UNIVERSITY OF TORONTO

THE GOVERNING COUNCIL

REPORT NUMBER 166 OF THE BUSINESS BOARD

April 28, 2008

To the Governing Council,
University of Toronto.

Your Board reports that it met on Monday, April 28, 2008 at 5:00 p.m. in the Council Chamber, Simcoe Hall, with the following members present:

Mr. Richard Nunn, (In the Chair)
Ms Catherine J. Riggall, Vice-President, Business Affairs
Professor Angela Hildyard, Vice-President, Human Resources and Equity
Mr. P. C. Choo
Ms Susan Eng
Mr. Alex Kenjeev
Dr. Joel A. Kirsh
Mr. Jim Linley
Mr. Gerald A. Lokash
Mr. Gary P. Mooney
Mr. David Oxtoby
Mr. John Varghese
Ms B. Elizabeth Vosburgh
Mr. Larry Wasser

Professor Vivek Goel, Vice-President and Provost
Ms Sheila Brown, Chief Financial Officer
Mr. Louis R. Charpentier, Secretary of the Governing Council
Ms Rivi Frankle, Chief Operating Officer, University Advancement, and Assistant Vice-President, Alumni Relations
Ms Christina Sass-Kortsak, Assistant Vice-President, Human Resources
Mr. Nadeem Shabbar, Chief Real Estate Officer

Secretariat:

Mr. Neil Dobbs*
Mr. Matthew Lafond

Regrets:

Ms Mary Anne Elliott
Dr. Gerald Halbert
Ms Paulette L. Kennedy
Dr. Stephan Mathias Larson
Mr. Geoffrey Matus
Mr. George E. Myhal
Professor Arthur S. Ripstein
Mr. Stephen C. Smith
Mr. Robert S. Weiss
Mr. Yang Weng
Mr. W. David Wilson

In Attendance:

Ms Karen Coll, Managing Director, Public Markets, University of Toronto Asset Management Corporation
Mr. Ira Gluskin, Chair of the Board, University of Toronto Asset Management Corporation
Dr. Anthony Gray, Special Advisor to the President
Mr. John Hsu, Managing Director, Risk Management and Operations, University of Toronto Asset Management Corporation
Ms Deepa Jacob, Research and Policy Analyst, Office of the Vice-President, Business Affairs

* By telephone.

In Attendance (Cont'd)

Professor George Luste, President, University of Toronto Faculty Association
Mr. John Lyon, Managing Director, Investment Strategy, University of Toronto Asset Management Corporation
Ms Anne MacDonald, the Director of Ancillary Services
Ms Susan F. MacDougall, Director, Environmental Health and Safety
Mr. Steve Moate, Senior Legal Counsel
Mr. William Moriarty, President and Chief Executive Officer, University of Toronto Asset Management Corporation
Ms Rosie Parnass, Quality of Work/Life Advisor and Director of Organizational and Staff Development

The Chair noted that the main theme of the meeting was human resources and equity and the largest part of the meeting would be devoted to that theme. Because, however, a number of guests from the University of Toronto Asset Management Corporation were present, the Board would at the beginning of the agenda consider UTAM's annual report and proposals concerning the relationship between the University and UTAM. It would then turn its attention to the major theme.

1. Report of the Previous Meeting: Report Number 165 – March 5, 2008

Report Number 165 (March 5, 2008) was approved.

THE FOLLOWING ITEM IS RECOMMENDED TO THE GOVERNING COUNCIL FOR APPROVAL.

2. Investments: Relationship with the University of Toronto Asset Management Corporation (UTAM) - Business Board Terms of Reference: Revisions

The Chair reminded members that the Board had had a first discussion of the relationship between the University and the University of Toronto Asset Management Corporation (UTAM) at the November 19th meeting. The Board had given its approval to a By-Law change, enabling the President of the University to cease service as an *ex officio* member of the Board. (The Vice-President, Business Affairs continued as an *ex officio* member.) The University administration was now represented by the Vice-President, Business Affairs and the Chief Financial Officer. The Board had also had a substantial first discussion of the matters now before it: (a) the revised terms of reference for the Business Board, and (b) the change from the current Service Agreement to a delegation of authority to UTAM approved by the Business Board plus an Investment Management Agreement approved by the Vice-President, Business Affairs. It was intended at that time that there would be further consultations, including consultations with lawyers to ensure that the proposed delegation of authority to UTAM would not amount to a breach of this Board's fiduciary duties. Those consultations had taken place, some changes had been made, and the matter was now before the Board for approval.

2. Investments: Relationship with the University of Toronto Asset Management Corporation (UTAM) - Business Board Terms of Reference: Revisions

The Chair said that the objective of the proposed amendment of the terms of reference was and remained a simple one: that the Business Board, acting for the Governing Council (which was the trustee of the endowment funds and administrator of the pension plans) should approve appropriate return targets and risk tolerances for the funds under UTAM's management and should monitor their achievement. On that basis, the management of the funds should be left to the UTAM management and staff – the people with the expertise - overseen by the University-appointed, expert UTAM Board.

On the recommendation of the Chair of the Business Board,

YOUR BOARD RECOMMENDS

THAT the proposed, revised section 5.1 of the Business Board Terms of Reference, "Financial Policy and Transactions," a copy of which is included in Appendix "A" hereto, be approved.

THE FOLLOWING ITEMS ARE REPORTED TO THE GOVERNING COUNCIL FOR INFORMATION

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007

The Chair reminded members that UTAM was responsible for investing University funds and the pension fund to achieve, over the long term, the University's return expectation within its stated risk parameters. UTAM was now making its annual accountability report not only to its controlling corporation but more importantly to its client. The Board should: (a) make its view known if it had concerns with respect to investment performance and level of risk, and (b) request any follow-up report(s), if appropriate. Apart from that, the annual report was for information. He noted that UTAM reported to the University through the Vice-President, Business Affairs.

