

The Regents of the University of California

**COMMITTEE ON FINANCE  
COMMITTEE ON INVESTMENTS**

July 19, 2007

The Committees on Finance and Investments met on the above date at University Center, Santa Barbara campus.

Members present: Representing the Committee on Finance: Regents Blum, Brewer, Dynes, Garamendi, Gould, Hopkinson, Island, Moores, Parsky, and Wachter; Advisory member Oakley, Staff Advisors Brewer and Johansen  
Representing the Committee on Investments: Regents Blum, Brewer, De La Peña, Dynes, Marcus, Moores, Parsky, and Wachter; Advisory member Oakley

In attendance: Regents Allen, Bugay, Lansing, Lozano, Ruiz, and Varner, Regents-designate Cole, Scorza, and Shewmake, Faculty Representative Brown, Secretary and Chief of Staff Griffiths, Associate Secretary Shaw, General Counsel Robinson, Chief Investment Officer Berggren, Provost Hume, Executive Vice Presidents Darling and Lapp, Vice Presidents Foley and Sakaki, Assistant Vice President Casey representing Acting Vice President Standiford, Chancellors Birgeneau, Drake, Fox, Kang, Vanderhoef, and Yang, Acting Chancellors Abrams, Blumenthal, and Grey, and Recording Secretary Bryan

The meeting convened at 10:40 a.m. with Committee on Investments Chair Wachter presiding.

**POLICY ON CONFLICT OF INTEREST FOR INVESTMENT ADVISORY COMMITTEE MEMBERS: Amendment of Policy Establishing the Investment Advisory Committee to Clarify Duties and Disclosure Obligations**

The Committees recommended that The Regents adopt, effective immediately, amendments to the policy establishing the Investment Advisory Committee, and amendments to the Policy on Conflict of Interest Regarding Assets Managed by the Treasurer, as shown below.

**Deletions shown by strikeout; additions shown by underlining**

**Policy on Conflict of Interest Regarding Assets Managed by the Treasurer**  
Approved September 22, 2005

The Regents has adopted Investment Policy Statements for the University of California Retirement Plan and General Endowment Pool, which assign limited roles and responsibilities to investment fiduciaries, with appropriate checks and balances.

The existing governance process has avoided the potential for and the appearance of conflicts of interest with respect to the selection of individual investments or investment managers by maintaining a separation of roles and responsibilities.

The Regents' Committee on Investments, ~~with advice from the Investment Advisory Committee~~, is responsible for oversight of the management of investments on behalf of The Regents. This involves the establishment of investment policies and oversight of the management of the assets with advice from the Investment Advisory Group. These responsibilities include approving an asset allocation policy, performance benchmarks, risk budgets, and investment guidelines.

The Treasurer is responsible for implementing the approved investment policies and the development of investment processes and procedures for asset allocation, risk management, investment manager selection and termination, allocation, monitoring and evaluation, and the identification of management strategies that will improve the investment efficiency of the Fund assets.

The General Counsel is responsible for determining that the Treasurer's responsibilities for selecting investment managers have been exercised free of any efforts to influence the Treasurer's selection by individuals within the Treasurer's Office, on the Investment Advisory Group, on the Board of Regents, or with oversight responsibility for the performance of the Treasurer's Office, with a financial interest in the selection, within the meaning of the Political Reform Act. Any such efforts to influence the Treasurer's selection of investment managers by such individuals with a financial interest in the selection is expressly prohibited. In the event such a prohibited effort to influence a Treasurer's Office selection of an investment manager is identified, the General Counsel shall immediately bring the matter to the attention of the Chair of the Regents' Committee on Investments.

In order to maintain the highest fiduciary standards and to continue to comply with institutional investment best practices, this Policy explicitly separates the roles and responsibilities of various UC fiduciaries to ensure the continuance of sound investment practice and the protection against real or perceived conflict of interest, especially with regard to the selection of individual investments or investment managers. By separating the duties of investment policy-making and investment implementation, The Regents' Committee on Investments has created an institutional framework to uphold the California Political Reform Act of 1974, which provides that public officials shall not make, participate in making, or influence a governmental decision in which the official has a financial interest.

**Deletions shown by strikeout; additions shown by underlining****1999 Policy Establishing the Investment Advisory Committee:**

