The Regents of the University of California

**COMMITTEE ON INVESTMENTS**
November 15, 2000

The Committee on Investments met on the above date at Covel Commons, Los Angeles campus.

Members present: Regents Atkinson, Bagley, Davies, Hopkinson, S. Johnson, Leach, Miura, and Parsky; Advisory member T. Davis

In attendance: Regents Bustamante, Fong, O. Johnson, Khachigian, Kohn, Kozberg, Lee, Montoya, and Preuss, Regents-designate Morrison and Seymour, Faculty Representatives Cowan and Viswanathan, Secretary Trivette, General Counsel Holst, Interim Treasurer Bowman, Assistant Treasurer Stanton, Provost King, Senior Vice Presidents Darling and Mullinix, Vice Presidents Broome, Drake, Gurtner, Hershman, and Saragoza, Chancellors Berdahl, Bishop, Cicerone, Dynes, Greenwood, Orbach, and Yang, Vice Chancellor Desrochers representing Chancellor Tomlinson-Keasey, and Recording Secretary Nietfeld

The meeting convened at 3:05 p.m. with Committee Chair Hopkinson presiding.

1. **READING OF NOTICE OF MEETING**

For the record, it was confirmed that notice had been given in compliance with the Bylaws and Standing Orders for a Special Meeting of the Committee on Investments to be held concurrently with the regularly scheduled meeting of the Committee for the purpose of selecting a private equity consultant.

2. **APPROVAL OF MINUTES OF PREVIOUS MEETING**

Upon motion duly made and seconded, the minutes of the meeting of September 14, 2000 were approved.

3. **PROPOSED REVISION OF PROXY POLICY: DIRECTLY INVESTED AND INDEX FUNDS**

The Interim Treasurer recommended that the following proxy policy be adopted and that the proxy policy implemented by the Office of the Treasurer as of December 15, 1994 be rescinded:

A. In general, but with certain exceptions, proxy issues that are of a routine business management nature, such as election of directors and appointment of auditors, are voted in accordance with the recommendations of management.

B. Business and social issues of a more controversial nature will be reviewed on a case-by-case basis and will generally be voted according to the Treasurer's Office Guidelines (attached).

C. The Regents may review and revise the Guidelines at any time or elect to vote a specific way on any particular issue that may arise.

D. The Treasurer will continue to directly vote proxy items for all companies held in the actively-managed equity portfolios, according to the Guidelines.

E. For the Russell 3000 and MSCI index funds, The Regents shall adopt a customized voting arrangement with State Street Global Advisors (SSgA) and its proxy advisor, Institutional Shareholder Services (ISS).[1]

F. SSgA and ISS will use the Guidelines in the voting of proxies.

G. Voting process:

   a. For all shares held in the actively-managed equity portfolios, the Treasurer will vote all proxies directly, in accordance with the Guidelines;

   b. For all shares held in the Russell 3000 index fund in those companies that are also held in the actively-managed equity portfolios, the Treasurer will review ISS's recommended vote and either accept or override that vote in order to provide consistency with its own vote on the shares held in the actively-managed portfolios;

   c. For all shares in companies held only in the Russell 3000 index fund, ISS will vote all proxies directly, in accordance with the Guidelines.

   d. For all shares in the MSCI EAFE index fund, SSgA will vote The Regents' shares according to the recommendations of its proxy committee.[2]

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[1] ISS is an established organization with expertise in the proxy voting and corporate governance fields used by numerous large institutions, including State Street, CalPERS, and CalSTRS.

[2] This area requires more specialized analysis for which the Treasurer's Office does not have current guidelines. Over time, a set of specialized foreign guidelines could be established by The Regents and included in the customized policy if so desired.

H. SSgA and ISS will provide a written summary of all proxy votes on all Regents' holdings on an annual basis.

The Committee was informed that Interim Treasurer Bowman had recommended a review of the Regents' Proxy policy and adoption of the proposed new policy in light of the following developments:

- Potential conflict of interest matters as described by General Counsel Holst in his April 1999 memo to the members of the Board: Voting of Proxies - California Political Reform Act Disqualification.

- The increasing complexity and time-consuming nature of evaluating proxy issues.

- The inclusion of the Russell 3000 and MSCI EAFE index funds as a component of The Regents' equity portfolios.

The current proxy policy is as follows:

> In general, but with certain exceptions, proxy issues that are of a routine business management nature are voted by the Treasurer to agree with management recommendations. In cases of matters that are controversial or relate to social issues, proposals will be submitted to each Board member for an individual vote.