Ms Riggall introduced the guests from UTAM and welcomed its new President and C.E.O, Mr. William Moriarty. Mr. Lyon had served with distinction as Interim President and C.E.O. until the appointment of Mr. Moriarty. She thanked Mr. Lyon and his colleagues for the excellent work they had done during the hiatus between the departure of Mr. Felix Chee and the arrival of Mr. Moriarty.

Mr. Lyon presented the annual report. He noted that UTAM managed $5.7-billion of financial assets for the University, in the Long-Term Capital Appreciation Pool (primarily endowment funds and also the funds set aside to meet the University's obligations under the

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007 (Cont'd)

Supplemental Retirement Arrangement), the pension fund, and the Expendable Funds Investment Pool (EFIP). The latter Pool represented the University's working capital and its size varied between about $450-million and $700-million, depending on the time of year.

- **Investment strategy: Portfolio construction**. The pension fund and the endowment fund were managed in a similar manner. UTAM was a manager of managers. Unlike such other institutional managers as the Ontario Teachers' Pension Plan or the Ontario Municipal Employee's Retirement System (OMERS), UTAM did not manage individual investments directly.

  UTAM reviewed its long-term asset mix annually, using optimization modeling to arrive at a mix that would provide the best return possible for an appropriate level of risk. This was a conventional approach in investment management, and it could be described as spending a risk budget to build a portfolio that would obtain the best possible long-term return for that risk spending. The University stated the acceptable risk tolerance and the return it expected to achieve at that level of risk. Those figures established the framework for UTAM'S asset mix. Those figures had to be reasonable from a historical perspective; while the appetite for return was unlimited, the appetite for risk was clearly limited.

- **Portfolio strategy: Asset mix**. Over the long-term, UTAM planned to invest 55% of assets in the public markets for stocks and bonds and 45% in alternative asset classes, including absolute-return hedge funds, private-market equity investments, and real assets including real estate and commodities. The allocation to private assets appeared to be very heavy compared to many Canadian funds. It was, however, more common for U.S. funds, and especially for the leading endowment funds in that country.

  UTAM updated its mix of the various asset classes annually. The general shape of the strategy had been established about three years ago and it had been fine-tuned since that time. UTAM was building up its investments in the alternative asset classes with patience and discipline over time. While the long-term target for such investments was 45% of assets, the actual weight as at December 31, 2007 was 16%. While the process of disciplined build-up of the alternative asset classes was proceeding, UTAM invested the money not used for those classes in the public-market asset classes (Canadian, U.S., and international stocks and bonds) *pro rata* to their weight in the asset mix. As a result, there was, in addition to the long-term policy asset mix, a near term asset mix, representing the target mix of asset classes with the *pro rata* increase in the public-market categories.

  Rebalancing and tactical changes to the asset mix were relatively infrequent. Because UTAM was a manager of managers, a change in asset mix would require that the

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007 (Cont'd)

manager(s) whose allocations were reduced sell assets and those whose allocations were increased buy additional assets. That would involve substantial frictional costs, causing UTAM to change its near-term asset mix only when clearly necessary. UTAM policy permitted management to move to 5% above or below the near-term asset mix for the significant asset classes. But UTAM management would use that flexibility infrequently, only if there was a high level of conviction that a tactical shift was required, and only to try to avoid loss rather than to seek to "beat the market." UTAM maintained a long-term orientation. When it was decided to move from the short-term asset mix target, UTAM would do so in a cost-effective manner, using index futures rather than moving funds between external investment managers.

- **Investment strategy: Diversification**. Diversification of investments in asset classes, geographical locations, and investment managers was a key factor in portfolio construction and risk management. It was a necessary but not sufficient tool of risk management. Investments in the real-asset category were currently being further diversified by new investments in infrastructure facilities. At the 2007 year-end, there were twenty active public-market securities managers of Canadian, U.S. and international equities and fixed-income investments. There were also 75 different managers for alternative investments. The large number was appropriate because of the non-normal risk curves for those investments. Diversification in the alternative asset category was achieved by a variety of different kinds of investments within the absolute-return hedge fund, private equity/debt and real-asset categories as well as by a large number of different managers. The nineteen hedge-fund managers included fourteen managers of funds of hedge funds, meaning that UTAM's hedge-fund investments were actually placed in over 300 funds, representing a super-diversified position. UTAM had to pay an extra layer of fees for fund-of-fund investments, but it had found that to be appropriate for three reasons. First, it provided diversification. Second, it allowed UTAM time to build up its own expertise in the area. Third, it freed up time for UTAM's staff to work on other asset classes. UTAM was at this stage moving to invest in more individual hedge funds.

  Mr. Lyon noted that with respect to private-market investments, UTAM had committed funds for 80% of its planned investments in private equity/debt and 50% of its target for investments in real assets. The amount of money actually invested by the managers was, however, much less than the amount committed. The valuation of many areas of private investments had declined significantly in the current market environment. UTAM was not unhappy about that development because it meant that its managers would be able to make future investments less expensively.

- **Investment strategy: Positioning in 2007**. Mr. Lyon displayed the asset mix for the endowment and pension funds as at December 31, 2007: Canadian equity 11%; U.S.

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007 (Cont'd)

equity 19%; International equity 19%; fixed income 23%; absolute return hedge funds 7%; private investments 6%; real assets 5%; and cash 10%. The two major funds were aligned as closely as possible so that investments could be made for both at a lower cost and so that UTAM could gain access to top alternative-asset funds by offering larger investments.

The asset mix departed from the near-term target mix in several respects. First, there was no provision for a cash position in the policy asset mix or in the near-term target mix. The investment of 10% of the funds in cash was a tactical position taken in the last half of 2007. The near-term target rates of the alternative asset classes were by definition equal to the actual weights, with the proportion under the policy asset mix allocated *pro rata* to the public-market asset classes. The allocation to fixed income was very slightly above the near-term target. In May of 2007, it had been decided to reduce the corporate credits in the fixed-income allocation by one half, replacing the corporate bonds and debentures with government bonds. That had been an important move in the light of declining credit quality. The cash position had been initiated in August 2007 at 6%, increasing to 10% in November. To achieve that position, the exposure to Canadian, U.S. and international equities had been reduced. The outcome of the decision had not been any improvement of performance in 2007, but UTAM had been more comfortable holding the 10% cash position during the difficult market period at the close of the year. In January 2008, the decision had added substantial value. The cash position was held in the form of hard cash assets and index futures.

