

**Report of the State Board of Education
Committee on School Finance/Permanent School Fund
July 16, 2015**

The State Board of Education Committee on School Finance/Permanent School Fund met at 9 a.m. on Thursday, July 16, 2015, in Room #1-104 of the William B. Travis Building, 1701 N. Congress Avenue, Austin, Texas. All members of the committee were present, as follows:

Presiding: Pat Hardy, chair; Lawrence A. Allen, Jr., vice chair; David Bradley; Ken Mercer; Thomas Ratliff

Public Testimony

This item provides an opportunity for the public to present testimony at the time the related item comes up for committee discussion or action. The procedures for registering and taking public testimony at State Board of Education committee meetings and general board meetings are provided at [http://tea.texas.gov/About TEA/Leadership/State Board of Education/SBOE Meetings/SBOE Operating Rules Amended 4-17-15/](http://tea.texas.gov/About_TEA/Leadership/State_Board_of_Education/SBOE_Meetings/SBOE_Operating_Rules_Amended_4-17-15/) or in the information section (yellow pages) of the agenda.

The Committee on School Finance/Permanent School Fund heard public testimony on agenda item #3. Information regarding the individuals who presented public testimony is included in the discussion of that item.

CONSENT ITEM

1. Per Capita Apportionment Rate for the 2014-2015 School Year

(Board agenda page III-1)
[Consent agenda item #(5)]

Lisa Dawn-Fisher, associate commissioner of school finance and chief school finance officer, presented this consent item. Dr. Dawn-Fisher explained that the per capita apportionment rate for the 2014-2015 school year was up slightly from \$257.274 to \$263.596 (Attachment A).

MOTION AND VOTE: *It was moved by Mr. Ratliff, seconded by Mr. Allen, and carried unanimously to recommend that the State Board of Education adopt a per capita apportionment rate of \$263.596 for the 2014-2015 school year.*

ACTION ITEMS

2. Proposed Amendment to 19 TAC Chapter 33, Statement of Investment Objectives, Policies, and Guidelines of the Texas Permanent School Fund, Subchapter A, State Board of Education Rules, §33.65, Bond Guarantee Program for School Districts

(First Reading and Filing Authorization)

(Board agenda page III-3)

[Official agenda item #13]

Dr. Dawn-Fisher presented this action item. Dr. Dawn-Fisher explained that amendments were made regarding the criteria for rating firms conducting ratings for the Bond Guarantee Program. Holland Timmins, executive administrator and chief investment officer of the Texas Permanent School Fund, explained that the criteria were formed based on a request for qualifications (RFQ).

Mr. Bradley requested that the item be brought to the next State Board of Education Committee on School Finance/Permanent School Fund for second reading with language clarifying that bonds be used for facilities directly related to educational purposes.

The committee discussed the implications of increasing the capacity multiplier to guarantee bonds.

MOTION AND VOTE: *It was moved by Mr. Bradley and seconded by Mr. Allen to amend the third sentence of 19 TAC §33.65(e)(1) as follows:*

The calculation capacity will be based on a multiplier of three and a half [~~three~~] times the cost value of the PSF.

The motion failed, with 2 members voting Aye and 3 members voting No, as follows:

<u>Aye:</u>	<i>Mr. Bradley</i>
	<i>Mr. Mercer</i>
<u>No:</u>	<i>Mr. Allen</i>
	<i>Ms. Hardy</i>
	<i>Mr. Ratliff</i>

MOTION AND VOTE: *It was moved by Mr. Ratliff, seconded by Mr. Bradley, and carried unanimously to recommend that the SBOE approve for first reading and filing authorization the proposed amendment to 19 TAC Chapter 33, Statement of Investment Objectives, Policies, and Guidelines of the Texas Permanent School Fund, Subchapter A, State Board of Education Rules, §33.65, Bond Guarantee Program for School Districts.*

3. **Proposed Amendment to 19 TAC Chapter 33, Statement of Investment Objectives, Policies, and Guidelines of the Texas Permanent School Fund, Subchapter A, State Board of Education Rules, §33.67, Bond Guarantee Program for Charter Schools**

(First Reading and Filing Authorization)

(Board agenda page III-17)

[Official agenda item #14]

The following individuals provided public testimony:

NAME: David Dunn
AFFILIATION: Texas Charter School Association

NAME: Thomas Sage
AFFILIATION: Andrews Kurth LLP

Dr. Dawn-Fisher presented this item. Dr. Dawn-Fisher explained that proposed amendments would require firms that rated charter schools for the Bond Guarantee Program to have at least one previous charter school rating before being approved.