In accordance with this policy, the Treasurer mails to all members of the Board of Regents any proposals included in proxy statements related to matters of public interest, and the Treasurer votes the proxy on the basis of a majority of written and telephone votes received from the Regents. Historically, several Regents have had on file with the Treasurer standing instructions to vote for or against certain issues or for or against all shareholder proposals.

In April 1999, the process was amended as the Regents were advised by General Counsel of certain conflict of interest matters. This resulted in the revocation of all Regents' standing instructions. From there on, the Regents were afforded the option to give the Treasurer discretion to vote their proxies, either on specific or all social and more controversial business issues.

Over the course of the past year, the Treasurer's Office has evaluated various corporations' options and compensation policies. The Treasurer's Office subscribes to two proxy monitoring services, the Investor Responsibility Research Center and The Proxy Monitor, to enhance its ability to understand and evaluate potentially controversial items. It has been the Treasurer's policy to include background materials from independent proxy monitoring services and the corporations on the more controversial items, along with the Treasurer's Office recommendations where possible, when soliciting the Regents' votes. However, there is no real opportunity or time for the Regents to discuss individual proxy issues as they arise.

In addition to time constraints and potential conflicts of interest, the proxy process will be further complicated with the addition of the Russell 3000 and MSCI EAFE index funds. While committed to a strong proxy policy for all core long-term holdings in the equity portfolio actively managed by the Treasurer's Office, it would be impractical for the current Treasurer's Office staff to evaluate and vote proxies for the large number of securities in the Russell 3000 and MSCI EAFE index funds which are not held in the actively-managed portfolios. The proposed procedure would provide the Treasurer's Office, the index fund manager, and its proxy advisor with a set of voting guidelines, ensuring consistency across The Regents' holdings.

The Interim Treasurer believes that the recommended policy would have several benefits in enhancing a Regent's own understanding of the issues involved; mitigating potential conflicts of interest inherent in Regents' casting individual votes; and resulting in a more rationalized proxy policy and greatly simplified process, considering the numerous companies held in the index funds.

Upon motion duly made and seconded, the Committee approved the Interim Treasurer's recommendation and voted to present it to the Board.

4. **AUTHORITY FOR STATE STREET BANK AND TRUST TO INVEST REGENTS' ASSETS IN FUTURES CONTRACTS RELATED TO INDEX FUNDS**

The Interim Treasurer recommended that the State Street Bank and Trust Company (State Street), as Investment Manager of that portion of The Regents' equity portfolio to be invested by State Street in the Russell 3000 index account and in the MSCI EAFE index account under the terms of the investment management contract between State Street and The Regents, be authorized to invest in stock index futures under the following circumstances and conditions:

(1) Futures would be used only to equitize dividends and receivables that accrue to the two accounts over time, as determined on an account basis for each of the two accounts.

(2) At no time will more than 3 percent of an account's assets be held in cash or in futures contracts.

(3) Futures contract exposure will be limited to the value of cash in the account; that is, no leverage will be used.

The Committee was informed that futures and options, also known as derivatives, are instruments that allow investment managers to meet financial objectives more effectively. An interim action item was recommended by the Investment Advisory Committee and approved by the President, the Chairman of the Board, and the Chair of the Committee, giving State Street the authority to use futures contracts to achieve benchmark characteristics in The Regents' transition portfolio.

The Regents approved an asset allocation plan in March 2000 that permitted limited use of derivatives in Regents' investments. Guidelines for the Treasurer's fixed income portfolio allow for bond and currency futures, while the guidelines for the Treasurer's U.S. equity portfolio expressly prohibit the use of derivatives because they are not necessary in order to meet investment objectives. The asset allocation plan did not include specific investment policies for the portion of The Regents' equity investments which are to be managed by the investment manager, State Street Bank and Trust Company, by investing that portion of the portfolio in the Russell 3000 index fund and in the MSCI EAFE index fund.

The benefit of using futures is that there would be no disruption in the asset allocation, because unusual cash holdings resulting from the inflow of new cash can be instantly and inexpensively invested in futures that help replicate the performance of the Russell 3000 and MSCI EAFE indices. This would enable State Street to be fully accountable for matching the performance of the respective indexes.

The Interim Treasurer recommends that State Street be granted the authority to use futures contracts beyond the transitional period of November 1 through December 31, 2000. The recommendation has been reviewed by Wilshire Associates, and it recommends adoption.

Upon motion duly made and seconded, the Committee approved the Interim Treasurer's recommendation and voted to present it to the Board.

