aid. A higher tuition rate strategy is tied to higher financial aid needs. Referring to a recent release of *Kiplinger's Personal Finances* distributed at the Committee of the Whole earlier, President Fogel pointed out that although UVM's "sticker price" is ranked higher than most public institutions, the University's ranking among public institutions for "in-state costs after aid" placed us 49<sup>th</sup> out of the 100 public institutions listed. Committee members emphasized the importance of holding down in-state tuition increases to keep students in Vermont, and being careful not to transfer costs to out-of-state students.

Chair McAneny summarized the discussion by outlining the analyses that had been requested by the committee for further review. Those included peer group tuition analyses of the relationship of in-state versus out-of-state tuition, gross and net tuition, the level of student debt at graduation, and how tuition increases are handled. She also asked that a matrix be created, reflecting the impact of a 1.0% increase in the University's tuition both in total and by in-state and out-of-state, to establish a baseline for comparison. An interim meeting prior to the next Board meeting in February was suggested to review these analyses.

Next, the committee discussed the current fundraising growth assumptions built into Version 5.0. It was debated whether the current assumptions were too conservative. President Fogel expressed his concern over increasing cash flow projections as a part of managing the University's debt costs. The committee requested that a matrix be formed, comparing fundraising growth as projected against a more aggressive growth projection, recognizing stretch goals.

In conclusion, President Fogel explained that he has charged the Provost, The Vice President for Finance and Administration, and the Vice President for Development and Alumni Affairs with developing strategies that would enable the following: (1) increase net expendable assets beyond those recorded in Version 4.0 of the SFP by a minimum of \$20 million over the course of the next four fiscal years beginning with FY 2007, (2) increase operating revenues by a total of \$20 million beyond Version 4.0 over the next four fiscal years, and (3) achieve savings that will reduce expenditures reflected in Version 4.0 by a minimum of \$20 million over the course of the next four fiscal years. The results of these strategies have been incorporated into Version 5.0 of the SFP.

### **Capital Funding Strategies for UVM**

Chris Cowen, Prager, Sealy & Co., LLC provided background to the committee of the University's current debt profile and the implications of different funding options on debt capacity and net assets over time. Internal funding options include unrestricted reserves and philanthropy. External funding options include third party debt, leases, and direct debt. Mr. Cowen explained that use of internal funding sources impacts the numerator (expendable net assets) of the viability ratio, while external funding sources impacts the denominator (total long-term debt). Utilizing internal funds has a similar impact on debt capacity as borrowing – i.e. cash funding a project does not preserve debt capacity. The use of external funding impacts the University's credit profile. Rating agencies distinguish between "on-credit/off-credit" and "on-balance sheet/off-balance sheet." Structuring a transaction to keep it off the balance sheet (e.g.,

developer financing, subsidiary borrowing) does not necessarily keep it off credit. The rating agency may choose to recognize it against the University's debt capacity.

Chair McAneny pointed out that the viability ratio neared capacity at the end of FY 2006. Whether the University borrows or uses its reserves will impact the ratio. In order not to go out of compliance on the viability ratio in the future, the University will need to focus on increasing net assets. Mr. Cowen outlined several activities to be considered to build net assets (and thereby debt capacity) over time including optimizing fundraising activities- specifically an increase in unrestricted gifts, sale of unproductive or non-core assets, improving operating efficiencies, and maximizing return on investable funds.

The committee requested an update of the competitive benchmark study of debt ratios for review at a future meeting.

At 12:00 p.m. the Budget, Finance and Investment Committee recessed. The committee reconvened at 1:30 p.m., in Memorial Lounge, 338 Waterman Building.

### **Sudan Divestiture Update**

John Snow, Chair, Sudan Divestiture Work Group, reported on the current status of the Sudan Divestiture and made (3) recommendations to the committee. The recommendations were: 1) work with State Street Global Advisors (SSgA) to initiate discussion with other investors in S&P 500 Tobacco Free regarding changing that fund to Tobacco/Sudan Free; 2) obtain cost from State Street, including fees and tracking error, for a separate fund that is Sudan/Tobacco free; and 3) inquire to Cambridge Associates as to the availability of other tobacco free/Sudan free index funds in the market.