The committee discussed the 5% capacity in reserve to prevent going over capacity, denial of bonds based on covenant violation to a financial obligation, and classification of property bought with state funds as state property in the Annual Financial Report.

MOTION AND VOTE: *It was moved by Mr. Bradley, seconded by Mr. Allen, and carried unanimously to delete the amendment to 19 TAC §33.67(f)(5)(F) that states:*

The charter district must classify all property purchased or improved with bond proceeds that is serviced with state funds as state property in the charter district's annual financial report.

MOTION AND VOTE: *It was moved by Mr. Ratliff, seconded by Mr. Allen, and carried unanimously to recommend that the SBOE approve for first reading and filing authorization the proposed amendment to 19 TAC Chapter 33, Statement of Investment Objectives, Policies, and Guidelines of the Texas Permanent School Fund, Subchapter A, State Board of Education Rules, §33.67, Bond Guarantee Program for Charter Schools, as amended, and to place this item on the consent agenda of the State Board of Education meeting of July 17, 2015.*

DISCUSSION ITEM

4. **Review of Permanent School Fund Securities Transactions and the Investment Portfolio**

(Board agenda page III-39)

Catherine Civileto, deputy executive administrator, provided a summary on the status of the Permanent School Fund portfolio. Reports presented to the committee were for the reporting period March 1 through May 31, 2015, unless otherwise noted. Ms. Civileto's report included reporting on the current fair market value of the Fund, the asset allocation mix as of May 31, 2015, PSF transactions occurring in the reporting period, revenues and expenditures for the fiscal period September 1, 2014 through May 31, 2015, the activity on the securities lending program for the fiscal period September 1, 2014 through May 31, 2015, the status of transfers from the General Land Office as per the resolution they agreed to for the current fiscal year, current status of the

Bond Guarantee Program and the available capacity in the program, broker commissions on both the internal and external equity portfolios for the period beginning January 1, 2015 through May 31, 2015, and short-term cash investments.

CONSENT ITEM

5. Ratification of the Purchases and Sales of the Investment Portfolio of the Permanent School Fund for the Months of March, April, and May 2015

(Board agenda page III-31)

[Consent agenda item #(6)]

MOTION AND VOTE: *Based on the information provided by staff and the recommendation of the executive administrator and chief investment officer and the commissioner of education, the committee recommended by unanimous consent to ratify the purchases and sales for the months of March, April, and May 2015 in the amount of \$1,150,624,120 and \$1,228,684,326, respectively, (Attachment B).*

DISCUSSION ITEM

6. First Quarter 2015 Permanent School Fund Performance Report

(Board agenda page III-41)

Tom Heiner, vice president and senior analytics consultant and Scott Berard, regional manager and investment analytics consultant with BNY Mellon performance and Risk Analytics, presented the first quarter of 2015 Permanent School Fund performance report. Mr. Heiner began with an overview of the U.S. and foreign capital markets. Mr. Heiner then reviewed the performance of the Fund for the first quarter 2015. He stated that the PSF returned 1.76% for the first quarter outperforming the target benchmark by 17 basis points. The Fund ranked in the 89th percentile of the Mellon Universe of Public Funds greater than \$1.0 billion for the 3-month period ending March 31, 2015.

Mr. Heiner reviewed first quarter 2015 performance of the Permanent School Fund by asset class, stating that the total domestic large cap equity composite outperformed its benchmark by two basis points for the quarter. Mr. Heiner added that Small/Midcap Equity portfolio outperformed its benchmark by four basis points. He added that international equities returned 3.49% for the quarter, having performed in line with its benchmark during the period. The fixed income portfolio returned 1.92% for quarter, exceeding its benchmark by 35 basis points. Mr. Berard stated that the Absolute Return composite returned 1.73% for the quarter, underperforming its benchmark, the HFRI Fund of Funds Composite Index, by 60 basis points. Mr. Berard added that the Real Estate composite returned 2.41% for the quarter, underperforming its benchmark by 71 basis points. Mr. Berard added that Total Risk Parity Strategies returned 3.82% in the fourth quarter of 2015, outperforming its benchmark by 230 basis points. He further stated that the Real Return Asset class returned -1.57% for the quarter, coming in above its benchmark by 66 basis points. He added that Emerging Market Debt returned -3.59% for the quarter, exceeding its benchmark by 37 basis points. Finally, Mr. Berard stated that private equity returned 1.62% for the quarter, falling short of its benchmark by 88 basis points for the quarter ending March 31, 2015.

