

**Report of the State Board of Education  
Committee on School Finance/Permanent School Fund  
November 17, 2016**

The State Board of Education Committee on School Finance/Permanent School Fund met at 9:02 a.m. on Thursday, November 17, 2016, 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 items #10 and #11. Information regarding the individuals who presented public testimony is included in the discussion of those items.

**CONSENT ITEM**

**1. Approval of Costs to Administer the 2016-2017 State-Developed Assessments to Private School Students**

(Board agenda page III-1)  
[Consent agenda item #(2)]

Tony Wilson, assessment policy analyst with student assessment, presented this item. Mr. Wilson explained that this item applies to private schools using state-developed assessments to evaluate their students. Mr. Wilson explained that the cost per assessment was determined by dividing the overall cost by the number of students that participated. Mr. Wilson answered questions from Mr. Ratliff, Mr. Bradley, and Ms. Hardy regarding administering state-developed assessments to private school students.

**MOTION AND VOTE:** *It was moved by Mr. Ratliff, seconded by Mr. Mercer, and carried unanimously to recommend that the State Board of Education approve the recommended per-student costs for administering the state assessments to private school students in 2016-2017.*

## DISCUSSION ITEMS

2. **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, §109.51, Uniform Depository Bank Bid or Proposal Form**

(Board agenda page III-45)

David Marx, director of financial compliance, presented this item. Mr. Marx explained that the proposed amendment would update the bank bid and proposal forms. This amendment would facilitate the acquisition of a depository contract that complies with current banking standards. Mr. Marx responded to questions from Ms. Hardy and Mr. Mercer regarding the amendment.

3. **Review of 19 TAC Chapter 30, Administration, Subchapter B, State Board of Education: Purchasing and Contracts**

(Board agenda page III-85)

Norma Barrera, director of purchasing and contracts, presented this item. Ms. Barrera explained that this item relates to the protest procedure for purchasing issues and dispute resolution. Ms. Barrera answered questions from Mr. Ratliff regarding the item.

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

(Board agenda page III-93)

Catherine Civiletto, 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 August 1, 2016 through September 30, 2016 unless otherwise noted. Ms. Civiletto's report included reporting on the current fair market value of the Fund, the asset allocation mix as of September 30, 2016, PSF transactions occurring in the reporting period, revenues and expenditures for the fiscal period September through August 31, 2016 and the fiscal period beginning September 1 through September 30, 2016, the historical activity on the securities lending program through the fiscal period ended August 31, 2016, as well as the month of September 2016, 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, 2016 through September 30, 2016, 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 August and September 2016**

(Board agenda page III-7)

[Consent agenda item #(3)]

**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 August and September 2016, in the amount of \$841,579,353 and \$726,730,498 respectively (Attachment A).*

## **DISCUSSION ITEM**

### **6. Third Quarter 2016 Permanent School Fund Performance Report** (Board agenda page III-95)

Tom Heiner of BNY Mellon Global and Risk Solutions, presented the third quarter of 2016 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 third quarter of 2016. He stated that the PSF returned 3.52% for the third quarter outperforming the target benchmark by 39 basis points. The Fund ranked in the 57th percentile or top of the third quartile of the Mellon Universe of Public Funds greater than \$1.0 billion for the 3-month period ending September 30, 2016.

Mr. Heiner reviewed third quarter 2016 performance of the Permanent School Fund by asset class, stating that the total domestic large cap equity composite outperformed its benchmark by five basis points for the quarter. Mr. Heiner added that Small/Midcap Equity portfolio outperformed its benchmark by three basis points. He added that international equities returned 6.81% for the quarter, having underperformed its benchmark by 10 basis points during the period. The fixed income portfolio returned 0.95% for the quarter, exceeding its benchmark by 49 basis points. Mr. Heiner stated that the Absolute Return composite returned 2.58% for the quarter, outperforming its benchmark, the HFRI Fund of Funds Composite Index, by 16 basis points. Mr. Heiner added that the Real Estate composite returned 2.22% for the quarter, outperforming its benchmark by 78 basis points. Mr. Heiner added that Total Risk Parity Strategies returned 2.77% in the third quarter of 2016, outperforming its benchmark by 28 basis points. He further stated that the Real Return Asset class returned -0.88% for the quarter, outperforming its benchmark by 54 basis points. He added that Emerging Market Debt returned 2.38% for the quarter, falling short of its benchmark by 30 basis points. Mr. Heiner stated that private equity returned 5.13% for the quarter, coming above its benchmark by 300 basis points. Finally, he stated that the total emerging market equity composite returned 9.32% for the third quarter 2016, outperforming its benchmark by 29 basis points.