Mr. Snow reported on the methodology used by the Work Group which followed the divestment model of the Sudan Task Force. The Work Group developed the list of 20 worst offender companies that was adopted by Investment Committee and letters were sent to managers – three versions depending on nature of fund – separate or commingled, with additional questions for SSgA. The non-pooled companies responded to the letters with either the securities “were not in the current holdings” and/or the securities “would be placed on a not to be purchased list.” The pooled fund managers were sent a letter asking to consider alternative products that exclude Sudan. The Work Group reviewed the summary of manager responses to the letters and was generally pleased with the level of response, with many accounts already containing no Sudan holdings.

SSgA responded that they did hold Schlumberger as part of S&P 500 Tobacco Free. This was seen as the most troublesome since it seemed likely to result in the largest holding of any offending company and it was likely to be on-going. SSgA indicated in their response that they had developed Sudan Free separate accounts for investors and also indicated they would be willing to work with UVM to determine if other investors in Tobacco Free would support adding Sudan Free to that fund.

Mr. Snow concluded that the Work Group would continue to meet quarterly if the Treasurer should decide to look at the S&P 500 Tobacco/Sudan Free; if not to meet twice a year.

The committee passed a motion vote to direct the Treasurer to pursue the recommendations as presented by Mr. Snow.

### Asset Allocation, Performance and Manager Review

Mr. Brantley reviewed the final report of performance numbers for the consolidated endowment fiscal year ended September 30, 2006:

	<b>LATEST %</b>	<b>CYTD%</b>
<b>ASSETS</b>	<b>QTD 06/30-</b>	<b>12/31/05-</b>
<b>\$mil</b>	<b>09/30/06</b>	<b>09/30/06</b>
Domestic Common Stock	96.9	3.6
Global ex U.S. Equity	49.4	6.0
Absolute Return	22.5	3.5
Hedged Equity	30.1	1.1
Inflation Hedge	12.1	(4.2)
Non-Mkt. Alternative Assets	8.2	---
Bonds	40.7	3.7
Cash	0.7	1.3
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<b>Total Externally Managed Assets</b>	<b>260.5</b>	<b>3.2</b>
<b>Total Internally Held Assets</b>	<u>3.6</u>	<b>6.4</b>
<b>Total Long Term Investment Pool</b>	<b><u>264.1</u></b>	

The total portfolio for the University as of September 30, 2006 included the following:

Long Term Investment Pool	\$264.1 million
Wilbur Trust	20.8 million
Separately invested funds	<u>7.6 million</u>
<b>Total Endowment</b>	<b><u>\$292.5 million</u></b>

UVM returns were 3.2% for the quarter-to-date and 6.4% for the calendar year-to-date, lagging the composite index (S&P 500 75%/LB Agg 25%) for the quarter year-to-date (5.2%) by 200 bps and for the calendar year-to-date (+7.2%) by 80 bps.

Mr. Brantley mentioned the informal November 6<sup>th</sup> meeting recommendations as to the asset allocation. Recommendations made included the shifting away from US Equity through allocation of 5% to Non-US Equity and another 5% to Inflation Hedging. He explained how the current quarter was relatively good compared to the previous disastrous quarter ending June 30, 2006.

The performance update packet provided by Cambridge Associates was reviewed thoroughly with the committee to provide the newest members with background and familiarity to the information contained in the reports. The returns for the trailing 3-months showed the greater advantage of U.S. Mid to Large-Cap over Small-Cap and the REITs, an asset the University has little exposure to, topping returns at an impressive 9.3%. The returns for the trailing 12-months were extremely favorable for Global ex U.S. Equities, Emerging Markets and REITs compared to the rest in the portfolio. The trend is value dominated versus growth; especially for the Small Cap sector. The current Price-Earnings Ratio of the S&P 500 is just under one standard deviation

of the mean. The global equity market valuations show that the Non US securities are more attractive in terms of total return on equity. There was discussion on the current valuations summary with regards to REITs, secondary REITs, and these types of projections leading to choices in the investment pool. The REITs have been overvalued in the past 2.5 years, but continue to provide high returns in the market.

