

**Report of the State Board of Education  
Committee on School Finance/Permanent School Fund  
September 14, 2017**

The State Board of Education Committee on School Finance/Permanent School Fund met at 9:05 a.m. on Thursday, September 14, 2017, 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: David Bradley, chair; Tom Maynard, Vice Chair; Lawrence A. Allen, Jr.; Patricia Hardy; Ken Mercer

Non-Committee Members Present: Donna Bahorich; Keven Ellis; Geraldine “Tincy” Miller

**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\\_1-31-17/](http://tea.texas.gov/About_TEA/Leadership/State_Board_of_Education/SBOE_Meetings/SBOE_Operating_Rules_Amended_1-31-17/) or in the information section (yellow pages) of the agenda.

The Committee on School Finance/Permanent School Fund received no presentations of public testimony.

**ACTION ITEM**

- 1. Proposed Amendment to 19 TAC Chapter 105, Foundation School Program, Subchapter A, Definitions, §105.1, Rules for the Definition of Tax Levy and Tax Collection**  
(Second Reading and Final Adoption)  
(Board agenda page III-1)  
[Official agenda item #7]

Leo Lopez, chief school finance officer, presented this item. This item would amend the definition of tax collections to comply with Texas Tax Code.

**MOTION AND VOTE:** *It was moved by Mr. Maynard, seconded by Ms. Hardy, and carried unanimously to recommend that the State Board of Education approve for second reading and final adoption the proposed amendment 19 TAC Chapter 105, Foundation School Program, Subchapter A, Definitions, §105.1, Rules for the Definition of Tax Levy and Tax Collection.*

## CONSENT ITEM

### **2. Per Capita Apportionment Rate for the 2017-2018 School Year**

(Board agenda page III-5)

[Consent agenda item #(1)]

Mr. Lopez presented this item. This item proposes a preliminary per capita apportionment rate of \$206.566. Mr. Lopez answered questions from Mr. Bradley and Mr. Maynard regarding the per capita apportionment rate.

**MOTION AND VOTE:** *It was moved by Ms. Hardy, seconded by Mr. Mercer, and carried unanimously to recommend that the State Board of Education adopt the recommended per capita rate for the 2017-2018 school year.*

## DISCUSSION ITEMS

### **3. Discussion of Proposed Amendment to 19 TAC Chapter 109, Budgeting, Accounting, and Auditing, Subchapter D, Uniform Bank Bid or Request for Proposal and Depository Contract, §109.52, Uniform Depository Bank Contract and Surety Bond Forms**

(Board agenda page III-19)

David Marx, director of Financial Compliance, presented this item. This item would update the depository contract adopted in rule to comply with changes made in Senate Bill (SB) 754.

### **4. Discussion of Proposed Amendment to 19 TAC Chapter 129, Student Attendance, Subchapter B, Student Attendance Accounting, §129.21, Requirements for Student Attendance Accounting for State Funding Purposes**

(Board agenda page III-33)

Mr. Marx presented this item. This item would update code to comply with SB 1152 and allow students that are pursuing enlistment in the military to be counted as present for funding purposes. Mr. Marx answered questions from Mr. Mercer regarding the amendment.

### **5. Texas Education Agency Legislative Appropriation Comparison by Major Component Fiscal Years 2016-2017 Compared to Fiscal Years 2018-2019 and Fiscal Year 2018 Administrative and Program Budgets**

(Board agenda page III-39)

Mary Ann Uranga Gill, budget director, presented a comparison of the Fiscal Years 2016-2017 budget to the Fiscal Years 2018-2019 budget. Ms. Uranga Gill explained some of the large variances in the budget and answered several questions from committee members related to the variances and the reduction of the budget.

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

(Board agenda page III-41)

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 May 1, 2017 through July 31, 2017 unless otherwise noted. Ms. Civileto's report included reporting on the current fair market value of the Fund, the asset allocation mix as of July 31, 2017,

PSF transactions occurring in the reporting period, revenues and expenditures for the fiscal period September 1, 2016 through July 31, 2017, the historical activity on the securities lending program for the fiscal period September 1, 2016, through July 31, 2017, 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 bond guarantee program, broker commissions on both the internal and external equity portfolios for the period beginning January 1, 2017 through July 31, 2017, internal fixed income ratings for the fiscal period from September 1, 2016 through July 31, 2017 and short-term cash investments for May, June and July 2017.