## 5. SELECTION OF PRIVATE EQUITY CONSULTANT

It was recommended that, following a presentation by the finalist, Cambridge Associates, The Regents select Cambridge Associates to provide private equity consulting services to The Regents.

**Summary of the Evaluation Committee Report**

Office of the President Procurement Officer Haskins, under the direction of Senior Vice President Mullinix, coordinated the selection process. The evaluation committee consisted of the following three members:

Professor Francis Longstaff, Anderson School of Management at UCLA
Mr. Kenneth Wisdom, Private Equity Officer, Office of the Treasurer
Mr. Harry Turner, Managing Director of Private Equity, the Stanford Management Company

Eleven Requests for Proposals (RFPs) were sent out to a list of candidates proposed by Wilshire Associates and further expanded with the assistance of the Treasurer's Office. Four responses were received.

The evaluation committee was asked to evaluate the proposals based upon detailed information on the firm's structure and organization, assets under management, alignment or conflict of interests, client base, personnel, resources, investment philosophy, investment process, allocation issues, and the estimated advisory service fees. Each committee member was asked to use a scorecard matrix to standardize the evaluation of each proposal. The scorecard is a matrix used for all major Treasury and banking vendor contracts, and the specific criteria were adopted from the disclosure requests in the private equity Request for Proposals for consulting services drafted by Wilshire Associates. Wilshire Associates was not asked to review the responses to the private equity consultant RFP due to potential conflicts of interest.

Based upon the scorecard, the evaluation committee ranked the candidates and presented the top firm to Senior Vice President Mullinix and Interim Treasurer Bowman for review. Both approved the selection and forwarded their recommendation to the Investment Advisory Committee at its October 17, 2000 meeting.

The private equity consultant will have a non-discretionary advisory relationship, ultimately reporting to the Board of Regents of the University of California. The consultant, while independent, will work with the Treasurer's Office private equity staff and assist the Treasurer's Office with the management of the private equity portfolio. The consultant will advise the Investment Advisory Committee and report to the Committee on Investments and The Regents in proposing overall strategy and individual private equity investments. Only those investments that have been recommended by both the Treasurer and the Consultant will be presented for consideration to the Investment Advisory Committee for approval by The Regents.

The fee proposed for the first year is $650,000.

**Presentation by Cambridge Associates**

Senior Vice President Mullinix introduced the representatives of Cambridge Associates, Ms. Jennifer Urdan and Mr. Lindsay Van Voorhis. Mr. Mullinix conveyed the regrets of Mr. Jim Baily, a co-founder of Cambridge Associates, who was not able to attend today's meeting.

Ms. Urdan summarized the Cambridge Associates presentation which had been distributed to the Committee. The mission of the firm is to provide its clients with thoroughly researched and independent advice. Cambridge Associates was established in 1973 as the result of a study of endowment management practices conducted for Harvard University. It provides investment consulting and financial planning services to over 600 clients, largely non-profit. The firm employs more than 440 employees in four offices. The firm does not have discretion over assets, but it takes an active role in its consulting relationships. The clients make final decisions on investment choices. She drew the Committee's attention to Cambridge's diverse list of clients with more than $1 billion in investments.

Ms. Urdan outlined the firm's distinctive strengths, which include a commitment to nonprofit institutions and alternative assets. Its clients' satisfaction is reflected in a 94 percent renewal rate for 1999. Cambridge is not affiliated with any financial institution and does not sell products or services to investment management firms.

Mr. Van Voorhis reviewed the section of the presentation which depicted the returns which can be obtained from investments in private equity, emphasizing the importance of the selection of the private equity manager. He stressed the firm's ability to rate the various venture capital funds. He reviewed the factors which constitute a successful approach to alternative assets investing, including access to top-tier funds, continuous identification of opportunities, emphasis on the strengths of the institution, and quick turn around on fund placement. In contrast, unsuccessful programs are characterized as taking a passive approach to investing and lacking a defined plan.

In implementing an alternative assets investment program, it will be necessary to set investment objectives and long-term asset allocation strategies, as well as to develop a written plan outlining allocations to specific alternative categories. On the implementation side, the University will need to establish a list of investment opportunities which will change over time and introduce the institution to the fund managers. Cambridge will provide ongoing information on how the funds perform.

Ms. Urdan continued that Cambridge advises its clients to diversify by time, by strategy, and by sector. The Regents' investments should be directed towards the top-performing managers. She drew the Committee's attention to the consulting team structure which is designed to provide The Regents with the expertise and resources necessary to meet its investment needs.