The Investment Returns by Manager discussion focused particularly on Longwood, with trailing returns of (7.1) QTD, (8.3) CYTD, (9.3) 1 year and a ranking of 93 for this quarter. Mr. Brantley discussed the rankings to the committee, explaining how Longwood's poor position was represented by a 93 meaning it only outperformed 7% of those in the Cambridge ranking. Mr. Brantley cited the following reasons for the manager's poor performance: stock selection (specifically in the Healthcare sector), overweight in the Technology sector, and personnel. Co-Vice Chair Cioffi reiterated that the manager was riding a period of above average returns since inception that no longer shows up on the 5 yr. trailing report. The Investment Subcommittee will be taking a closer look at Longwood and considering other alternatives as well. Mr. Brantley highlighted the importance of patience in the investment manager portfolio and used Ark's predecessor, Eagle, as an example to the issue of timing with hiring and firing managers. Trustee Hube asked about the conclusions that should be drawn from the Investment Returns by Manager. Mr. Brantley answered that it is a data point for review and monitoring in terms of selection, transfer of funds, and hiring/firing of management; which should be used in conjunction with outside factors.

Templeton was singled out due to its strong absolute and relative performance as an International Equity Manager. The Hedge Funds, as a unit, performed well in both the absolute and relative returns. The new multi-strategy hedge fund manager, HBK, hired as of the November 1<sup>st</sup> will hopefully help to capture the fund of funds market returns in the next quarter. The bond market was relatively flat compared to the benchmarks, but still contributed a solid return to the portfolio.

In the November 6<sup>th</sup> meeting of the former Investment Committee, Chair Cioffi questioned Mr. Brantley regarding portfolio allocation. The University's current asset allocation is composed of 80:20 equity to bond ratio and Mr. Brantley recommends to keep within the range of 15-20% allocation in bonds. Trustee Boyce is comfortable with the composition of fixed income and recommends no tinkering between equity and bonds with regards to the asset allocation. Chair Cioffi and Trustee Snow would like to see the 10% Inflation Hedging allocation, proposed by Cambridge Associates, to be taken from Bonds. Chair Cioffi explains that the Inflation Hedging allocation could be reached within 6-9 months and that the 5% taken from Bonds would still keep a 50-55% equity allocation, which has only been tinkered with twice this year.

A motion was passed to reduce the allocation target for U.S. Equities from 35% to 30%, increase the Global ex -U.S. Equity target from 17.5% to 22.5%, increase the Inflation Hedging target from 5% to 10%, and reduce the allocation target for Bonds from 20% to 15%.

### **Annual Review of Debt Policy**

Mr. Cowen completed his presentation on capital funding strategies from this morning. He summarized the implications of the different funding options covered on debt capacity and net assets. It is important to consider all potential funding sources and to recognize that the University's internal limits and guidelines, while important, do not represent external debt

capacity. Chair McAneny added that the committee was faced with two issues: Does the University have debt capacity and if so, how much, and what is the most efficient way to use this debt capacity, and, what are our options for growing net assets?

The discussion turned to the annual review of the debt policy. The debt policy, adopted in September 2004, prescribes that the policy will be reviewed on an annual basis and changed or revised as deemed appropriate. The only change proposed at this time is acknowledging the new committee structure, replacing "Debt Subcommittee" with "Budget, Finance, and Investment Committee" where stated in the document. Mr. Cowen provided the committee with an overview of the University's current debt policy for educational purposes. He explained that debt policies are institution-specific and provide linkage between strategic, financing and capital plans. The debt ratios, viability and debt burden, were reviewed as well as a modified viability ratio that recognized the importance of considering deferred maintenance requirements. Deferred maintenance costs, estimated at \$264 million in FY 2006, are a real liability not contained on the balance sheet. Information on the University's current debt portfolio and debt service structure was also provided.

### **Capital Project Resolution**

The committee unanimously approved the Carbon Monoxide Detection Project: \$2.22 million project is phase two of a two-phase project to install centralized carbon monoxide detection systems in all UVM-owned residence halls/sleeping quarters. The resolution is provided in full below.