- **Investment performance: Key measures**. There were three key performance indicators for the portfolios. First, there was performance relative to the University's return target: a net real return of 4% per year - that is a return of 4% after all costs and after inflation. That absolute target was a difficult one to meet in years when the markets were poor and an easy one in years when the markets were good. Therefore, achievement of that performance measure was best judged in terms of average performance over a longer term of three to five years. In fact, the target used a ten-year horizon. The second performance indicator was return relative to a market benchmark. That criterion was used both for overall fund performance, where the benchmark was a weighted combination of specific market indices (e.g. the Standard and Poor's / Toronto Stock Exchange Composite Index of Canadian stocks or the DEX Universe Index of Canadian bonds). The elements of the total-fund benchmark were also used to judge the performance of the individual asset classes. Because the benchmarks moved in tandem with the markets, they were useful in judging performance both in the long term and the short term. The third performance measure was return relative to that of funds in a peer universe. That measure could also be used for total-fund return as well as the returns generated by individual asset classes. Particularly for total-fund return, that measure had to be considered with some skepticism. The funds in the peer universe were quite different, with varying objectives

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007 (Cont'd)

and risk tolerances. Even the basis of reporting was different, with some funds reporting their gross return (before costs) and some (including UTAM) reporting net return.

- **Investment return for 2007**. For the 2007 year, the endowment fund had earned a return of 6.1% and the pension fund 6.0%. For the five years ended December 31, 2007, average annual returns were 11.7% for the endowment fund and 11.5% for the pension fund. The performance of the alternative asset classes had been very strong. Canadian equities had provided a solid return. U.S. and international equities had, however, struggled, especially in the second half of the year, following the appearance in May of globally difficult market conditions.

- **Investment return relative to the University target**. The University required, as noted, a 4% net real return for the endowment fund and the pension fund. For 2007, the return of the endowment fund had missed that target by 27 basis points (i.e. 27/100 of 1%), and the return of the pension fund had missed the target by 40 basis points. The returns, however, followed four consecutive years of outperforming the target. For the five-year period ended December 31, 2007, the endowment fund had outperformed the target by 560 basis points (i.e. 5.6%) and the pension fund by 540 basis points (i.e. 5.4%). On a dollar basis, over the five years, the funds had provided returns amounting to about $970-million in excess of the University's target. Missing the target in 2007 equated to $17-million. Hence, the very good performance in the previous four years had provided a very substantial cushion for other years when markets were difficult, including 2007 and probably 2008.

- **Investment performance relative to the benchmark return**. The performance of the endowment fund had exceeded its benchmark in four of the past five years as had the performance of the pension fund in three of the past five years. The endowment fund had just outperformed its benchmark in 2006 while the pension fund had returned 72 basis points below the benchmark. In that year, the benchmark and the asset mix for the pension fund had been changed to match that of the endowment fund by reducing the proportion of fixed-income investments and increasing equity investments. One-time transition costs for the change had had a negative impact on the pension fund's performance, but the new asset mix had improved the 2006 performance of the pension fund by about 2% for the year and was proving to be of long-term benefit. Hedge funds and private-market investments had been key contributors to performance in 2007. At this time, the return on private equity/debt investments and private-market real assets was assumed to equal a benchmark; therefore they were not deemed to add value relative to a benchmark despite their strong performance. Public-market investments had turned in very good performance during the first half of 2007, but they had fallen off in the second half. In total, about one half of the public-market managers had exceeded their asset-category benchmarks for 2007, but one half had not done so.

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007 (Cont'd)

- **Investment performance relative to the peer universe**. Relative to the RBC Dexia Balanced Fund Universe of Canadian funds, both the endowment fund and the pension fund had in 2007 ranked in the top percentile of funds – i.e. they had outperformed 99% of other funds. For the two-, three- and four- and five-year periods ended December 31, 2007, both funds had ranked in the top decile, i.e. they had outperformed at least 90% of other Canadian funds. In the survey of over 700 endowment funds by the U.S. National Association of College and University Business Officers (NACUBO), the University of Toronto endowment fund ranked in the third percentile for the five-year period ending in December 31, 2007 and in the 12th percentile for the one-year period ending December 31, 2007. As noted, it was important to exercise some skepticism with respect to the relative rankings because different funds had different risk tolerances and reporting criteria (although the University of Toronto funds reported returns after all costs, adopting the most rigorous criteria).

- **Risk management methods**. UTAM gave on-going attention to a number of quantitative and qualitative methods for risk management. Those methods were well established within the investment industry. Risk-management was handled internally; UTAM used few consultants. It used historical performance information provided by its own external investment managers, who were top-tier managers and provided excellent information at a low cost. The application of risk-management techniques was intended to ensure that risk was consistent with the University's risk-tolerance – an average standard deviation of no more than 10% over any ten year period. UTAM sought to maximize risk-adjusted investment returns within that tolerance. To do so, UTAM constructed its portfolios to select appropriate asset classes and geographic locations that met risk and return criteria, and to select those assets with appropriate correlations with each other – i.e. to select asset classes that tended not to move up or down in value too much in step with each other. One great benefit of the alternative asset classes was the low correlation of their returns with those of public-market asset classes. Risk management was also an important factor in selecting managers. The process for selection of investment managers included both a review of their investment practices and returns and also of their operations, including their risk management.

- **Risk management: Actual portfolio risk levels**. Over the past four years ended December 31, 2007, the level of risk in the two major funds, measured in terms of rolling 36-month standard deviation of returns, had been significantly less than the 10% University-specified risk tolerance and it had been tending downwards over time. The outcome was the provision of a cushion to deal with events causing market declines such as the recent credit crisis. The construction of a lower risk portfolio was also appropriate as UTAM deployed assets into alternative investments – an area of potentially greater volatility.