In response to a question from Regent Hopkinson, Ms. Urdan explained that the development of the fee schedule was based on the information that was provided in the RFP. Cambridge applied its fee schedule to the work it estimated would be performed in years one, two, and three of the contract. Cambridge also assumed that the performance monitoring would be done by The Regents and the Treasurer's Office. The fee structure includes an investment planning review of Regents' current and proposed investments, as well as attendance at six meetings per year, including attendance at Investment Advisory Committee meetings that are concurrent with Regents meetings. The basic fee will also cover the fact sheets issued by the firm and general research on the asset class.

Regent Parsky emphasized the importance of written recommendations from Cambridge Associates with respect to all private equity commitments. In addition to the responsibilities outlined in the RFP, the Regents will also be interested in receiving an annual statement of investment strategy. The Regents will wish to review the sourcing of high-quality managers in the marketplace and receive a due diligence report. In terms of the contract, Regent Parsky believed that it would be in the best interest of The Regents to review the contract on an annual basis. It should be subject to termination on thirty days' notice.

In response to a question from Regent Bustamante, Committee Chair Hopkinson recalled that the asset allocation plan sets the performance for the private equity fund at the Russell 3000 plus three percent.

Regent Bustamante asked who would be held accountable for the program's performance. Regent Hopkinson responded that the Office of the Treasurer was responsible for making investment decisions, with the advice of Cambridge Associates. Interim Treasurer Bowman pointed out that the measurement of the success of a consultant is largely subjective for the first few years of the program. It is possible, however, to judge how valuable the firm's information has been. Once an investment has been made in a fund, one can tell fairly soon how well the fund will perform.

Regent Bustamante questioned the validity of retaining a firm whose performance cannot be measured in the short term. Regent Preuss suggested that the performance would be judged by the type of information provided by Cambridge Associates to enable The Regents to make better investment decisions.

Interim Treasurer Bowman believed that the retention of Cambridge Associates was analogous to hiring capable staff in the Office of the Treasurer. The firm will be evaluated on the quality of its recommendations. The goal of achieving the results of the Russell 3000 plus three percent is based upon the experience of investments made in this asset category. Regent Hopkinson added that this expectation had been adopted as a part of the asset allocation plan.

Regent Preuss recalled that the Office of the Treasurer had presented a discussion on the value of the relationships between The Regents and its venture capital partners. The presentation by Cambridge Associates referred to the firm's role in introducing the University to various firms. He asked for comment on the service that Cambridge would be providing in that area. Mr. Van Voorhis responded that Cambridge would help to identify the superior funds and introduce staff in the Treasurer's Office to them. Cambridge would also support the University as a long-term, stable investor in the fund. Ms. Urdan stressed that Cambridge is able to provide good advice because of its lengthy experience in the field and its knowledge of which funds are coming on the market.

Regent Parsky noted that prior to the adoption of the asset allocation plan the Treasurer had invested approximately three percent of the portfolio in private equity. During the review of the asset allocation strategy, it was determined that the allocation to this investment category should be increased to five percent of the portfolio. The selection of a private equity consultant is part of the process of implementing this decision. This action is consistent with the approach taken by most public pension funds in seeking outside expertise in the area of private equity. Because the Treasurer's Office is not fully staffed in this area, the Regents recognized the need to retain an outside consultant to assist in maintaining partnerships and developing new ones.

Upon motion duly made and seconded, the Committee approved the recommendation and voted to present it to the Board.

## 6. UPDATE ON ASSET ALLOCATION PLAN IMPLEMENTATION

Interim Treasurer Bowman recalled that the transition plan for The Regents' portfolios contains a time line for bringing the portfolios into compliance by December 31, 2000. The funding of the Russell 3000 and MSCI EAFE index funds began on November 1, and full compliance is on track for December 31, 2000. The one exception is the extension to June 30, 2000 for reducing the duration of the bond portfolios. It is anticipated that the reduction will actually occur prior to June 30.

The University of California Retirement Plan (UCRP) and the General Endowment Pool (GEP) are in full compliance with all of the asset allocation targets. The only major difference between the two funds is in private equity. UCRP's current percentage of private equity is slightly above the minimum of the allowed range. As such, UCRP will be allocated the majority of all future commitments to private equity partnerships in order to achieve the target allocation. GEP is at the target allocation and will continue to receive allocations to future partnership commitments in order to maintain its weighting, but at a slower pace than in prior years. The 403(b) equity fund is in compliance with all asset class targets except for private equity.