## **CONSENT ITEM**

- 7. Ratification of the Purchases and Sales of the Investment Portfolio of the Permanent School Fund for the Months of May, June and July 2017**  
**(Board agenda page III-7)**  
[Consent agenda item #(2)]

**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 May, June and July 2017, in the amount of \$1,313,244,900 and \$1,279,125,889 respectively (Attachment A).*

## **DISCUSSION ITEM**

- 8. Second Quarter 2017 Permanent School Fund Performance Report**  
(Board agenda page III-43)

Tom Heiner of BNY Mellon Global and Risk Solutions, presented the second quarter of 2017 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 second quarter of 2017. He stated that the PSF returned 2.87% for the second quarter outperforming the target benchmark by 17 basis points.

Mr. Heiner reviewed second quarter 2017 performance of the Permanent School Fund by asset class, stating that the total domestic large cap equity composite outperformed its benchmark by one 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 6.10% for the quarter, exceeding its benchmark by 24 basis points during the period. The fixed income portfolio returned 1.62% for quarter, exceeding its benchmark by 17 basis points. Mr. Heiner stated that the Absolute Return composite returned 0.59% for the quarter, underperforming its benchmark, the HFRI Fund of Funds Composite Index, by 19 basis points. Mr. Heiner added that the Real Estate composite returned 3.16% for the quarter, outperforming its benchmark by 118 basis points. Mr. Heiner added that Total Risk Parity Strategies returned 1.11% in the second quarter of 2017, underperforming its benchmark by 132 basis points. He further stated that the Real Return Asset class returned -1.43% for the quarter, beating its benchmark by 27 basis points. He added that Emerging Market Debt returned 3.17% for the quarter, underperforming its benchmark by 45 basis points. Mr. Heiner stated that private equity returned 4.12% for the quarter, coming above its benchmark by 125 basis points. Finally, he stated that the total emerging market equity composite returned 6.68% for the second quarter 2017, outperforming its benchmark by 41 basis points.

## CONSENT ITEMS

### **9. Determination as to Whether Transfers May be Made from the Permanent School Fund to the Available School Fund**

(Board agenda page III-9)  
[Consent agenda item #(3)]

Carlos Veintemillas, deputy chief investment officer, and director of fixed income gave a presentation describing the two constitutional limits on distributions from the Permanent School Fund. The two limits require that an annual distribution cannot be greater than six percent of the value of the Fund assets and the total amount of distributions from the current and previous nine state fiscal years cannot exceed the total return on the Fund assets over the same time period. Mr. Veintemillas stated that both tests were satisfied, allowing for a distribution from the PSF to the Available School Fund for fiscal year 2018.

**MOTION AND VOTE:** *By unanimous consent, the committee recommended that the State Board of Education determine that a distribution of approximately \$1.236 billion for fiscal year 2018 is permitted under Texas Constitution, Article VII, Subsection 5(a)(2).*

### **10. Decision on Real Estate Investments**

(Board agenda page III-13)  
[Consent agenda item #(4)]

The PSF real estate consultant, Courtland Partners, was represented by Tom Hester, Senior Vice President, joined by PSF staff member, Nick Tramontana, Portfolio Manager. Mr. Hester provided an introduction for a real estate investment recommendation, Blackstone Real Estate Partners Asia II, L.P., a U.S. dollar denominated fund offered by Blackstone Real Estate. Mr. Hester 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. Hester also provided a report on the real estate co-investment program, including an update on the recent transaction activity. He reported that the transaction is in compliance with the standards set forth in the real estate investment policy.

**MOTION AND VOTE:** *By unanimous consent, the committee recommended to the State Board of Education approval to execute agreement(s) with BREP Asia II L.L.C., its general partner, necessary to make an investment commitment of up to \$75 million in Blackstone Real Estate Partners Asia II, L.P., subject to continued due diligence and negotiation of fund terms, and authorization for contract execution by the Commissioner of Education.*

### **11. Implementation of SB 1480 Related to the Bond Guarantee Program and Charter Schools**

(Board agenda page III-15)  
[Consent agenda item #(5)]

Holland Timmins, chief investment officer and executive administrator, presented the item. Mr. Timmins gave a presentation describing Senate Bill 1480, 85<sup>th</sup> Legislature, Regular Session, and its impact on the bond guarantee program. The bill increases charter guarantee capacity, moves management of the reserve fund to the SBOE, and increases payments to the reserve fund. The bill

requires the Board to establish for Fiscal Year 2018 the capacity of the bond guarantee program for charter district bonds.