- Function: The Investment Advisory Committee Group shall function in an oversight and evaluative role providing advice to The Regents with respect to all aspects of the investment program establishment of investment policies and investment performance, including, but not limited to, investment strategies, polices and procedures; investment performance; investment personnel in the Office of the Treasurer; external investment advisors managers; and Office of the Treasurer budget.
- Authority: The Committee on Investments has authority under Regents Bylaw 12.5 for management of investments of the Corporation, and the Advisory Committee Group shall have no management or action authority except in the event of express delegation by The Regents or the Committee on Investments. In addition, the Investment Advisory Group shall have no authority for selection of specific investments, including the selection of investment managers or individual investments.
- Composition: The Advisory Committee Group shall have not more than nine six and not fewer than seven four members, of which not more than four nor fewer than three shall be Regents (one of whom shall be Chairman of the Committee on Investments and one of whom shall be the President of the University who may be represented by an Officer of the University who would serve as his designee). Members of the Advisory Committee and its Chairman who may be a Regent shall be appointed by the Board of Regents upon recommendation of the Nominating Committee on Governance. Membership is limited to investment professionals, faculty, and UC Foundation members not currently serving as Regents. Members of the Advisory Committee Group shall serve for an initial term of four years and may serve a second term of four years.
- Meetings: Meetings Members of the Advisory Committee Group shall be meet only as non-voting advisors in meetings of The Regents' Committee on Investments, which are noticed and conducted in accordance with the provisions of the Bagley-Keene Open Meeting Act. Meetings shall be held at least quarterly, and may be held more frequently as required, for review of investment performance and other matters.
- Reports: The Advisory Committee Group may request the Treasurer, other University of California staff, and such external sources as the Committee Group shall determine advisable to provide reports on investment matters. The Advisory Committee shall provide through its Chairman periodic reports to the Board and the Committee on Investments on the activities of the Advisory Committee.

Consultant: The Advisory Committee Group may recommend to the Committee on Investments that one or more consultants be retained from time to time to advise the Advisory Committee Group and the Committee on Investments.

Conflicts: Members of the Advisory Committee Group shall upon taking and leaving office and annually during their terms, with updates when information changes, disclose all existing and potential conflicts of interest and shall abstain from voting on any such matters. ~~the following: their status and the status of their immediate family, within the meaning of the Political Reform Act, as partners, members, executive officers or employees with any and all investment management firms, as well as any financial interests or other positions in such firms that would place them in a position to control the direction of the management and policies of the firm, through a 5% or greater ownership of voting securities, or otherwise.~~

Expenses: Members of the Advisory Committee Group shall receive no compensation for their services. They shall be reimbursed for expenses associated with service on the Advisory Committee Group in accordance with policies applicable to members of the Board.

### ***Summary of Proposed Amendments***

The proposed amendments do the following:

1. Reconstitute the Investment Advisory Committee as the Investment Advisory Group (IAG), which would be advisory to The Regents' Committee on Investments. Eligibility to serve on the IAG would be limited to investment professionals, faculty, and UC Foundation members not currently serving as Regents.
2. Clarify that the responsibilities of the IAG are to advise on the establishment of investment policies and investment performance, and do not include selection of specific investments or the selection of investment managers.
3. Require disclosure by IAG members of their financial interests in investment management firms, when these interests reach a certain threshold.
4. Require the General Counsel to take action to assure that selections of investment managers by the Treasurer's Office have been exercised free of any conflicts of interest.

At the November 1999 meeting, The Regents established the Investment Advisory Committee (IAC) to provide advice to The Regents' Committee on Investments and the Treasurer in connection with management of the investments of the Corporation. The function of the IAC was described as an "oversight and evaluative role providing advice to The Regents with respect to all aspects of the investment program."

The IAC initially met separately from the Committee on Investments. Its membership consists of seven to nine members, of which three to four are required to be Regents (one of whom is the Chair of the Committee on Investments and one of whom is the President, represented by a designee).<sup>1</sup>

In recent years, the IAC has met together with The Regents' Committee on Investments, providing advice to The Regents' Committee. Thus, membership by Regents on the IAC does not appear to be necessary, since Regents are present whenever the IAC meets. There is no reason for Regents who are members of The Regents' Committee on Investments to sit in a dual capacity at Committee on Investments meetings, serving both as members of the Committee on Investments and as members of the IAC. As a practical matter, the IAC is not functioning as a separate University Committee, but as a group of advisers to The Regents' Committee on Investments.

Accordingly, amendments are recommended to the policy establishing the IAC to reconstitute it as the Investment Advisory Group (IAG), which would be advisory to The Regents' Committee on Investments. Eligibility to serve on the IAC would be limited to investment professionals, faculty, and UC Foundation members not currently serving as Regents.<sup>2</sup>

Another development since the 1999 creation of the IAC is the Regents' 2005 Policy on Conflict of Interest Regarding Assets Managed by the Treasurer. This policy "separates the roles and responsibilities" of The Regents' Committee on Investments and the Treasurer, "in order to maintain the highest fiduciary standards" and to protect "against real or perceived conflict of interest, especially with regard to the selection of individual investments or investment managers." The 2005 policy makes clear that the Treasurer is responsible for "investment manager selection and termination, allocation, monitoring, and evaluation," among other things.