Mr. Jeff Heil, Head of Equity Investments, recalled that when he reported to the Committee in September, the main area of compliance affecting the equity fund portfolios was the funding of the Russell 3000 index fund. The transfer of cash and securities to fund the Russell 3000 and MSCI EAFE index funds in UCRP, GEP, and the equity fund occurred on November 1, 2000. The total actual dollar amount transferred to the index fund manager for investment in the index funds was $11.6 billion, with $8.3 billion designated for the Russell 3000 fund and $3.3 billion for the MSCI EAFE fund. The primary effect on the securities under active management was to position the portfolios to the correct weightings in the various industry sectors versus the Russell 3000 security weightings. The equity portfolios are now in compliance with all of the new portfolio guidelines.

Mr. Randy Wedding, Head of Fixed Income, reported that since the last meeting the Treasurer's Office had come into compliance with the portfolio guidelines that constrain investment in emerging market, high-yield, and securities issued by foreign issuers. The Office is now in compliance with the 25 percent guideline in these three portfolios. The Office is within two percent of the guideline level of ten percent for non-dollar securities. Mr. Wedding was confident that this objective would be met by December 31. He reported that since May the bond duration for UCRP had been reduced from 11.6 to 10.3 years. The benchmark level is 7.7 years, plus or minus 20 percent. The market will be allowed to dictate when full compliance is reached. A progressive decline in interest rates over the year had resulted in a more rapid reduction in bond duration that was originally anticipated. The bonds should be at the top of the range by the first quarter of 2001. Once compliance has been achieved, it will be necessary to determine from a portfolio management standpoint whether the duration should be at the target.

Regent Bustamante asked when investments would be made in tobacco stocks as part of the transition to the index funds. Interim Treasurer Bowman noted that the University has no investments in tobacco. The Regents' investment in the indices will be on a security-by-security basis. There has been no investment in tobacco stocks by the University in either the Russell 3000 or the MSCI EAFE index fund.

Mr. Steve Nesbitt of Wilshire Associates continued that the transition to the index funds will be completed by December 31, 2000. The decision to exclude certain stocks from the indices ideally should be made before then, but it could be postponed. Mr. Bowman noted that if no decision is made by the end of the year, it may be necessary to revise the guidelines by which the performance of the indices will be measured, but this performance should not be affected to any significant extent by the delay. This would allow The Regents to make a decision about the investment in tobacco stocks at the January 2001 meeting. Regent Bustamante suggested that it would be wise for The Regents to make this decision now in order to give direction to the Treasurer. Regent Hopkinson noted that no action was scheduled for this matter at today's meeting.

Mr. Nesbitt reported that any decision to exclude stocks from The Regents' portfolio raises the issues of risk and return. The Regents must evaluate whether or not the decision to exclude stocks will have an impact on either. The objective of an index fund is to track a specific index. If certain stocks are excluded, it becomes more difficult to track the index.
Regent Bustamante asked whether it was Mr. Nesbitt's professional opinion that the Regents could maintain their fiduciary responsibilities while excluding tobacco stocks from the index fund. Mr. Nesbitt recalled that certain stocks were removed from the portfolios when The Regents divested from South Africa and substitute investments were made. Each decision must be made on a case-by-case basis. It may be possible to identify stocks to substitute for tobacco stocks in the index funds, but they will not be perfect substitutes. It depends upon the type of stocks one wishes to

eliminate. No stocks are eliminated from The Regents' actively managed portfolios for any basis other than return.

Regent Hopkinson recalled that The Regents chose to invest in an index fund in order to diversify the portfolios. A passively managed index fund is less expensive than the use of outside managers or hiring new staff. As stocks are excluded from the index fund, the Regents become active managers. The elimination of one or two minor stock types should not have a significant effect on the fund's performance.

Mr. Bowman noted that analysts in the Treasurer's Office evaluate each investment in the actively managed portfolios. Any decision to purchase or sell is based on forecasts of future earnings. The staff has found that the risk involved in investing in companies that produce tobacco products has been unacceptable. No individual analyses are made, however, with respect to investment in an index fund. He believed that to do so would negate the fundamental purpose of an index fund, which is to replicate the performance of the economy from which the securities are taken.

Chairman Johnson asked how the exclusion of certain stocks would affect the fund's ability to track the index. Mr. Nesbitt explained that the expectation is that The Regents' investments will track the index within plus or minus 20 basis points. If the index is at 10 percent over the course of the year, The Regents should be within 9.8 to 10.2 percent. If an industry were to be eliminated, the tracking range would increase to 9.6 to 10.4 percent, which could potentially double the tracking variation. The Regents will need to evaluate whether or not this is acceptable.

