

ATTACHMENT II
Text of Proposed Amendments 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

§33.15. Objectives.

- (a)-(b) (No change.)
- (c) Investment rate of return and risk objectives.
 - (1)-(4) (No change.)
 - (5) The rate of return objective of the total PSF fund shall be to earn, over time, an average annual total rate of return that meets or exceeds the rate of return of a composite benchmark index, consisting of representative benchmark indices for the asset classes in which the PSF is invested that are aggregated in proportion to the strategic target asset allocation of the total PSF fund as determined by the SBOE ~~[actual asset allocation of the PSF for the relevant time period]~~, while maintaining an acceptable risk level compared to that of the composite benchmark index.
 - (6) The rate of return objective of each asset class in which the PSF is invested, other than the short-term cash fund, shall be to earn, over time, an average annual average rate of return that meets or exceeds that of a representative benchmark index for such asset class in U.S. dollars, combining dividends, capital appreciation, income, and interest income, as applicable, while maintaining an acceptable risk level compared to that of the representative benchmark index.
 - (7) The objective of the short-term cash fund shall be to provide liquidity for the timely payment of security transactions, while earning a competitive return. The expected return, over time, shall meet or exceed that of the representative benchmark index, while maintaining an acceptable risk level compared to that of the representative benchmark index.
 - (8) (No change.)
- (d) (No change.)

§33.20. Responsible Parties and Their Duties.

- (a) The Texas Constitution, Article VII, §§1-8, establishes the Available School Fund, the Texas Permanent School Fund (PSF), and the State Board of Education (SBOE), and specifies the standard of care SBOE members must exercise in managing PSF assets. In addition, the constitution directs the legislature to establish suitable provisions for supporting and maintaining an efficient public free school system, defines the composition of the PSF and the Available School Fund, and requires the SBOE to set aside sufficient funds to provide free instructional materials for the use of children attending the public free schools of this state.
- (b) The SBOE shall be responsible for overseeing all aspects of the PSF and may contract with any of the following parties, whose duties and responsibilities are as follows.
 - (1) An external investment manager is a Person the SBOE retains by contract to manage and invest a portion of the PSF assets under specified guidelines.
 - (2) A custodian is an organization, normally a financial company, the SBOE retains to safe keep, and provide accurate and timely reports of, PSF assets.
 - (3) A consultant is a Person the SBOE retains to advise the SBOE on PSF matters based on professional expertise.
 - (4) Investment Counsel is a Person retained under criteria specified in the PSF Investment Procedures Manual to advise PSF investment staff and the SBOE Committee on School Finance/Permanent

School Fund within the policy framework established by the SBOE. Investment Counsel may be assigned such tasks as asset allocation reviews, manager searches, performance analysis, recommendations on spending policy, performance reporting, and benchmarking [recommendations] and research related to the management of PSF assets, with any such assigned tasks to be performed in consultation with PSF staff.

- (5) A performance measurement consultant is a Person retained to provide the SBOE Committee on School Finance/Permanent School Fund an analysis of the PSF portfolio performance. The outside portfolio performance measurement service firm shall perform the analysis on a quarterly or as-needed basis. Quarterly reports shall be distributed to each member of the SBOE Committee on School Finance/Permanent School Fund and Investment Counsel, and a representative of the firm shall be available as necessary to brief the committee.
 - (6) The State Auditor's Office is an independent state agency that performs an annual financial audit of the Texas Education Agency (TEA) at the direction of the Texas Legislature. The financial audit, conducted according to generally accepted auditing standards, is designed to test compliance with generally accepted accounting principles. The state auditor performs tests of the transactions of the PSF Investment Office as part of this annual audit, including compliance with governing statutes and SBOE policies and directives. The TEA Internal Audit Division will participate in the audit process by participating in entrance and exit conferences, being provided copies of all reports and management letters furnished by the external auditor, and having access to the external auditor's audit programs and working papers.
 - (7) The SBOE may retain independent external auditors to review the PSF accounts annually or on an as-needed basis. The TEA Internal Audit Division will participate in the audit process by participating in entrance and exit conferences, being provided copies of all reports and management letters furnished by the external auditor, and having access to the external auditor's audit programs and working papers.
- (c) The SBOE shall meet on a regular or as-needed basis to conduct the affairs of the PSF.
- (d) In case of emergency or urgent public necessity, the SBOE Committee on School Finance/Permanent School Fund or the SBOE, as appropriate, may hold an emergency meeting under the Texas Government Code, §551.045.
- (e) The SBOE shall have the following exclusive duties:
- (1) determining the strategic asset allocation mix between asset classes based on the attending economic conditions and the PSF goals and objectives;
 - (2) ratifying all investment transactions pertaining to the purchase, sale, or reinvestment of assets by all internal and external investment managers for the current reporting period;
 - (3) appointing members to the SBOE Investment Advisory Committee;
 - (4) approving the selection of, and all contracts with, external investment managers, financial advisors, Investment Counsel, financial or other consultants, or other external professionals retained to help the SBOE invest PSF assets;
 - (5) approving the selection of, and the performance measurement contract with, a well-recognized and reputable firm retained to evaluate and analyze PSF investment results. The service shall compare investment results to the written investment objectives of the SBOE and also compare the investment of the PSF with the investment of other public and private funds against market indices and by managerial style;
 - (6) setting policies, objectives, and guidelines for investing PSF assets; and
 - (7) representing the PSF to the state.
- (f) The SBOE may establish committees to administer the affairs of the PSF. The duties and responsibilities of any committee established shall be specified in the PSF Investment Procedures Manual.

- (g) The PSF shall have an executive administrator, with a staff to be adjusted as necessary, who functions directly with the SBOE through the SBOE Committee on School Finance/Permanent School Fund concerning investment matters, and who functions as part of the internal operation under the commissioner of education. At all times, the PSF executive administrator and staff shall invest PSF assets as directed by the SBOE according to the Texas Constitution and all other applicable Texas statutes, as amended, and SBOE rules governing the operation of the PSF. The PSF staff shall:
- (1) administer the PSF, including investing and managing assets and contracting in connection therewith, according to SBOE goals and objectives;
 - (2) execute all directives, policies, and procedures from the SBOE and the SBOE Committee on School Finance/Permanent School Fund;
 - (3) keep records and provide a continuous and accurate accounting of all PSF transactions, revenues, and expenses and provide reports on the status of the PSF portfolio;
 - (4) advise any officials, investment firms, or other interested parties about the powers, limitations, and prohibitions regarding PSF investments that have been placed on the SBOE or PSF investment staff by statutes, attorney general opinions and court decisions, or by SBOE policies and operating procedures;
 - (5) continuously research all internally managed securities held by the PSF and report to the SBOE Committee on School Finance/Permanent School Fund and the SBOE any information requested, including reports and statistics on the PSF, for the purpose of administering the PSF;
 - (6) establish and maintain a procedures manual that implements this section to be approved by the SBOE;
 - (7) make recommendations regarding investment and policy matters to the SBOE Committee on School Finance/Permanent School Fund and the SBOE , except for formal recommendations for benchmarks for internally managed PSF asset classes, which duties the Committee will assign to an appropriate third party who will present such recommendations after consultation with PSF staff ; and
 - (8) establish and maintain accounting policies and internal control procedures concerning all receipts, disbursements and investments of the PSF, according to the procedures adopted by the SBOE.