The breadth of the 1999 charge to the IAC (advice re: "all aspects of the investment program") is arguably not consistent with the separation of roles and responsibilities manifest in the 2005 Regents' policy. Accordingly, amendments are recommended to the 1999 policy clarifying that the IAC has no authority for the selection of specific investments or investment managers. The 2005 policy is also proposed to be amended to make clear that the IAG provides advice with respect to investment policies and asset allocation, but does not have ultimate responsibility for the management of investments. The primary responsibility for managing investments belongs to the Chief Investment Officer, who is charged with implementing the investment policies developed and approved by the Committee on Investments and adopted by The Regents.

These proposed amendments are consistent with current practices, in terms of the functioning of the IAC, the Committee on Investments, and the Treasurer's Office. They

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<sup>1</sup> Current outside members are Mr. David Fisher, Mr. William Hambrecht, Mr. John Hotchkis, and Mr. Charles Martin.

<sup>2</sup> References to the IAC in the Investment Policy Statements for the University of California Retirement Plan and General Endowment Pool will be changed to conform to these amendments, if they are adopted.

are designed to ensure that written policies are consistent with each other and with actual practices. The foregoing approach has worked well, and the Office of the General Counsel is not aware that any actual conflicts of interest have arisen in the exercise of their responsibilities by any of these three groups. Nevertheless, questions have been raised about perceived conflicts of interest regarding selection by the Treasurer's Office of outside fund management firms in which IAC members have had financial interests.<sup>3</sup>

Given the importance of perception issues and the ongoing commitment of The Regents and the Office of the President to assure public and employee trust, accountability, and transparency, amendments to the 1999 policy creating the IAC are proposed that require disclosure by Investment Advisory Group members of their status, or the status of members of their "immediate family"<sup>4</sup> as: "partners, members, executive officers, or employees with any and all investment management firms, as well as any financial interests or other positions in such firms that would place them in a position to control the direction of the management and policies of the firm, through a five percent or greater ownership of voting securities, or otherwise."

This disclosure would be required upon taking and leaving office as IAG members, annually during their terms, and whenever any information contained in the disclosures changes.

Choices of outside investment managers by the Treasurer's Office are already reviewed by independent investment consultants to assure that the Treasurer's Office's choices are financially sound and represent "best practices" among institutional investment fund sponsors of similar size and circumstances.

An additional amendment to the 2005 Policy on Conflict of Interest Regarding Assets Managed by the Treasurer is proposed, requiring the General Counsel to determine that there have been no efforts to influence the Treasurer's Office's selection of investment managers by anyone in the Treasurer's Office, on the IAG, on the Board of Regents, or with oversight responsibility for the Treasurer's Office, who has a "financial interest" in the selection, within the meaning of the Political Reform Act. The amendment also includes an express prohibition on any such efforts to influence the Treasurer's Office's selections. In the event such a prohibited effort to influence a Treasurer's Office selection is identified, the General Counsel shall immediately bring the matter to the attention of the Chair of The Regents' Committee on Investments. The General Counsel will work with the Treasurer's Office to establish a protocol for exercise of these responsibilities.

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<sup>3</sup> The 1999 policy currently provides that IAC members shall disclose all "existing and potential conflicts of interest". There have been no disclosures of actual conflicts by IAC members, and the General Counsel's Office is not aware of any. As reported at the May 2007 meeting, in item F9, soon after the establishment of the IAC there was an effort to require disclosure by IAC members of a broad range of financial investments, despite the absence of any conflicts posed by these investments. After one IAC member resigned, no further efforts were made to require these overbroad disclosures.

<sup>4</sup> "Immediate family" is defined under the Political Reform Act, and for purposes of this proposed policy, as: spouse, including registered domestic partner, and dependent children.

The General Counsel's Office is prepared to provide information annually to the IAG, The Regents' Committee on Investments, and the Treasurer's Office on avoiding conflicts of interest, and to respond to questions at any time from IAG members, Regents, or employees in the Treasurer's Office.

Regent Lozano stated her strong belief that disclosure should occur regardless of the level of ownership. Regent Blum concurred that normal practice is to disclose any relationship. Committee Chair Wachter pointed out that, while he agrees with the principle of an absolute zero threshold, in practice such a policy would pose difficulty. He noted that the intent is not to subject the IAG to the same level of disclosure as that of The Regents, and expressed his concern that such a disclosure policy may deter people from serving on the IAG due to the burden it places on them.

Regent Lozano suggested an amendment that, due to the complexity of the issue, the disclosure of conflicts portion of the proposal be pulled. Regent Wachter accepted the amendment and stated that the issue of disclosure will come back to The Regents in September 2007 after discussion regarding the threshold.

General Counsel Robinson clarified that without the threshold requirement set forth in the proposed policy, the current disclosure requirement will remain in place for the next two months. The current policy states that disclosure will be made in the case of an actual or potential conflict via self-reporting by members of the IAC, and that it is the responsibility of the General Counsel to take action in the event that a member of the IAC self-reports such a conflict.

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

The meeting adjourned at 10:55 a.m.

Attest:

Secretary and Chief of Staff