#### **Carbon Monoxide Monitoring Project Resolution (Phase II)**

WHEREAS, the University intends to install centralized carbon monoxide monitoring systems in all its residence halls and sleeping quarters; and

WHEREAS, on February 11, 2006, the Board of Trustees approved Phase I of the installation; and

WHEREAS, Phase I was completed during the summer of 2006, and the administration is ready to proceed with planning and implementation of Phase II; and

WHEREAS, the University has adopted its Commercial Paper Note Resolution (the "Resolution") on November 13, 2004, and thereby established a commercial paper program; and

WHEREAS, it may be beneficial to obtain internal or external interim financing, including the use of commercial paper, until bonds can be issued at the appropriate time for the installation;

NOW THEREFORE, BE IT RESOLVED, that the President and Vice President for Finance and Administration and University Treasurer, or their successors or designees, are hereby authorized to commence Phase II of the Carbon Monoxide Monitoring Project, and to execute any and all contracts and documents necessary to undertake the Project at a total project cost not to exceed \$2,100,000;

BE IT FURTHER RESOLVED, that the President and Vice President for Finance and Administration and University Treasurer, or their successors or designees, are hereby authorized to obtain internal or external interim financing, including the use of commercial paper, until bonds can be issued for the project; and

BE IT FURTHER RESOLVED, that the external interim financing, including the use of commercial paper, shall be in an amount not to exceed \$2,220,000, included in which shall be Costs of Issuance, as that term is defined in the Resolution, in an amount not to exceed \$45,000, and capitalized interest in an amount not to exceed \$75,000; and

BE IT FINALLY RESOLVED, that the Secretary or Assistant Secretary will provide certificates of incumbency, as required, showing the names and signatures of those persons appointed to any of the positions heretofore mentioned, and further, that any officer of this corporation is hereby authorized to certify this resolution to whom it may concern; and

WHEREAS, the University expects to pay certain expenditures (the "Reimbursement Expenditures") in connection with the Project before the issuance of indebtedness for the purpose of financing costs associated with the Project on a long-term basis; and

WHEREAS, the University reasonably expects that debt obligations in an amount not expected to exceed \$2,220,000 will be issued and that certain of the proceeds of such debt obligations will be used to reimburse the Reimbursement Expenditures; and

WHEREAS, Section 1.150-2 of the Treasury Regulations requires the University to declare its reasonable official intent to reimburse prior expenditures for the Project with proceeds of a subsequent borrowing;

NOW, THEREFORE, the University of Vermont declares:

Section 1. The University of Vermont finds and determines that the foregoing recitals are true and correct.

Section 2. This declaration is made solely for purposes of establishing compliance with the requirements of Section 1.150-2 of the Treasury Regulations. This declaration does not bind the University to make any expenditure, incur any indebtedness, or proceed with the Project.

Section 3. The University hereby declares its official intent to use proceeds of indebtedness to reimburse itself for Reimbursement Expenditures.

Section 4. This declaration shall take effect from and after its adoption.

### **Acceptance of Gifts and Grants**

The resolution to accept gifts and grants was approved unanimously by the committee for recommendation to the full Board.

### **Acceptance of Gifts and Grants**

RESOLVED, that the Board of Trustees hereby accepts gifts in the amount of \$3,693,777.00 for the period July 1, 2006, through September 30, 2006, and grants and contracts in the amount of \$27,803,281.00 for the period July 1, 2006, through September 30, 2006.

### **FY 2008 State Capital Appropriation Request**

Vice President Gower reported that the Commission on Higher Education Funding (CHEF) had met in consultation and that the Vermont State Colleges all agreed to the asking amount of \$4,000,000; which was the same amount requested for FY 2007. The University received \$1,700,000 in funding for FY 2007. Board Chair Lisman explained that the CHEF agreement minimizes competition amongst colleges for state funding.

The following resolution was approved unanimously by the committee for recommendation to the full Board.

### **State Capital Appropriation Request - Fiscal Year 2008**

RESOLVED, that the President be and hereby is authorized to request \$4,000,000 from the Governor and Legislature of the State of Vermont toward construction, renovation, and major maintenance in advancement of the mission of the University of Vermont.

