

**Report of the State Board of Education  
Committee on School Finance/Permanent School Fund  
September 13, 2018**

The State Board of Education Committee on School Finance/Permanent School Fund met at 9:07 a.m. on Thursday, September 13, 2018, in Room #1-104 of the William B. Travis Building, 1701 N. Congress Avenue, Austin, Texas. Attendance was noted as follows:

Present: David Bradley, chair; Tom Maynard, vice chair; Lawrence A. Allen, Jr.; Patricia Hardy; Ken Mercer

**Public Testimony**

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

**CONSENT ITEM**

**1. Per Capita Apportionment Rate for the 2018–2019 School Year**

(Board agenda page III-1)

[Consent agenda item #(3)]

Al McKenzie, director, school finance, presented this item that proposes a preliminary per capita apportionment rate of \$459.764. Mr. McKenzie answered questions from the committee regarding the per capita apportionment rate.

**MOTION AND VOTE:** *It was moved by Mr. Maynard, seconded by Mr. Bradley, and carried unanimously to recommend that the State Board of Education adopt the recommended per capita apportionment rate of \$459.764 for the 2018-2019 school year.*

**DISCUSSION ITEM**

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

(Board agenda page III-11)

Catherine Civiletto, 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 May through July 2018 unless otherwise noted. Ms. Civiletto's report addressed the current fair market value of the Fund, the asset allocation mix as of July 31, 2018, PSF transactions occurring in the reporting period, revenues and expenditures for the fiscal period beginning September 1 through July 31, 2018, the activity in the securities lending program for the fiscal period beginning September 1 through July 31, 2018, 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, 2018 through July 31, 2018, fixed income rating changes for the fiscal period beginning September 1, 2017 through July 31, 2018, and short-term cash investments.

## **CONSENT ITEM**

- 3. Ratification of the Purchases and Sales of the Investment Portfolio of the Permanent School Fund for the Months of May, June, and July 2018**  
(Board agenda page III-3)  
[Consent agenda item #(4)]

**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 May, June, and July 2018, in the amount of \$1,341,584,400 and \$1,424,194,637 respectively (Attachment B).*

## **DISCUSSION ITEM**

- 4. Second Quarter 2018 Permanent School Fund Performance Report**  
(Board agenda page III-13)

Tom Heiner BNY Mellon Global and Risk Solutions, presented the second quarter of 2018 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 2018. He stated that the PSF returned -0.26% for the fourth quarter underperforming the target benchmark by 33 basis points.

Mr. Heiner reviewed second quarter 2018 performance of the Permanent School Fund by asset class, stating that the total domestic large cap equity composite exceeded its benchmark for the quarter by four basis points. Mr. Heiner added that the Small/Midcap Equity portfolio outperformed its benchmark by four basis points. He added that international equities returned -3.40% for the quarter, outperforming its benchmark by seven basis points during the period. The fixed income portfolio returned -0.17% for quarter, falling short of its benchmark by one basis point. Mr. Heiner stated that the Absolute Return composite returned 1.38% for the quarter, beating its benchmark, the HFRI Fund of Funds Composite Index, by 78 basis point. Mr. Heiner added that the Real Estate composite returned 1.99% for the quarter, underperforming its benchmark by 21 basis points. Mr. Heiner added that the Total Risk Parity Strategies returned 0.35% in the second quarter of 2018, underperforming its benchmark by 164 basis points. He further stated that the Real Return Asset class returned 0.48% for the quarter, underperforming its benchmark by 14 basis points. He added that Emerging Market Debt returned -11.87% for the quarter, underperforming its benchmark by 145 basis points. Mr. Heiner stated that private equity returned 0.64% for the quarter, coming short of its benchmark by 224 basis points. Finally, he stated that the total emerging market equity composite returned -8.19% for the second quarter 2018, underperforming its benchmark by 23 basis points.

## **CONSENT ITEMS**

- 5. Determination as to Whether Transfers May be Made from the Permanent School Fund to the Available School Fund**  
(Board agenda page III-5)  
[Consent agenda item #(5)]

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 2019.

Keith Stronkowsky, Senior Consultant, NEPC, LLC stated that NEPC was in agreement with PSF staff recommendations.

**MOTION AND VOTE:** *By unanimous consent, the committee recommended that the State Board of Education approve a distribution to the Available School Fund of approximately \$1.236 million for fiscal year 2019.*

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

(Board agenda page III-9)

[Consent agenda item #(6)]

The PSF real estate consultant, Courtland Partners, was represented by Steve Novick, Partner, and Kieran Farrelly, Managing Director, joined by John Grubenman, Director of Private Markets for PSF, Nick Tramontana and Kathryn Gernert, Portfolio Managers for PSF. Mr. Novick and Mr. Grubenman provided a brief introduction of four real estate investment recommendations.