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007 (Cont'd)

- **Risk-adjusted return – a perspective**. It was interesting to note that over the past year and a half, the volatility of UTAM's absolute-return hedge funds (measured again in terms of the rolling 36-month standard deviation of returns) had been about half that of fixed-income investments. The risk of fixed-income investments had been about one half that of Canadian equities. While those risk levels would change over time, it was interesting to observe that the return on hedge funds for 2007 had been 9.1%, that on fixed-income investments had been 2.4% and that on Canadian equities 9.7%. Mr. Lyon reiterated that the under-use of the full risk tolerance was important in the light of the unknown future risk of investment in the alternative asset classes.

- **Cost effectiveness**. UTAM's costs had been stable between 2003 and 2007, ranging between 47 basis points (i.e. 0.47% of assets) to 58 basis points until 2007, when costs had increased to 76 basis points. The 2007 increase had been anticipated because investment in alternative assets and private funds had increased, and private funds were at their most expensive in the early stages of the investment. This additional cost was worthwhile; alternative assets represented about 7½% of the average assets in the two major funds but had in 2007 generated about 20% of their return. The Commonfund Endowment survey of North American endowments with over U.S.$1-billion under management had shown that the average cost of their management was 92 basis points, substantially more than UTAM's 76 basis points.

- **Outlook for 2008**. Mr. Lyon observed that market conditions had been very difficult since mid-2007. In the first quarter of 2008, the U.S. markets had declined by 9.5%, international markets by 8.9% and the Canadian market by 2.8%. For January and February 2008, the endowment and pension funds had declined by 4.5%, although they had performed slightly better than their benchmarks. The Expendable Funds Investment Pool had earned a return of 1.1% during the first two months. For the twelve months ended February 29, 2008, the endowment and pension funds had approximately held their value but not achieved a gain. The expendable Funds Investment Pool was up by 4.3% over the twelve months.

- **Comparisons with major Canadian pension funds**. As noted, the University's pension fund had a return of 5.98% for 2007, a bit better than the benchmark return of 5.89%. The Ontario Municipal Employees' Retirement System (OMERS) had a return of 8.7% with a benchmark of 5.6%. The Ontario Teachers' Pension Plan (Teachers) had a return of 4.5% with a benchmark of only 2.3%. That demonstrated the difficulty of comparing performance among funds. The Canada Pension Plan Investment Board, unlike UTAM, OMERS, and Teachers, did not use the calendar year for reporting. Its used a March 31 fiscal year. For the last nine months of 2007 (April to December), the C.P.P. fund was essentially flat - up by 0.5%.

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007 (Cont'd)

Invited to address the Board, Mr. Moriarty said that he was very pleased to be a part of UTAM. He was very encouraged by UTAM's approach during a very difficult period in the markets, and he was very encouraged by the quality of the UTAM team. His personal focus was now to work on understanding UTAM's investment process and its external managers. His objectives were to gain a full understanding of the priorities of the organization and to work on improving its fine track record.

Invited to address the Board, Professor Luste said that faculty members and librarians were the largest stakeholder group in the pension plan, representing about two thirds of its liabilities and assets. He outlined a number of issues he had with respect to the investment of the pension fund.

- **Costs**. While investors could not control the securities markets, foreign exchange rates or interest rates, they could control costs. Professor Luste had perceived an alarming increase in pension plan costs, which now amounted to an average of $8-million per year since the formation of UTAM. Costs as a proportion of assets in the pension fund had amounted to about 20 basis points in the years before UTAM was formed. The cost above that 20 basis-point base in the years from 2000 (when UTAM was formed) to 2007 amounted to $68-million.

- **Active management and performance incentives**. While UTAM might respond that investors get what they pay for, in the case of the investment funds world in general and the University's pension fund in particular, it appeared to be the case that investors did not get what they paid for. The structure of compensation in UTAM provided very large incentives to use active management in order to seek to outperform the benchmark. A major benefit of passive management was lower costs, as demonstrated in the years before the formation of UTAM. Professor Luste had prepared a simple model comparing UTAM's returns with a simple passive portfolio consisting 50% of the Canadian universe bond index and 50% of the Toronto Stock Exchange Composite Index. (Especially because UTAM hedged all of its returns into Canadian dollars, the simple model consisting only of Canadian indices seemed appropriate.) That passive model had outperformed UTAM over the past eight years, and it had done so at a lower level of volatility and at a lower cost. On a large asset base, the effect of that underperformance was huge, amounting to more than $200-million. He referred members to the document he had handed out at the meeting. On page 5, a 1991 article by William F. Sharpe stated the case for passive management.

- **Alternative assets and hedge funds**. Professor Luste had very serous concerns about the investments in alternative assets: they had very high fees, it was not certain that they would add value in the long run, and there were serious issues of transparency concerning the investments. He thought that it was wholly improper to invest pension-fund money

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007 (Cont'd)

and trust funds in assets that were not transparent. He noted that investors had placed money in certain hedge funds such as Long-Term Capital Management and in the investment bank Bear Stearns. Those investments had appeared at the time to be safe and conservative, but they soon became worthless or close to it. Professor Luste referred members to two articles that had been reproduced, beginning on pages 9 and 12 of his handout, entitled "Why today's hedge fund industry may not survive" and "Hedge funds come unstuck on truth-twisting lies." He urged that members read the articles and be aware of the serious issues connected with hedge-fund investing.

Professor Luste expressed his frustration that he was allowed only five minutes to deal with these very fundamental issues. He stated that the University had to fulfill its pension promise to retirees and to the active members of the pension plan. Any failure to do so because of a failure of the pension fund investments would have an impact not only on pensioners but also on the on-going viability of the University.

Among the matters that arose in discussion were the following.

