MINUTES

BOARD OF REGENTS’ COMMITTEE ON BUDGET AND FINANCE MEETING

March 15, 2012

I. CALL TO ORDER

Committee Chair Dennis Hirota called the meeting to order at 10:07 a.m. on Thursday, March 15, 2012, at University of Hawai‘i at Mānoa, Campus Center Executive Dining Room, 2465 Campus Road, Honolulu, Hawai‘i 96822.

Committee members in attendance: Committee Chair Dennis Hirota; Barry Mizuno; Saedene Ota; Jan Sullivan; and Matthew Williams.

Others in attendance: Regents Chair Eric Martinson (ex officio committee member); Regents Vice Chair James Lee; Regent Coralie Matayoshi; President M.R.C. Greenwood, Ph.D.; Executive Vice President for Academic Affairs/Provost, Linda Johnsrud, Ph.D.; Vice President for Budget & Finance/Chief Financial Officer, Howard Todo; Associate Vice President for Capital Improvements, Brian Minaai; Executive Administrator and Secretary of the Board of Regents, Keith Amemiya, Esq., and others as noted.

II. APPROVAL OF MINUTES OF DECEMBER 21, 2011 MEETING

Upon motion by Regent Ota and second by Regent Mizuno, the minutes of the December 21, 2011 meeting were unanimously approved.

III. PUBLIC COMMENT PERIOD

Secretary Amemiya announced that no persons submitted written testimony or signed up to orally testify regarding today’s agenda items.

IV. AGENDA ITEMS

Investment Monitor Report

Peter Backus, of MorganStanley SmithBarney, went over the Investment Performance Report for the UH Endowment fund for the period ending December 31, 2011. Backus provided the global and interest rate forecasts for the upcoming year.

The UH Endowment’s Total Fund Performance for the fourth quarter of 2011 was 5.66% versus the UH Index Objective of 5.57%. The portfolio increased in market value during the quarter from $53.1 million to $56.1 million for a net increase of $3.0 million.

Backus reviewed the Investment Performance Summary as of December 31, 2011, including UH’s Total Portfolio, and Balanced, Domestic Equity, International Equity, Fixed Income, and Short Term funds.

At the previous Committee on Budget and Finance meeting (on December 21, 2011), the Committee approved reallocating funds. Backus reported the $8 million that was
removed from the Neuberger Berman Balanced account and reallocated $4 million each to the Bank of Hawai‘i Fixed Income account and the Wisdom Tree Equity Income Fund, was not yet reflected in the report, as the transaction took place in January 2012.

Backus also commented on the Brandes International Equity fund, which drew concern from the Regents at the December Committee meeting because of its low performance. Backus reported that the fund performed well in the fourth quarter and did better than the benchmark.

Through March 14, 2012, the value of the UH Endowment Fund was $59.6 million. The managers who were performing poorly are experiencing strong comebacks in the first quarter.

Backus included information on the fiscal returns by annual fiscal year and the annual returns by calendar year, which was distributed to the Committee members. MorganStanley SmithBarney also provided the Manager Review of Investment Policy Compliance. There were no findings on Specific Performance Tests and Asset Allocation. However, there were a couple of Qualitative Criteria items that were flagged, but none were considered material. There was no suggested action for NWQ and Neuberger Berman, which was viewed as positive. However, Brandes is a named defendant in a claim, and Backus will continue to monitor the situation.

In response to a question from Regent Williams, Backus said that MorganStanley SmithBarney is fairly cautious about its equity output, and is already at its top estimate. However, many times analysts have to re-think things when markets reach beyond expectations. Part of the logic behind the reallocation made in the previous Committee meeting in December was to emphasize an equity income ATF for the money that went back into equities. It is wise to have some extra income in the portfolio so that if markets start to trade sideways, you are still getting the income. MorganStanley SmithBarney is not trying to get overly aggressive and chase the market’s rally. A lot of asset allocation is still determined by managers, and their ability to move between equities and fixed income; the managers are fairly quick to adapt.

**Quarterly Financial Status Report as of September 30, 2011**

Vice President for Budget and Finance/Chief Financial Officer, Howard Todo, went over the Selected Balance Sheet Items and Liquidity Measures (Cash and Investments, Accounts Receivable, Net, Endowment Investment, Bonds Payable, and Net Assets). He also went over the Income Statement Metrics (Total Revenue, Total Operating Expenses, Operating Income (loss), Total Non Operating Revenues (Expenses), and Increase (Decrease) in Net Assets). The analytical comments included in the materials to the Regents by the UH Administration gave some explanation for the changes in amounts of the funds from FY 2010 to FY 2011.

The analytical comments that VP Todo addressed included:

- No. 1: The cash and investment balance are highest at the start of the fiscal year (July 1, 2011) and decreases throughout the year as general funds appropriated for the year are expended.
• No. 2: Accounts receivable increased by $23 million, due to an increase in Federal, State and Private contract and grant receivables ($2 million) and an increase of student receivables from tuition ($21 million).
• No. 3: Bonds payable as of December 31, 2011 as compared to the prior year decreased by $12 million due to principal payments and year-end adjustments.
• No. 4: Net Assets continue to increase.
• No. 5: Employee head counts. President Greenwood noted that there was large growth in the number of lecturers, mainly because of the enrollment growth in Community Colleges.

Committee Chair Hirota said that he would like to see more faculty in critical areas, in light of the fact that one of his favorite subjects – regarding storm drainage – is no longer being offered by the UH Mānoa’s College of Engineering.

VP Todo also briefly went over the Income Statement Metrics as of December 31, 2011: Total Revenue, Total Operating Expenses, Operating Income, Total Nonoperating Revenues, and Increase in net assets.

• No. 6: The $28 million increase in net student tuition and fees was the result of year-over-year increases in tuition revenues and enrollment headcount.
• No. 7: The year to date $13 million increase in compensation and benefits is due to an increase in employee headcount and the restoration of faculty salaries to the December 31, 2009 rate.
• No. 8: Fiscal year to date State appropriations increased by $18 million, primarily due to the prior year budget base reduced by the reinstatement of $22 million of ARRA (American Recovery and Reinvestment Act of 2009) funds.
• No. 9: Interest expense for the December 31, 2011 fiscal year was $8 million more than the prior year due to the increase in debt service associated with the 2010 Series bond issuance in October 2010.
• No. 10: Capital State appropriations represent State General Obligation Bond Funds released by the Governor for Capital Improvement Projects (CIP) appropriated by the Legislature in the State CIP Budget. As of the second quarter, the Governor released $84 million less in funding over the same period last fiscal year.

Following an inquiry by Regent Sullivan about projects with interest debt payments when projects have not yet started, and whether policy exists over the timing of debt service payments, a discussion on the topic ensued, focusing on the UH Hilo Student Housing project and the Pacific Health Sciences Research Center. VP Todo replied that UH revenue bond issuance is determined by amount requests and repayment options. Debt service is charged to the actual project. Under the State system, you can’t contract without having the funds.

VP Todo also explained the Consolidated Funding Report as of December 31, 2011: Appropriated Operating Funds, Capital Improvements Program (CIP) Funds, Federal & Trust Extramural Funds, Other Non-Appropriated Funds, and Total Resources – All Fund Types.
V. ADJOURNMENT

There being no further business, upon motion by Regent Ota and second by Regent Sullivan, and with unanimous approval, the meeting was adjourned at 11:15 a.m.

Respectfully Submitted,

[Signature]

Keith Y. Amemiya, Esq.
Executive Administrator and
Secretary of the Board of Regents