Interim Treasurer Bowman spoke to the long-term implications that could result from eliminating a stock from the portfolio. The next social issue could involve a more significant portion of the index fund.

Regent Montoya asked whether there was a trend of index funds withdrawing from tobacco stocks based on poor performance. Mr. Bowman noted that the Russell 3000 consists of the top 3,000 companies in the United States based upon capitalization, which is a function of the number of shares issued and their market value. If tobacco companies fell out of the top 3,000 companies, they would not be included in the indices.

Regent Fong asked why The Regents' index fund would not match the performance of the Russell 3000. Mr. Nesbitt explained that the objective is to match the return of the Russell 3000, but there is a margin of error because the index manager is not expected to replicate exactly all 3,000 stocks, particularly the smaller 1,000 stocks.

Secretary Trivette distributed communications received concerning the update on asset allocation plan implementation.

(For speaker's comments, see the minutes of the November 15, 2000 meeting of the Committee of the Whole.)

7. **TREASURER'S ANNUAL REPORT**

The Interim Treasurer recommended that the Committee forward to The Regents the **Treasurer's Annual Report** for the fiscal year ended June 30, 2000.

It was recalled that the Bylaws state that the Committee on Investments shall report periodically to the Board concerning the investments operations of the University. The Treasurer's Annual Report goes into detail concerning these operations.

Upon motion duly made and seconded, the Committee approved the Interim Treasurer's recommendation and voted to present it to the Board.

[The report was mailed to all Regents in advance of the meeting, and a copy is on file in the Office of the Secretary.]

The meeting adjourned at 4:15 p.m.

Attest:

Secretary

# TREASURER'S OFFICE GUIDELINES FOR PROXY VOTING*

## I. Social Issues

Issues that are controversial or relate to social issues (i.e., tobacco issues, animal testing, military contracts, etc.) are reviewed on a case-by-case basis in light of their potential long-term economic impact on shareholders, along with ongoing review of company codes of conduct and social responsibility, any existing UC policies, and the advice of independent proxy monitor services. This may result in a vote against management if the company is not reasonably responsive to shareholder concerns.

## II. Corporate Governance

**The Treasurer's Office recommends the following:**

A. Classified Board (or staggered board proposals)
The Treasurer's Office recommends annual elections for directors and that classified boards not be allowed, as they tend to entrench management.

B. Cumulative voting or restoration of cumulative voting issues.
In general, the Treasurer's Office recommends a vote in favor of cumulative voting. California law allows companies incorporated in the state to eliminate cumulative voting with shareholder vote.

C. Preemptive Rights: restoration of limited preemptive rights.
Normally good for shareholders, the Treasurer's Office recommends a vote in favor.

D. Confidential Voting Issues.
The Treasurer's Office recommends a vote with management, as existing voting safeguards are normally adequate to protect shareholder interests.

E. Authorization of blank check preferred (poison pill): The Treasurer's Office recommends a vote against these anti-takeover measures as they overtly entrench management and have specific anti-takeover intent.

F. Fair price super-majority proposals; the Treasurer's Office recommends a vote against supermajority proposals of 85 percent or more.

* Company-specific issues, such as past performance, shareholder responsiveness, etc. may result in a deviation from the standard recommendation.

G. Golden Parachutes: The Treasurer's Office recommends a vote against these incentives for management, as they are usually overly-rich rewards for executives upon a takeover of the company.

## III. Compensation Issues
**The Treasurer's Office recommends the following:**

A. Stock option plans resulting in over 10 percent dilution shall be examined on a case-by-case basis to determine the dilution in the context of the peer group and norms. Plans with excessive dilution may be voted against.

B. Stock options for non-employee directors are examined on a case-by-case basis. Excessively rich plans for non-employee directors, where the annual payments exceed the average for its peer group may be voted against.

C. Compensation for non-employee directors which takes the form of retirement payments are normally voted against.

D. Exchanging underwater options (granting lower-priced options to replace higher-priced options) issues are normally voted against.

E. Granting stock options to executives to be exercised at less than fair market value are normally voted against.

F. Employee Stock Purchase Plans normally are voted in favor as they involve a purchase of common shares at 15 percent of market value through payroll deduction. Plans at discounts of more than 85 percent (although there are very few) are examined on a case-by-case basis.