

**Report of the State Board of Education
Committee on School Finance/Permanent School Fund
April 15, 2021**

The State Board of Education Committee on School Finance/Permanent School Fund met at 10:16 a.m. on Thursday, April 15, 2021, in the State Board of Education Room, Room #1-104 of the William B. Travis Building, 1701 N. Congress Avenue, Austin, Texas. Attendance was noted as follows:

Present: Tom Maynard, chair; Lawrence A. Allen, Jr., vice chair; Keven Ellis; Patricia Hardy; Marisa Perez-Diaz

Public Testimony

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

ACTION ITEM

- 1. Proposed Amendment to 19 TAC Chapter 109, Budgeting, Accounting, and Auditing, Subchapter C, Adoptions By Reference, §109.41, Financial Accountability System Resource Guide (Second Reading and Final Adoption)**
(Board agenda page III-1)

David Marx, senior director, financial compliance, explained that the proposed amendment would adopt by reference the updated *Financial Accountability System Resource Guide* (FASRG). He also explained the contents of the FASRG and the public comments received.

MOTION AND VOTE: *It was moved by Dr. Ellis, seconded by Ms. Perez-Diaz, and carried unanimously to recommend that the State Board of Education approve for second reading and final adoption the proposed amendment to 19 TAC Chapter 109, Budgeting, Accounting, and Auditing, Subchapter C, Adoptions By Reference, §109.41, Financial Accountability System Resource Guide; and*

Make an affirmative finding that immediate adoption of the proposed amendment to 19 TAC Chapter 109, Budgeting, Accounting, and Auditing, Subchapter C, Adoptions By Reference, §109.41, Financial Accountability System Resource Guide, is necessary and shall have an effective date of 20 days after filing as adopted with the Texas Register.

DISCUSSION ITEM

2. **Discussion of Proposed Amendment to 19 TAC Chapter 109, Budgeting, Accounting, and Auditing, Subchapter B, Texas Education Agency Audit Functions, §109.25, State Compensatory Education Program Reporting and Auditing System**
(Board agenda page III-8)

Mr. Marx explained that the proposed amendment would update references to statutory citations that were renumbered by House Bill (HB) 3, 86th Texas Legislature, 2019.

ACTION ITEMS

3. **Adoption of Review of 19 TAC Chapter 109, Budgeting, Accounting, and Auditing, Subchapter A, Budgeting, Accounting, Financial Reporting, and Auditing for School Districts, Subchapter B, Texas Education Agency Audit Functions, Subchapter C, Adoptions by Reference, and Subchapter D, Uniform Bank Bid or Request for Proposal and Depository Contract (Adoption of Review)**
(Board agenda page III-11)

Mr. Marx explained that the rules being reviewed provide requirements for school districts relating to budgeting, accounting, financial reporting, and auditing; Texas Education Agency (TEA) financial review functions; adoption by reference of the *Financial Accountability System Resource Guide* (FASRG); and the bank bid, proposal, and depository contract and surety bond forms.

MOTION AND VOTE: *It was moved by Dr. Ellis, seconded by Ms. Perez-Diaz, and carried unanimously to recommend that the State Board of Education adopt the review of 19 TAC Chapter 109, Budgeting, Accounting, and Auditing, Subchapter A, Budgeting, Accounting, Financial Reporting, and Auditing for School Districts, Subchapter B, Texas Education Agency Audit Functions, Subchapter C, Adoptions by Reference, and Subchapter D, Uniform Bank Bid or Request for Proposal and Depository Contract, and that the item be placed on the consent agenda of the State Board of Education.*

4. **Proposed Repeal of 19 TAC Chapter 105, Foundation School Program, Subchapter A, Definitions, §105.1, Rules for the Definition of Tax Levy and Tax Collection (First Reading and Filing Authorization)**
(Board agenda page III-61)

Amy Copeland, director, state funding, explained that the proposed repeal would implement House Bill (HB) 3, 86th Texas Legislature, 2019, which removed the State Board of Education's (SBOE's) rulemaking authority related to the definitions of tax levy and tax collection for the Foundation School Program (FSP).

MOTION AND VOTE: *It was moved by Dr. Ellis and carried unanimously to recommend that the State Board of Education suspend the board operating procedures in accordance with §5.2(a) to allow consideration at first reading and filing authorization; and*

Approve for first reading and filing authorization the proposed repeal of 19 TAC Chapter 105, Foundation School Program, Subchapter A, Definitions, §105.1, Rules for the Definition of Tax Levy and Tax Collection; and that the item be placed on the consent agenda of the State Board of Education.

DISCUSSION ITEMS

5. Report by the State Auditor’s Office on the Audit of the Permanent School Fund’s Financial Statements and Certification of the Bond Guarantee Program for the Fiscal Year Ending August 31, 2020

(Board agenda page III-65)

Mr. Maynard introduced Michael Clayton, audit manager, and Bill Hunter, managing senior auditor from the State Auditor’s Office (SAO) for presentation of the annual audit of the Permanent School Fund for the year ending August 31, 2020, and for presentation of results of the Certification of the Permanent School Fund’s Bond Guarantee Program for fiscal year 2020.