**MOTION AND VOTE:** *For Fiscal Year 2018, the monthly estimate of the available capacity of the Permanent School Fund to guarantee bonds for charter districts (19 TAC 33.67(d)) will incorporate the change in the calculation of the bond guarantee program's charter capacity pursuant to Senate Bill 1480, 85<sup>th</sup> Legislature, Regular Session. As authorized by SB 1480, the State Board of Education establishes the BGP charter capacity increase for FY 2018 at the full twenty percent (20%) allowed under the law.*

## **DISCUSSION ITEM**

### **12. Discussion of 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, and §33.67, Bond Guarantee Program for Charter Schools**

(Board agenda page III-45)

Mr. Timmins presented the item. He stated that the agenda item was for discussion only and provided the committee an opportunity to discuss legislative changes that impacted the rule. Mr. Timmins anticipated that the item would be brought back at the next meeting for first reading and filing authorization.

## **CONSENT ITEM**

### **13. Presentation on the Commodities Asset Class for the Permanent School Fund**

(Board agenda page III-17)

[Consent agenda item #(6)]

Carlos Veintemillas, deputy chief investment officer and Katie Reissman, portfolio manager provided the presentation. The presentation covered the benefits of commodities, the mandate objectives and strategy and performance. The committee directed staff and NEPC to explore the possibility of managing a portion of the commodity strategy in-house.

## **DISCUSSION ITEMS**

### **14. Report of the Permanent School Fund Executive Administrator and Chief Investment Officer**

(Board agenda page III-69)

Mr. Timmins provided the committee an update on PSF litigation. He also provided the committee with information regarding the preliminary fund value.

### **15. Review of the Permanent School Fund Governance**

(Board agenda page III-71)

Mr. Bradley called on Chuck Campbell, partner with Jackson Walker and Board fiduciary counsel, to make a presentation on the operational structure of the Permanent School Fund related primarily to governance, fiduciary, and legal matters. Mr. Campbell gave an overview of the current governance structure, the non-profit corporation option available under the Texas Education Code,

and an additional alternative of a “government” corporation. The considerations of each structure were addressed and compared.

Mr. Bradley sought the committee’s consent to ask Mr. Campbell to further research the non-profit corporation structure and present a more detailed presentation on it at the Committee meeting in November. The consent was given.

The meeting of the Committee on School Finance/Permanent School Fund adjourned at 2:15 p.m.

**TEXAS PERMANENT SCHOOL FUND  
SUMMARY OF TRANSACTIONS FOR APPROVAL  
(Including External Manager's Trades)  
For May 1, 2017 through July31, 2017**

Purchases/Capital Calls:

Short Term Fixed Income	\$ -
Long Term Fixed Income	431,082,689
Public Market Equities	195,627,915
Alternative Investments	686,534,296
Foreign Exchange	-
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TOTAL	<u>\$ 1,313,244,900</u>

Sales/Distributions:

Short Term Fixed Income	\$ -
Long Term Fixed Income	196,132,315
Public Market Equities	569,158,929
Alternative Investments	513,834,645
Foreign Exchange	-
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TOTAL	<u>\$ 1,279,125,889</u>

General Land Office Contributions:

FY 2016 Cumulative July 2016	FY 2017 Cumulative July 2017
\$131,250,000	\$150,000,000

Based on the above information provided by staff including a report that deposits to the Permanent School Fund from the General Land Office were \$150,000,000 through July 2017 for fiscal year 2017 versus \$131,250,000 through July 2016 for fiscal year 2016, and the recommendation of the Executive Administrator and Chief Investment Officer and the Commissioner of Education; it is moved by unanimous consent that the Committee on School Finance/Permanent School Fund ratify for the months of May 2017, June 2017, and July 2017, Permanent School Fund portfolio purchases of \$1,313,244,900 and sales of \$1,279,125,889.