(a) Asset-backed commercial paper. A member asked about the University's exposure to asset-backed commercial paper, which had been generally viewed as a safe, income-generating type of investment, but had suffered very substantial losses in recent months. Mr. Lyon replied that the University's exposure to non-bank, asset-backed commercial paper had been very small, with about $4.5-million in the pension fund, $1.3-million in the endowment fund, and no exposure in the Expendable Funds Investment Pool. At the end of November, UTAM had written down the value of those investments by 50% - a very conservative action given that most other investors had written down the value of this commercial paper by only 10% - 15%. Although some favourable new information had become available in February, UTAM had retained the 50% write-down. UTAM had supported the proposal of the Crawford Committee to convert this commercial paper into longer dated debt – a step that it thought to be the right one for the funds.

(b) Investment costs and private-market investments. A member noted that while the cost of the management of the endowment and pension funds had been only 76 basis points for 2007, UTAM planned to increase the proportion of the funds invested in the private markets, where returns were potentially better but where costs were significantly higher. Mr. Lyon agreed that costs would be higher. UTAM had not prepared a specific *pro forma* forecast of the higher costs as further private-market investments were made. In the early years of private-market investments, the managers were paid a proportion of the amounts committed to their funds. Thereafter, a more substantial portion of their compensation came from a share of the profits (from their "carry."). Most of UTAM's private-market investments were currently in their early years. In later years, distributions from the funds as well as cash-flow from the wind-up of funds would be substantial and would reduce the average cost of the investments.

3. Investments: University of Toronto Asset Management Corporation: Annual Report, 2007 (Cont'd)

A member observed that the managers for private-market funds were generally paid 1% - 2% of committed funds per year plus, for example, 20% of the profits above a certain level of preferred return. That presumably would increase costs substantially. Mr. Lyon replied that UTAM, like all other investors in private-market funds, did not include the carry – the 20% or so of the profits above the preferred return – in the calculation of management costs. That amount simply reduced the return reported on the investments. UTAM's practice was the usual one. In fact, its reporting of costs was more diligent than that of most other investors. Some did not include any amount for the cost of private-market investments but simply deducted the cost from the total return. There were other inconsistencies: some investors reported only gross costs, while others took into account "net back" fees – the fees earned by the managers (as an example) for service on the boards of directors of investee companies, when those fees were returned to the fund.

Invited to ask a question, Professor Luste asked whether there was additional indirect exposure to asset-backed commercial paper through UTAM's investments in hedge funds. Mr. Lyon replied that the concern dealt only with commercial paper that was not backed by the banks. Most of the hedge funds in which UTAM had invested were U.S. operations and those that made investments internationally. Therefore, exposure to Canadian, non-bank, asset-backed commercial paper, if any, would be quite small.

(c) Professor Luste's concerns. A member asked that there be a specific response to two of the matters raised by Professor Luste: (i) his view that simple passive investments would have generated a superior return to that achieved over the years by UTAM at a lower level of risk; and (ii) his concern about investment in hedge funds.

Ms Riggall replied that she had only now seen Professor Luste's paper, and it would be inappropriate for her to respond at this time. She would, however, be pleased to provide a written response.

(d) Outlook for 2008. A member noted that market conditions had been very poor in recent months, and he asked about UTAM's outlook for the remainder of 2008. Mr. Lyon said that he anticipated that 2008 would continue to be a difficult year. However, UTAM was not seeking to time the market; it did not have a crystal ball to forecast the future. He thought that the market was likely at a bottom and would continue to vary around that generally low level. UTAM would therefore likely slowly increase the weight of its equity investments.

4. Investments: Documentation regarding the Relationship between the University of Toronto and the University of Toronto Asset Management Corporation: Delegation of Authority and Investment Management Agreement

On the recommendation of the Vice-President, Business Affairs,

YOUR BOARD APPROVED

Subject to Governing Council approval of the revised section 5.1 of the Business Board Terms of Reference, "Financial Policy and Transactions,"

(i) The proposed 2008 Delegation of Authority from the Governing Council of the University of Toronto to the University of Toronto Asset Management Corporation, a copy of which is attached hereto Appendix "B"; and

(ii) THAT the Amended and Restated Service and UTAM Personnel Agreement, most recently approved by the Business Board on behalf of the Governing Council of the University of Toronto on April 7, 2003, including its Schedule "C" (Performance Benchmarks) most recently approved by the Business Board on April 4, 2005, be rescinded, effective May 21, 2008.

The Board received for information the 2008 Investment Management Agreement between the Governing Council of the University of Toronto and the University of Toronto Asset Management Corporation.

5. Vice-President, Human Resources and Equity, and Employment Equity: Annual Report, 2007

The Chair commented on the main theme for the meeting: human resources and equity. He said that the strength of the University lay in its human resources – its faculty and staff – as well as in its students. The recruitment, retention, experience, development and equitable treatment of faculty and staff were immensely important topics, as was the health and safety of everyone on the University's campuses. Faculty and staff also represented by far the University's largest item of expense.

Professor Hildyard said that her annual report was more comprehensive than in previous years, including the previously separate annual report on Health and Safety. The report had moved from a focus on process to a stress on accountability. The overall thrust of the Human Resources and Equity portfolio was to ensure that the University was an employer of choice. About 65% of the University's gross operating budget was spent on salaries and wages and on

5. Vice-President, Human Resources and Equity, and Employment Equity: Annual Report, 2007 (Cont'd)

benefits. The University employed 1,979 tenured or tenure-stream faculty, 1,045 other academics, 145 librarians, 288 research associates, 4,479 unionized administrative staff and 918 non-union administrative staff, for a total of 8,845 full-time or part-time employees, a growth of 21% since 2000. There were, in addition, approximately 10,000 casual staff. Employees were represented by 17 different unions or associations in 21 bargaining units. For the current year, the University was or would be negotiating with 14 of them. Professor Hildyard dealt with the following topics in her report.

