The Regents of the University of California

COMMITTEE ON INVESTMENTS
September 21, 2006

The Committee on Investments met on the above date at the UCSF–Mission Bay Community Center, San Francisco.

Members present: Regents Blum, Dynes, Moores, Parsky, Pattiz, Schilling, and Schreiner; Advisory member Oakley

In attendance: Regents Coombs, De La Peña, Gould, Hopkinson, Island, Johnson, Kozberg, Lansing, Marcus, Preuss, Ruiz, and Varner, Regents-designate Allen, Brewer, and Bugay, Faculty Representative Brown, Acting Secretary Shaw, Acting General Counsel Blair, Chief Investment Officer Berggren, Provost Hume, Executive Vice President Darling, Vice President Broome, Chancellors Bishop, Fox, Vanderhoef, and Yang, Acting Chancellor Blumenthal, and Recording Secretary Nietfeld

The meeting convened at 12:40 p.m. with Committee Vice Chair Schilling presiding. She recalled that a quorum had not been present at the August 24, 2006 joint meeting of the Committee on Investments and the Investment Advisory Committee, and thus the action items from that meeting would be taken up at today's meeting.

1. **APPROVAL OF MINUTES OF PREVIOUS MEETING**

Committee Vice Chair Schilling informed the Committee that the minutes from the August 24, 2006 meeting were not available for approval.

2. **REAL ESTATE PORTFOLIO INVESTMENT GUIDELINES**

The Chief Investment Officer recommended, and Richards & Tierney concurred, that the attached Investment Guidelines for Real Estate investments for the University of California Retirement Plan (UCRP) and General Endowment Pool (GEP) be approved. These revised guidelines are to be effective immediately.

Chief Investment Officer Berggren recalled that The Regents had approved a 5 percent allocation to Real Estate (RE) in both the UCRP and GEP in May 2003. At that time, Investment Guidelines for both public and private real estate were approved. The Office of the Treasurer began to implement the RE allocation in late 2004, and at that time recommended modified investment guidelines. With the addition of a Director of Real Estate and a new strategy for implementing the allocation, additional modifications are recommended.

Chairman Parsky observed that amending investments guidelines was not an insignificant act by The Regents. He believed that it would be important to have a statement in writing from Richards & Tierney that that Office of the Chief Investment Officer has the capability to carry out the new guidelines. The same request would apply to the proposed guidelines for Absolute Return.

Upon motion duly made and seconded, the Committee approved the Chief Investment Officer's recommendation and voted to present it to the Board.

3. **ABSOLUTE RETURN STRATEGIES INVESTMENT GUIDELINES**

The Chief Investment Officer recommended, and Richards & Tierney concurred, that the attached Investment Guidelines for Absolute Return Strategies for the University of California General Endowment Pool be approved. These revised guidelines are to be effective immediately.

It was recalled that in May 2006, The Regents approved a new asset allocation policy for the General Endowment Pool in which the portion of the GEP invested in Absolute Return (AR) strategies was increased from 10 percent to 15 percent. The Committee had previously asked the Treasurer to develop a plan to modify the AR portfolio, which would continue to be diversified but also be balanced across a broad range of strategies, including higher-volatility, equity-type strategies which offer higher expected returns. These proposed investment guidelines are necessary to implement a larger allocation to AR strategies.

In order to implement this strategy, the Chief Investment Officer recommends, and Richards & Tierney concurs, that several guidelines be modified or added, the purpose of which is to reduce concentration risk and allow a more globally diversified portfolio. These changes include:

- Reduction of the permitted ranges around target allocations of the principal sub-strategies within AR strategies
- Clarification on the limitation of the use of leverage for the total AR portfolio
- Limitation on the percentage of underlying investments in emerging market securities
- Expansion of the limit on the percentage of underlying investments in Non-U.S. securities (developed and emerging markets)

Upon motion duly made and seconded, the Committee approved the Chief Investment Officer's recommendation and voted to present it to the Board.

4. **PROPOSED POLICY ON LEGAL PROCEEDINGS RELATED TO INVESTMENTS OF THE UNIVERSITY OF CALIFORNIA**

The Chief Investment Officer and The Regents' investment consultant Richards & Tierney recommended that a policy be adopted regarding the initiation of legal proceedings relating to investments of or managed by the University of California. In the proposed policy, jurisdiction over initiation of litigation relating to investments of or managed by the University of California will be shifted from the Committee on Finance to the Committee on Investments.