CONSENT ITEM

7. Decision on Real Estate Investments

(Board agenda page III-33)
[Consent agenda item #(7)]

The PSF real estate consultant, Courtland Partners, was represented by Steve Novick, Principal/Chief Operating Officer, and was joined by John Grubenman, director of private markets for PSF. Mr. Grubenman provided an introduction to a real estate investment recommendation and Mr. Novick presented the *European Property Investors Special Opportunities 4, L.P.* offered by *Tristan Capital Partners LLP*, as General Partner. Mr. Novick described the due diligence process conducted by both Courtland and PSF staff, provided a brief overview including its objectives and strategy, and outlined the merits and considerations. Mr. Grubenman stated that the board would need to approve a waiver of the requirement for service providers to be registered with the Securities and Exchange Commission and also review and approve the manager's relationship with a placement agent.

MOTION AND VOTE: *The committee recommends to the State Board of Education approval to execute agreement(s) with Tristan Capital Partners LLP, necessary to make an investment commitment of up to €50 million in European Property Investors Special Opportunities 4, L.P., a euro denominated fund, subject to continued due diligence and negotiation of fund terms, to approve the relationship between Tristan Capital Partners LLP and LAZARD FRÈRES & CO. LLC, after determining it meets the standards of 19 TAC Chapter 33, Section(j)(5), which has been disclosed in writing, and also, to approve a waiver of the PSF Real Estate Investment Policy Statement requirement for the investment manager (Tristan) to be a registered investment advisor with the Securities Exchange Commission and authorization for contract execution by the Commissioner of Education.*

DISCUSSION ITEM

8. Overview on Permanent School Fund Private Equity Program

(Board agenda page III-43)

Mr. Grubenman and Rhett Humphreys, partner at NEPC, gave a presentation on the private equity asset class. Mr. Grubenman described the current structure of the asset class. Mr. Humphreys described structures for the private equity program after the current phase expires. The committee directed staff to provide additional information regarding the private equity program structure at the September meeting.

CONSENT ITEMS

9. Approval of Pool of Qualified Respondents to the Request for Qualifications (RFQ) for Rating Agencies for the Permanent School Fund

(Board agenda page III-35)

[Consent agenda item #(8)]

Ms. Hardy called on Mr. Timmins, executive administrator and chief investment officer, to address the item. Mr. Timmins stated the goal of the RFQ was to identify credit ratings firms qualified to provide credit rating services for the Texas Permanent School Fund investment portfolio and the bond guarantee program.

Mr. Timmins summarized the responses to the RFQ and answered questions from Mr. Ratliff about the number of rating agencies active in rating charter schools and the fees associated with such ratings.

MOTION AND VOTE: *By unanimous consent, the committee recommended to the State Board of Education to approve the following credit rating agencies: Fitch, Standard & Poor's, and Moody's, to provide credit rating services for the Texas Permanent School Fund's bond guarantee program.*

10. Presentation by Finalist Candidates for Investment Counsel Services for the Permanent School Fund

(Board agenda page III-37)

[Consent agenda item #(9)]

Mr. Timmins provided the committee an overview of the Investment Counsel RFP evaluation process. The two finalists, NEPC and Wilshire, presented to the committee about services.

MOTION AND VOTE: *It was moved by Mr. Allen, seconded by Mr. Ratliff, and carried by unanimous vote to recommend to the State Board of Education to approve an agreement with NEPC, LLC for investment counsel services for the Texas Permanent School Fund (RFP #701-15-023), subject to fee negotiation, and for authorization for contract execution by the Commissioner of Education.*

DISCUSSION ITEM

11. Report of the Permanent School Fund Executive Administrator and Chief Investment Officer

(Board agenda page III-45)

Mr. Timmins provided the committee an update from the 84th Legislative Session. He also provided the committee an update on the PSF investment manager watch list.

The meeting of the Committee on School Finance/Permanent School Fund adjourned at 2:45 p.m.