- **Employee experience survey**. The survey, conducted in 2006, had drawn a 52% response rate, which was a very good one. Mercer Delta, which had carried out the survey, had concluded that it presented a highly favourable picture of the employee experience at the University. The survey pointed to many relative strengths, including: diversity and equity, cooperation and collegiality, employee engagement, organizational values, work design, teaching and research, and collaboration and collegiality among members of the faculty and librarians. The survey also pointed out potential opportunities to enhance the employee experience, including: further assistance with growth and development, workload and work/life balance, services and support for faculty and advancement opportunities for librarians.

- **Employee experience survey: Most favourable responses**. The five most favourable responses from the survey were: 88% of all employees had a good understanding of what was expected of them in their job; 87% were proud to work at the University of Toronto; 85% thought that their co-workers and colleagues treated them with respect; 83% felt either very motivated or fairly motivated in their jobs; and 82% would recommend the University as a good place to work.

- **Employee experience survey: Least favourable responses**. The most unfavourable responses were: 60% thought their work load was unreasonably heavy; 32% felt that their workload did not allow them to meet performance expectations without sacrificing quality; 32% felt that the stress of their work was negatively affecting their job performance; 31% did not agree that promotions, transfers and appointments were made fairly at the University; and 31% did not agree that new employees received adequate orientation when joining the University. The University had, since the completion of the survey, initiated an orientation program for new employees. Concern about the negative effect of stress was more prevalent among faculty than staff and among women than men.

- **Employee experience survey: Motivation of employees**. In comparison with other employers who had used the Mercer Delta survey, the proportion of both University faculty and staff who felt fairly or very motivated was well above the benchmark.

- **Employee experience survey: Employees who felt left out because of membership of a designated group**. A small proportion of faculty and staff sometimes felt left out in their work units because of their gender, ethic or cultural origin (including race and

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aboriginal status), religious affiliation, disability or sexual orientation. The proportion feeling left out was relatively similar for faculty, librarians and staff.

- **Employee experience survey: Workload and work/life balance**. About 60% of employees felt that their workload was "heavy" or "much too heavy." The issue was a concern to all groups - faculty, librarians and staff - although it was an issue for 69% of faculty. The concern of faculty members was an interesting one because they, more than other employees, had control over their workload. However, to be the best in their field, faculty had to compete on a world stage and that required considerable commitment. The University, of course, should not discourage that approach, but it should find ways to provide better support to the faculty. A significant proportion of employees, again primarily faculty (37%), were concerned that their workload did not allow an acceptable balance between their work and their personal lives.

- **Employee experience survey: Responding to the results**. To respond to the concerns demonstrated by the survey, the University had formed a number of working groups. For staff, they included groups on: workload and work/life balance; appointments, transfers and promotions; and training, development, feedback and recognition. A group had been formed to consider workplace equity for faculty and staff. Finally, a joint working group had been formed by the Faculty Association and the University on faculty workload and work/life balance issues. In addition, because the responses had differed marginally among divisions, each division was reviewing its results and developing action plans to address local issues.

- **Leadership development**. The University's mentorship program paired staff at the middle and junior levels with more senior leaders. The program placed a strong emphasis on succession planning, with five pairs selected to be part of a pilot succession planning program, with a special emphasis on the role of the Chief Administrative Officer / Senior Business Officer. In addition, the University had made a commitment to mentor internationally trained professionals who were looking for employment in the Toronto area. This program was offered through the Toronto Region Immigrant Employment Council (TRIEC). The Ontario Institute for Studies in Education of the University of Toronto (OISE/UT) was offering M.Ed. and certificate programs in Higher Education with a special emphasis on leadership. Professor Hildyard taught in that program, which had enrolled 38 staff members in its first year. The University had also entered into a partnership with the School of Continuing Studies to offer senior professionals / managers a special rate on courses in its Strategic Leadership Program. Finally, Human Resources staff continued to work in cooperation with staff in the Office of the Vice-President and Provost to offer training to new academic administrators.

- **Workplace wellness**. The University had been named a Top 10 Family Friendly Employer for 2007 and given a Corporate Award for Employee Assistance Program

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Excellence by the Employee Assistance Society of North America. It had held a week-long series of events entitled "Adding Balance to Every Day." It had begun a pilot program on telecommuting with two departments in Facilities and Services. It had increased access to the support programs provided by the Family Care Office and had held an Elder Care Fair.

- **Health and well-being**. The University had taken a more proactive approach to assisting employees to return to work after sick leave or long-term disability and to accommodate them when required to deal with disabilities. The University had noted an increase in stress and mental-health issues and was taking steps to assist employees in dealing with them. It had continued its focus on health promotion, for example encouraging hand-washing and offering blood-pressure clinics.

- **Health and safety** was a matter of particular interest to the Board, given the personal legal liability of members for any University failure to exercise due diligence in ensuring compliance with health and safety law and regulations. The University was focusing on risk management within an increasingly regulated environment. The Ontario Ministry of Labour classified the universities as part of the educational sector, which included primary and secondary school boards. Given the broad range of university activities, they had higher rates of critical and general accidents, and all Ontario universities had been placed by the Ministry on a "last chance list" for the 10% of institutions with the worst accident rates. The University was addressing the implications of that situation. It was developing performance indicators in the area of health and safety and was increasing the use of e-learning to broaden the reach of training in the area. With respect to the worker / management Joint Health and Safety Committees, Professor Hildyard was pleased to report an increase from 46% to 77% in the rate of compliance with the requirement that the Committees be duly constituted and meet at least four times annually. The problem of non-compliance was complicated by the fact that there were too many such committees, some established under collective agreements, and the University was continuing to work on the consolidation of the committees to a more appropriate number.

  There had been a substantial decline over the past few years in the number of work days lost because of accidents and in the average number of days lost per accident. The largest number of accidents had occurred among members of the skilled trades, caretaking and grounds staff, daycare workers and support staff, and hospitality workers at the 89 Chestnut Street Residence. The average rate of lost-time accidents among the trades workers, the caretaking and grounds staff and the University police was 4.2% compared to the U.S. university benchmark of 4.4%. The most frequent accidents involved contacts (striking or being struck by things), falls and manual materials handling. The University was continuing its effort to improve its safety record, focusing on accident prevention.