It was recalled that it is the practice of the General Counsel to seek approval of the Board of Regents before initiating significant litigation. Because the General Counsel is under the general jurisdiction of the Committee on Finance, the General Counsel has submitted recommendations to initiate litigation to that committee for consideration and recommendation to the Board. In addition, where emergency action must be taken to protect the interests of the University prior to the next meeting of the Board, the General Counsel has, pursuant to the Regents' Policy on Interim Authority, sought approval from the Chairman of the Board or the Chair of Finance before initiating suit.

Since 2001, the University has been involved as a plaintiff in four lawsuits seeking compensation for damage to the University's investments arising from alleged violations of federal and State securities laws. In 2002, the University sought and obtained lead plaintiff status in two federal class actions. In 2003, the University initiated two suits on its own behalf separate from on-going class actions. All of these actions seek compensation which, if obtained, would be paid to the University's investment funds. Furthermore, the University's investment funds are responsible for any unreimbursed costs the University may incur in connection with the litigation. Under retention agreements with outside counsel, counsel is responsible for litigation costs it incurs, which are reimbursed from any recovery. The University has thus far been successful in the class actions in recovering its own out-of-pocket costs from the class settlement funds. Because the costs and benefits of such litigation are to the University's investment funds, it is recommended that jurisdiction over lawsuits in this area be shifted from the Committee on Finance to the Committee on Investments.

Upon motion duly made and seconded, the Committee approved the Chief Investment Officer's recommendation and voted to present it to the Board.

5. **REGENTS' INVESTMENT POLICY WITH RESPECT TO UC CAMPUS FOUNDATIONS**

Committee Chair Wachter has recommended that the following investment policy for the UC Campus Foundations be approved.

INVESTMENT POLICY FOR THE UC CAMPUS FOUNDATIONS

The Regents' generalist investment consultant shall conduct an annual review of each Campus Foundation's investment policy and performance, including:

- Asset allocation relative to its policy, and
- Performance by asset class and relative to its benchmarks,
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and provide a report to the Committee on Investments annually on their findings.

In addition, on a one-time basis, to be completed within the Fiscal Year 2006-2007, The Regents' investment consultant will review the written investment policies and governance structure of each Foundation to ensure that each set of written policies includes, at a minimum:

- Asset allocation target percentages,
- Ranges for each asset class,
- Policy benchmarks for each asset class and in total, and
- Investment guidelines for each asset class.

Foundations that seek the investment returns and risk profile of the General Endowment Pool) are encouraged to adopt the investment policies and guidelines of the GEP. If any Foundation's policies differ materially from those of the GEP, the Foundation is required to explain the differences to The Regents' generalist investment consultant.

The Regents' generalist investment consultant shall review, initially and at the time of any change, each Foundation's asset allocation policy. In the case that a Foundation's target asset class weights are (or will be) outside the ranges currently set annually for the GEP for the next fiscal year, the Foundation is required to explain its rationale to The Regents' generalist investment consultant. The Regents' generalist investment consultant will then provide an assessment and recommendation to the Committee on Investments, at the next scheduled meeting of the Committee on Investments. As long as an exception to The Regents' investment policies continues, it will be re-evaluated by The Regents' investment consultant on an annual basis.

If any Foundation makes changes to its policy (asset allocation percentages and/or benchmarks), it must communicate such change to The Regents' generalist investment consultant before such change can be effective.

This policy is to be effective immediately.

The Committee was informed that the intention of the policy would be to clarify the fiduciary responsibility of The Regents with respect to UC Campus Foundations. The General Counsel has determined that The Regents has ultimate fiduciary responsibility over all investments of the University, including those of the Campus Foundations. In order to demonstrate proper oversight of the Foundations' investment portfolios, the above Investment Policy is proposed.

Regent Hopkinson was concerned that the policy did not explicitly state that The Regents would approve the asset allocation ranges for the foundations. Chief Investment Officer Berggren recalled that each of the foundations is required to be knowledgeable about The Regents' asset allocation policies and, in most instances, should adhere to them. If, for some reason, there is a specific, supportable reason for a campus foundation to be outside the asset allocation policies, the exception must be reviewed by the Committee and by the investment consultant.

Chairman Parsky saw the need for the policy to be rewritten to reflect the fact that The Regents set the asset allocation plan for the GEP. Each foundation must be in compliance with that plan unless specific approval is received for an exception.

The Committee agreed that the policy should be referred back to Committee Chair Wachter and Chief Investment Officer Berggren.

The meeting adjourned at 12:45 p.m.

Attest:

Acting Secretary