Mr. Hunter stated that the SAO issued an unqualified opinion on the financial statements audited for the period. He stated that the SAO conducted a review of internal controls and identified no reportable weakness or other items at the Texas Education Agency.

Mr. Hunter then presented the results of the Certification of the Permanent School Fund’s Bond Guarantee Program for the fiscal period. He stated that the amount of bonds guaranteed during fiscal year 2020 was within all regulatory limits established by the Texas Education Code (§45.053(a) and (d), and §45.0531(a) and (b)), the Internal Revenue Service (Notice 2010-5 dated December 16, 2009), and the State Board of Education, and that the Fund had sufficient reserves to meet the State Board of Education’s reserve requirements for the same period.

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

(Board agenda page III-66)

Catherine Civileto, deputy executive administrator, provided a summary of the status of the Permanent School Fund portfolio. Reports presented to the committee were for the reporting period December 1, 2020, through February 28, 2021, unless otherwise noted. Ms. Civileto’s report included reporting on the current fair market value of the Fund; the asset allocation mix as of February 28, 2021; PSF transactions occurring in the reporting period; revenues and expenditures for the fiscal period beginning September 1 through February 28, 2021; the activity in the securities lending program for the fiscal period beginning September 1 through February 28, 2021; the status of transfers from the General Land Office (GLO) as of February 28, 2021, as per approved resolutions; 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, 2020 through December 31, 2020, and the period beginning January 1, 2021, through February 28, 2021; fixed income rating changes for the fiscal period September 1, 2020, through February 28, 2021; and short-term cash investments.

ACTION ITEMS

7. **Ratification of the Purchases and Sales of the Investment Portfolio of the Permanent School Fund for the Months of December 2020, January 2021, and February 2021**
(Board agenda page III-67)

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 that the State Board of Education ratify the purchases and sales for the months of December 2020 and January and February 2021, in the amounts of \$1,807,953,391 and \$1,851,830,304, respectively (Attachment A).*

8. **Report on the Permanent School Fund Liquid Account**
(Board agenda page III-68)

Ms. Civileto provided a summary of the status of the Permanent School Fund Liquid Account. Reports presented to the committee were for the reporting period December 1, 2020 through February 28, 2021. Ms. Civileto's report included reporting on the current fair market value of the Liquid Account; the asset allocation mix as of February 28, 2021; transfer activity between the GLO and the Liquid Account; cumulative Income and Realized Gains transferred to the SBOE from the Liquid Account as of February 28, 2021; transactions occurring in the reporting period; and ratification of the cumulative Purchases and Sales of the Liquid Account from December 1, 2020, through February 28, 2021.

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 that the State Board of Education ratify the purchases and sales of the Permanent School Fund Liquid Account for the period December 1, 2020, through February 1, 2021, in the amounts of \$684,875,077 and \$204,950,145 respectively (Attachment B).*

9. **Adoption of an Annual Report on the Status of the Bond Guarantee Program**
(Board agenda page III-69)

Holland Timmins, executive administrator and chief investment officer, presented the annual report of the Bond Guarantee Program as required by the Texas Education Code and requested that the committee adopt the report as presented.

MOTION AND VOTE: *By unanimous consent, the committee recommended that the State Board of Education adopt the annual report on the status of the Bond Guarantee Program as of August 31, 2020.*

DISCUSSION ITEMS

10. **Fourth Quarter 2020 Permanent School Fund Performance Report**
(Board agenda page III-70)

Mr. Mike Maher, vice president of BNY Mellon Global and Risk Solutions, presented the fourth quarter 2020 Permanent School Fund performance report. Mr. Maher began with an overview of the U.S. and foreign capital markets. Mr. Maher then reviewed the performance of the Fund for the fourth

quarter of 2020. He stated that the PSF returned 10.09% net of fees for the fourth quarter, outperforming the target benchmark by 54 basis point. Mr. Maher attributed most of the outperformance to Fixed Income, Private Equity, and Emerging Market Debt.

Mr. Maher reviewed the fourth quarter 2020 performance of the Permanent School Fund by asset class, stating that the total domestic large cap equity composite returned 12.18%, outperforming its benchmark for the quarter by 3 basis point. Mr. Maher added that Small/Midcap Equity portfolio returned 26.44% in the quarter, outperforming its benchmark by 8 basis points. He added that international equities returned 17.38% for the quarter, outperforming its benchmark by 9 basis points for the period.

The fixed income portfolio returned 0.49% for quarter, outperforming its benchmark by 56 basis points. Mr. Maher stated that the Absolute Return composite returned 6.24% for the quarter, underperforming its benchmark, the HFRI Fund of Funds Composite Index, by 185 basis points. Mr. Maher added that the Real Estate composite returned 2.49% for the quarter, outperforming its benchmark by 91 basis points. He further stated that the Real Return Asset class returned 5.78% for the quarter, underperforming its benchmark by 7 basis points. He added that Emerging Market Debt returned 11.83% for the quarter, outperforming its benchmark by 226 basis points. Mr. Maher stated that private equity returned 11.43% for the quarter, outperforming its benchmark by 338 basis points. Finally, he stated that the total emerging market equity composite returned 19.01% for the fourth quarter 2020, underperforming its benchmark by 69 basis points.