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- **Equity and diversity**. Professor Hildyard noted that the eleven equity offices currently made annual reports through her to the University Affairs Board. She anticipated that their report would also come to the Business Board in 2009. There had been an increase in the collaboration among the equity offices and the divisions. There had been an increase in the awareness of equity-related policies and resources. The "EQ ITY - it includes you" campaign had been a very helpful tool in making the point that equity was the responsibility of all members of the University. Sessions in cultural fluency and other equity topics had been held in the divisions to build the capacity to address differences in cultural values.

- **Equity and diversity**: **Divisional initiatives**. The Faculty of Applied Science and Engineering had sponsored outreach programs to schools to promote engineering careers to diverse students. The Faculty of Arts and Science had undertaken an initiative to diversify its curriculum to reflect better the diversity of its student body. The Faculty of Law had established an accessibility and diversity committee. The Faculty of Medicine had appointed an Associate Dean for Equity and Professionalism. All divisions were working on equity and diversity issues.

- **Employment equity: Academic highlights**. Over 50% of all faculty hired in 2007 were women – a landmark achieved for the first time in 2007. Overall, women formed 34.8% of the faculty compared to external availability of 36.2%. Members of visible minorities were 13.3% of the faculty, compared to external availability of the same proportion, 13.3%. Aboriginal people and people with disabilities were still under-represented. Sexual minorities formed 4.4% of the faculty. There were no external availability data for that group. In academic leadership positions, the proportion of women was again close to the availability data. In other categories, members of the designated groups were still under-represented.

- **Employment equity: Administrative staff**. Women formed 62.4% of the administrative staff of the University, exceeding external availability in most categories. Members of visible minorities were 29.9% of the staff, exceeding external availability in many categories. Members of sexual minorities formed 4.6% of the administrative staff; again there were no external availability data. As in previous years, aboriginal people and persons with disabilities were under-represented in several categories. The number of staff members from the designated groups taking advantage of training and development opportunities was consistent with the representation of those groups in the staff.

- **Employment equity: Current initiatives**. As noted, four working groups had been formed to follow up on the employee experience survey, including one with a specific focus on equity. That group would follow up on the small proportion of employees who reported sometimes feeling left out or treated unfairly owing to their gender, ethnic or

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cultural origin, religious affiliation, disability or sexual orientation. Work was being carried out to determine ways to improve faculty recruitment, integration, promotion and retention, using the data from the employee satisfaction survey augmented by data obtained through the Collaborative on Academic Careers in Higher Education (COACHE). A Human Resources toolkit was being developed to facilitate outreach to diverse communities to broaden the applicant pool for the recruitment of administrative staff. An awareness campaign was being developed to foster understanding concerning mental health issues. Finally, the University, through its special Human Resources officer for Aboriginal peoples, was establishing a career development program for Aboriginal employees. Professor Hildyard noted that she represented the Council for Ontario Universities on the Ontario government's Committee for Employment Standards, established pursuant to the *Accessibility for Ontarians with Disabilities Act*. Her experience in that role had enabled her to confirm that the University's outreach and support efforts surpassed those of the majority of other employers.

Among the matters that arose in questions and discussion were the following.

(a) Internal promotion. A member noted that over 30% of the University's employees did not believe that promotions, transfers and appointments were made fairly at the University. Of all of the postings for administrative staff positions in 2007, over 45% had gone to external candidates. Given that the University prided itself on having the best employees, it seemed unreasonable that so high a proportion of postings would be filled by people other than current University staff. Ms Sass-Kortsak replied that the postings represented a very real mix of positions. Many were entry-level positions, in which staff already employed at the University would have no interest. Others were highly specialized positions such as laboratory technicians or information-technology specialists, for which no internal candidate would be qualified. The University did emphasize career development. It had considered the question of the ideal proportion of positions to be filled by internal and external candidates, and it recognized that the current proportion might not be the ideal one.

(b) On-line application for administrative staff positions and security of personal data. A member noted that the on-line application process was handled by a U.S. corporation. As a result, data could end up with the U.S. Department of Homeland Security and it could be the basis of such damaging actions such as the placement of an applicant on the U.S. "no fly" lists. Ms Sass-Kortsak and, at the invitation of the Chair, Mr. Moate, replied that the system of on-line applications was managed by the Taleo Corporation, and its offices and computer servers were located in the United States. That fact was made clear on the application system. It was Mr. Moate's view, as well as that of the Freedom of Information / Protection of Privacy Officer and others, that the use of the system did not violate Ontario or federal legislation concerning the protection of privacy. The Government of Canada had decided not to place any restriction on the processing or holding of information by foreign corporations such as Taleo. The *Patriot Act* in the United States did give the U.S. government the potential plenipotentiary power to gain access

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to any information stored by U.S. corporations. However, given the nature of the operation and the legality of the process according to Canadian law, the University deemed the application process to be an appropriate one and, given the absence of satisfactory domestic alternatives, a useful one. Internal candidates for positions who were concerned about the of the privacy of their information were given the option of applying by means of a paper application rather than the on-line system. Mr. Moate noted that the matter had been raised by the United Steelworkers' Union and that a response had been provided to it.

(c) Reconciliation of the achievement of equity goals with the commitment to hiring the best candidate. A member asked how the University would set about employing members of designated groups and at the same time employing the best candidate for a position. Professor Hildyard replied that the University focused on obtaining as broad and deep an applicant pool as possible from which the best qualified applicants would be interviewed. If, for example, all of the applications for a given position were males, the University would be proactive and would encourage more outreach to attract female applicants. In addition, the University made efforts to provide training and development opportunities that would ensure the success of current employees, including those who were members of the designated groups. The outreach efforts to Aboriginal organizations was an example of a major effort currently underway.