Mr. Novick introduced a real estate investment recommendation in Madison Realty Capital Debt Fund IV, L.P. offered by Madison Realty Capital Debt Fund IV GP, L.L.C. Mr. Novick, Mr. Grubenman, and Ms. Gernert 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.

**MOTION AND VOTE:** *By unanimous consent, the committee recommended that the State Board of Education approve execution of agreement(s) with Madison Realty Capital Debt Fund IV GP, L.L.C., necessary to make an investment commitment of up to \$100 million in Madison Realty Capital Debt Fund IV, L.P., subject to continued due diligence and negotiation of fund terms, and authorization for contract execution by the Commissioner of Education.*

Mr. Farrelly introduced a real estate investment recommendation in European Property Investors Special Opportunities 5 SCSp offered by EPISO 5 (GP) S.A.R.L. Mr. Farrelly, Mr. Grubenman, and Mr. Tramontana 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.

**MOTION AND VOTE:** *By unanimous consent, the committee recommended to the State Board of Education approve execution of agreement(s) with EPISO 5 (GP) S.A.R.L., necessary to make an investment commitment of up to €75 million in European Property Investors Special Opportunities 5 SCSp, subject to continued due diligence and negotiation of fund terms, and authorization for contract execution by the Commissioner of Education.*

Mr. Novick introduced a real estate investment recommendation, in TPG Real Estate Partners III, L.P. offered by TPG Real Estate GenPar III, L.P. Mr. Novick, Mr. Grubenman, and Mr. Tramontana 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.

**MOTION AND VOTE:** *By unanimous consent, the committee recommended that the State Board of Education approve execution of agreement(s) with TPG Real Estate GenPar III, L.P., necessary to make an investment commitment of up to \$75 million in TPG Real Estate Partners III, L.P., subject to continued due diligence and negotiation of fund terms, and authorization for contract execution by the Commissioner of Education.*

Mr. Novick introduced a real estate investment recommendation, in PAG Enhanced Credit Fund II, L.P offered by PAG Enhanced Credit GP II Limited. Mr. Novick, Mr. Grubeman, and Mr. Tramontana 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.

**MOTION AND VOTE:** *By unanimous consent, the committee recommended that the State Board of Education approve execution of agreement(s) with PAG Enhanced Credit GP II Limited, necessary to make an investment commitment of up to \$100 million in PAG Enhanced Credit Fund II, L.P., subject to continued due diligence and negotiation of fund terms, and authorization for contract execution by the Commissioner of Education.*

## **DISCUSSION ITEMS**

**7. Activities Related to a Student Art Competition to Develop a Permanent School Fund Logo**  
(Board agenda page III-15)

Mr. Maynard gave an update on the progress of the contest preparations. He continues to research the history of the fund along with staff to post more information on the portal for the benefit of the students who may submit. Mr. Maynard reminded fellow committee members about the need for SBOE to donate to the cause and he asked staff to send everyone a reminder memo. The contest portal will open on October 1, 2018 and the judging committee will do its work in November 2018.

**8. Report of the Permanent School Fund Executive Administrator and Chief Investment Officer**  
(Board agenda page III-17)

Holland Timmins, chief investment officer and executive administrator, provided the committee an update on the charter district reserve fund. He noted the information was not included in the PSF investment portfolio report because the funds are not part of the PSF. Mr. Timmins informed the committee that the SEC issued amended rule changes for the Bond Guarantee program disclosure (SEC Rule 15c2-12) that will be incorporated into the Investment Procedures Manual and presented at a future board meeting. He reported that the PSF received the Government Finance Officers Association (GFOA) Certificate of Achievement for Excellence in Financial Reporting for FY17.

The meeting of the Committee on School Finance/Permanent School Fund adjourned at 11:12 a.m.

**TEXAS PERMANENT SCHOOL FUND  
SUMMARY OF TRANSACTIONS FOR APPROVAL  
(Including External Manager's Trades)  
For May 1, 2018 through July 31, 2018**

Purchases/Capital Calls:

Long Term Fixed Income	\$ 379,116,463
Public Market Equities	298,219,823
Alternative Investments	<u>664,248,114</u>
TOTAL	<u>\$ 1,341,584,400</u>

Sales/Distributions:

Long Term Fixed Income	\$ 189,575,042
Public Market Equities	851,179,743
Alternative Investments	<u>383,439,852</u>
TOTAL	<u>\$ 1,424,194,637</u>

General Land Office Contributions:

FY 2017	FY 2018
Cumulative	Cumulative
April 2017	April 2018
\$150,000,000	\$176,250,000

Based on the above information provided by staff including a report that deposits to the Permanent School Fund from the General Land Office were \$176,250,000 through July 2018 for fiscal year 2018 versus \$150,000,000 through July 2017 for fiscal year 2017, 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 2018 and July 2018 Permanent School Fund portfolio purchases of \$1,341,584,400 and sales of \$1,424,194,637.

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