### **Summer Session Tuition Rates**

This is the final of five annual rate increases to normalize the summer tuition rates with the other semester rates. The summer session (summer 2007) is an increase of \$26 (6.8%) to \$410 per credit hour for in-state students and \$94 (10.0%) to \$1,034 for out-of-state students. The proposal to increase summer tuition required a decision at this time in order to communicate to the various marketing channels. There have been measurements to study the effect of the tuition increase on enrollment, which have shown non-degree student enrollment has decreased. Trustee Hudson-Wilson posed the question of what were the expectations of the summer program; specifically relating to the correlation to increase in tuition price and the decrease in non-degree student enrollment. Student Representative Haggerty asked whether the tuition increase for the summer would be at the current rates or at next academic year's rates. Co-Vice Chair Cioffi explained that the summer increase in rates would be at the current academic year's rates.

The resolution to increase summer session tuition rates 6.8% for Vermont students and 10% for out-of-state students was approved unanimously by the committee for recommendation to the full Board.

### **Summer Session Tuition Rates**

RESOLVED, that the Board of Trustees hereby approves increases in tuition for the Summer Session from \$384 to \$410 per credit hour for in-state students and from \$940 to \$1,034 per credit hour for out-of-state students. The increases are to become effective with the 2007 summer session.

## **Creation of Investment Subcommittee and Appointment of Members**

The resolution to create an Investment Subcommittee and appoint its initial members: Trustees Robert Cioffi, Chair; John Snow; Ian Boyce; Susan Hudson-Wilson, and Thomas Little was approved unanimously by the committee for recommendation to the full Board.

### **Resolution Approving Creation of Investment Subcommittee and Appointment of its Initial Members**

RESOLVED, that the Board of Trustees hereby establishes an Investment Subcommittee of the Committee on Budget, Finance, and Investment and charges it with the oversight of investment management decisions as set forth in the charge herein stated between regular meetings of the full Committee and such other duties as may be delegated by the Committee.

BE IT FURTHER RESOLVED, that the initial members of this Subcommittee will be Robert Cioffi, chair; John Snow; Ian Boyce; Susan Hudson-Wilson, and Thomas Little.

#### **Subcommittee Charge**

The Subcommittee shall have responsibility for oversight, hiring, and termination of managers and advisors engaged for the investment of the University's Long-term Investment Pool, and shall report on these actions at regular meetings of the Budget, Finance, and Investment Committee ("the Committee").

The Subcommittee shall be responsible for making adjustments to individual investment allocations to conform to the University's asset allocation policy as recommended by the Committee and approved by the Board. The Subcommittee shall also review the asset allocation policy and make recommendations to the Committee for its consideration at least once annually.

Notwithstanding the foregoing, the Subcommittee shall, between meetings of the Committee, make decisions relating to investment managers and investments that are necessary in the best interests of the University. Any such decisions shall be reported to the Committee and its next regular or special meeting.

The Subcommittee shall oversee the work of the University Treasurer with respect to execution of investment decisions and cash management policies in regards to the Limited-Term Investment Pool.

The Subcommittee will exercise its charge in a manner consistent with University governance, including the Board's reserved rights and delegations of authority.

## **Process for Action on Socially Responsible Investing Requests**

The Committee on Socially Responsible Investing (CSRI) has been eliminated as a result of the Board's reorganization of committees. The Budget, Finance and Investment Committee will take on the responsibility formally managed by the CSRI for requesting from the community items

for consideration. As needed, the committee will appoint workgroups to study issues and report back.

It was proposed that the committee would call for issues from the University community twice each year and would appoint ad hoc committees to address issues as needed. The Treasurer was directed to make the first call to the community.

### **Vice President's Report**

Due to time constraints, Vice President Gower referred the committee to written reports provided in the Board materials on the following topics: FY 2006 Treasurer's Report; FY 2007 Budget Status; Treasury Operations; FY 2008 Budget Planning; Capital Projects Report; and PeopleSoft Update.

### **Other Business**

There was a quick meeting assessment for committee members to provide feedback on the new Budget, Finance, and Investment Committee structure. The feedback was as follows: people enjoyed the discussion versus presentation format and the leadership of staff and Board, and believed improvement was needed in the area of timing to encourage active debate.

### **Adjournment**

There being no further business, the meeting was adjourned at 3:35 p.m.

Respectfully submitted,

Deborah McAneny, Chair