11. Review of the Core Fixed Income Asset Class for the Permanent School Fund
(Board agenda page III-71)

Carlo Veintemillas, deputy executive administrator and director of fixed income, gave an update on the fixed income team and structure and then introduced Gareth Williams, portfolio manager, and Kevin Godin, fixed income analyst. Mr. Williams and Mr. Godin provided an overview of the core fixed income strategy and process.

ACTION ITEMS

12. Approval of the Selection of a Firm(s) to Provide Investment Management for a Private Equity Emerging Manager Program and a Private Real Estate Emerging Manager Program for the Texas Permanent School Fund and the State Board of Education as outlined in Request for Proposal 701-21-001 and Authorization for Contract Execution by the Commissioner of Education
(Board agenda page III-72)

Mr. Timmins presented an update related to the request for proposal (RFP) for Investment Management Services for both a Private Equity Emerging Manager program and a Private Real Estate Emerging Manager program, to fill the new 1% allocation, with the primary investment objective of generating additional value for the Permanent School Fund.

The PSF general consultant, NEPC was represented by Keith Stronkowsky, senior consultant, joined by John Grubenman, director of private markets, and Kathryn Gernert, portfolio manager. They presented information about the search process.

The following three (3) firms gave presentations by their respective representatives:

- Hamilton Lane Advisors, LLC
- GCM Grosvenor
- Neuberger Berman Alternatives Advisers, LLC

MOTION AND VOTE: *It was moved by Mr. Allen, seconded by Dr. Ellis, and carried unanimously, to recommend that the State Board of Education approve execution of agreement(s) with Neuberger Berman Alternative Advisors, necessary to make an investment commitment of up to \$300 million for Investment Management Services for a Private Equity Emerging Manager program for the Texas Permanent School Fund and Authorization for Contract Execution by the Commissioner of Education; and,*

Approve execution of agreement(s) with GCM Grosvenor, necessary to make an investment commitment of up to \$150 million for Investment Management Services for a Private Real Estate Emerging Manager program for the Texas Permanent School Fund and Authorization for Contract Execution by the Commissioner of Education.

13. Review the Processes that Consider Board Member Nominees for State Board Positions
(Board agenda page III-73)

Mark Shewmaker, managing director of special projects and portfolio manager, provided the committee an overview on the process for selecting nominees to be sent to the Governor for membership on the School Land Board and the Teacher Retirement System board.

MOTION AND VOTE: *By unanimous consent, the committee recommended that the State Board of Education approve the procedure for selecting nominees to be sent to the Governor for membership on the School Land Board and the Teacher Retirement System Board as presented by staff.*

DISCUSSION ITEM

14. Report of the Permanent School Fund Executive Administrator and Chief Investment Officer
(Board agenda page III-74)

Mr. Timmins informed the committee that Moody’s Investors Service reaffirmed the rating of the Texas Permanent Bond Guarantee Program. He also provided an update on the PSF intern program.

The meeting of the Committee on School Finance/Permanent School Fund adjourned at 2:20 p.m.

**TEXAS PERMANENT SCHOOL FUND
SUMMARY OF TRANSACTIONS FOR APPROVAL
(Including External Manager's Trades)
For December 1, 2020 through February 28, 2021**

Purchases/Capital Calls:

Long Term Fixed Income	\$ 771,813,330
Public Market Equities	328,760,370
Alternative Investments	<u>707,379,691</u>
 TOTAL	 <u><u>\$ 1,807,953,391</u></u>

Sales/Distributions:

Long Term Fixed Income	\$ 251,975,711
Public Market Equities	666,840,117
Alternative Investments	<u>933,014,476</u>
 TOTAL	 <u><u>\$ 1,851,830,304</u></u>

General Land Office Contributions:

FY 2020 Cumulative February 2020	FY 2021 Cumulative February 2021
\$5,000,000	\$22,500,000

Based on the above information provided by staff including a report that deposits to the Permanent School Fund from the General Land Office were \$5,000,000 through February 2020 for fiscal year 2020 versus \$22,500,000 through February 2021 for fiscal year 2021, 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 December 2020, January 2021, and February 2021 Permanent School Fund portfolio purchases of \$1,807,953,391 and sales of \$1,851,830,304.

**TEXAS PERMANENT SCHOOL FUND
SUMMARY OF TRANSACTIONS FOR APPROVAL
FOR PSF LIQUID ACCOUNTS
For December 1, 2020 through February 28, 2021**

Purchases:

Fixed Income	\$ 162,688,482
Public Market Equities	<u>522,186,595</u>
TOTAL	<u><u>\$ 684,875,077</u></u>

Sales:

Fixed Income	\$ 164,785,928
Public Market Equities	<u>40,164,217</u>
TOTAL	<u><u>\$ 204,950,145</u></u>

Based on the above information provided by staff 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 period December 1, 2020 through February 28, 2021 Permanent School Fund Liquid Account purchases of \$684,875,077 and sales of \$204,950,145.