(d) Cost-effectiveness of the equity offices. A member noted that there were eleven different equity offices. There had, however, been no discussion of the costs of those offices or whether the existence of different offices represented the most cost-effective way of providing their services. Professor Hildyard noted that there was a detailed report on the work of the equity offices, which would be presented to the University Affairs Board the next day. There were few benchmarks of cost effectiveness. While it would be possible to consider the number of complaints they handled, a major goal of the offices was to improve the culture of the University with respect to the members of the designated groups. Ms Sass-Kortsak also noted that the equity offices often had multiple functions. For example, the Health and Well-Being officer had multiple functions, including the equity function. Professor Hildyard took under advisement the member's question on the measurement of cost-effectiveness in relation to outcomes.

6. Quarterly Report on Compliance with Legal Requirements

The Board received for information the quarterly report, dated April 17, 2008, on compliance with the University's health and safety obligations.

7. Professional and Managerial Staff – Policy Revisions

The Chair noted that the proposed policy revisions had been reviewed and endorsed by the Senior Appointments and Compensation Committee of the Governing Council.

7. Professional and Managerial Staff – Policy Revisions (Cont'd)

Professor Hildyard said that there were three changes proposed to the Compensation Policy for professionals and managers. First, a new paragraph in the introduction to the Policy made clear that the University would focus on performance and contribution in its compensation decisions. Second, the PM 6 salary group was to be included in the group for which salary increases would be based solely on an annual assessment of merit; there would be no across-the-board increase for positions in the PM 6 and more senior categories. Increases would be accelerated for good performers until the salary reached the breakpoint, after which they would increase at a reduced rate. Third, for professionals and managers whose salaries were above the notional maxima for their salary ranges, increases would be administered in accordance with the regulations approved by the Senior Appointments and Compensation Committee. For professionals and managers who had reached the maximum of the salary range and who provided exceptional effort or contribution, one-time-only payments could be made. Approval would be required for such payments above a level specified by the Vice-President, Human Resources and Equity. At present, that level was $5,000. Professor Hildyard had not wanted to specify that maximum in the Policy, however, in order to avoid the need for frequent policy revisions to take inflation or other factors into account.

Professor Hildyard said that the proposed revisions to the Problem Resolution Policy had arisen from the request of the professional / managerial group itself. Among other changes, a professional or manager would be entitled to seek advice from a Human Resource Manager from any University office rather than only from the officer in the staff member's own unit, who might well already be involved in the matter. In addition, the professional / manager would have the opportunity to present a complaint up the organizational ladder or directly to the Vice-President, Human Resources and Equity. The members of the professional / managerial group were pleased with the proposed revisions, which they thought would bring about a much improved Policy.

On the recommendation of the Vice-President, Human Resources and Equity,

YOUR BOARD APPROVED

The revised Policy on Compensation for Professionals/Managers, a copy of which is attached hereto as Appendix "C"; and

The revised Policy on Problem Resolution for Professionals/Managers, a copy of which is attached hereto as Appendix "D".

The Chair, on behalf of the Board, thanked Professor Hildyard, Ms Sass-Kortsak and their colleagues for their reports and proposals, and for their work to serve the University and its employees. Their work was very much appreciated.

8. Ancillary Operations: Residential Housing – Operating Results and 2008-09 Plan

On the recommendation of the Vice-President, Business Affairs,

YOUR BOARD APPROVED

The operating budget for the St. George Campus Residential Housing Ancillary for 2008-09, as contained in the "2008-09 Budget" column of Schedule 1 to the "Overview of Operations and Business Plan for 2008-2013."

9. Capital Projects Report as at March 31, 2008

The Board received for information the Report on Capital Projects as at March 31, 2008.

10. Borrowing: Status Report to March 31, 2008

The Board received for information the Status Report on Borrowing as at March 31, 2008.

11. Reports of the Administrative Assessors

University Credit Rating Report

Ms Riggall drew members' attention to the April 15, 2008 Credit Opinion from Moody's Investors Service, which reaffirmed the University's credit rating at Aa1, with a stable outlook.

12. Date of Next Meeting

The Chair reminded members that the next regular meeting was scheduled for Thursday**,** June 19, 2008 at 5:00 p.m. That meeting would, among other things, consider the report of the Audit Committee on the audited financial statements for 2007-08.

13. Other Business

Human Resources: Early Retirement Window for Staff Members Represented by the United Steelworkers of America, Local 1998

A member recalled that the Board had in April 2006 acted, on the recommendation of the Vice-President, Human Resources and Equity, to extend the early retirement window for members of the staff represented by the Steelworkers' union. He understood that the administration had decided not to recommend an extension upon the expiry of the current collective agreement on June 30, 2008. The window had previously been extended as a prelude to negotiations between the parties. That had been a reasonable course of action then and there

13. Other Business (Cont'd)

Human Resources: Early Retirement Window for Staff Members Represented by the United Steelworkers of America, Local 1998 (Cont'd)

had been no rationale offered as to why it was not a reasonable course of action at this time. The cost would be negligible.

THE BOARD MOVED IN CAMERA.

Professor Hildyard responded to the question *in camera*.

14. Real Estate Transactions

The Board considered and approved recommendations from the Chief Real Estate Officer concerning two real estate transactions.

15. Human Resources: Professional, Managerial and Confidential Staff and English-as-a-Second-Language Instructors – Salary Increase, July 1, 2008

The Board considered a recommendation from Professor Hildyard with respect to the July 1, 2008 salary increase for professional, managerial and confidential staff and English-as-a-Second-Language instructors.

On the recommendation of the Vice-President, Human Resources and Equity,

YOUR BOARD APPROVED

The July, 2008 salary increases for Professionals and Managers, Confidentials and English-as-a-Second Language Instructors, as proposed in Professor Hildyard's memorandum to the Business Board of April 17, 2008.

THE BOARD RETURNED TO OPEN SESSION.

The meeting adjourned at 7:00 p.m.

Secretary　　　　　　Chair

May 26, 2008

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