## **CONSENT ITEMS**

### **7. Decision on Real Estate Investments** (Board agenda page III-9) [Consent agenda item #(4)]

The PSF real estate consultant, Courtland Partners, was represented by Steve Novick, principal and chief operating officer, and Tom Hester, senior vice president. Holland Timmins, chief investment officer and executive administrator for PSF informed the committee that staff had one item to present.

Mr. Novick provided an introduction to a real estate investment recommendation, DRA Growth and Income Fund IX, L.L.C. offered by Manageco, IX, L.L.C., as General Partner. 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. Novick 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 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 Manageco, IX, L.L.C., as General Partner., necessary to make an investment commitment of up to \$75 million in DRA Growth and Income Fund IX, L.L.C., subject to continued due diligence and negotiation of fund terms, and authorization for contract execution by the Commissioner of Education.*

Mr. Novick also provided the committee an update on co-investment with an existing manager.

**8. Overview of the Permanent School Fund Real Estate Policy**

(Board agenda page III-11)

[Consent agenda item #(5)]

The PSF real estate consultant, Courtland Partners, was represented by Mr. Novick and Tom Hester and joined by Mr. Timmins.

Mr. Timmins discussed select provisions in the *Real Estate Investment Policy Statement* regarding co-investments and secondaries. Mr. Timmins described co-investments and secondaries and explained the benefits that these types of investments have provided the PSF Real Estate and Private Equity portfolios. Mr. Novick recommended making changes to the *Real Estate Investment Policy Statement* to broaden the opportunity set of real estate investment managers with whom the PSF may invest in co-investment and secondaries to make prompt investments when opportunities arise. Mr. Rhett Humphreys, Partner at PSF general consultant, NEPC, concurred with the recommendation.

**MOTION AND VOTE:** *It was moved by Mr. Ratliff, seconded by Mr. Allen, and carried by unanimous consent to adopt the changes to the Real Estate Policy Statement, as discussed.*

**DISCUSSION ITEM**

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

(Board agenda page III-97)

Mr. Timmins provided the committee on an update on the QMA manager regarding their chairman being replaced. He noted that this change would have minimum impact.

**ACTION ITEMS**

**10. 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-13)

[Official agenda item #12]

The following individuals provided public testimony:

NAME: Colleen Dippel

AFFILIATION: Families Empowered

NAME: Karalei Nunn  
AFFILIATION: Meridian World School

NAME: Barbara ten Brink  
AFFILIATION: None

NAME: John Murphy  
AFFILIATION: KIPP Houston Public Schools

Leo Lopez, chief school finance officer, presented this item. Mr. Lopez explained that the proposed amendment would increase the multiplier used in calculating the capacity of the Permanent School Fund (PSF) from 3.25 to 3.5 times the cost value of the PSF. Mr. Lopez answered questions from Mr. Bradley regarding the increased capacity.

**MOTION AND VOTE:** *It was moved by Mr. Ratliff, seconded by Mr. Bradley, 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 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, as amended, to read as follows:*

- (e) *Determination of PSF capacity to guarantee bonds.*
- (1) *Each month the commissioner will estimate the available capacity of the PSF. If necessary, the commissioner will confirm that the PSF has sufficient capacity to guarantee the bonds before the issuance of the final approval for the guarantee in accordance with subsection (g)(3) of this section. The calculation of capacity will be based on a multiplier of three and one-half [one-fourth] times the cost value of the PSF **effective March 1, 2017, and a multiplier of three and three-fourths times the cost value of the PSF effective September 1, 2017.** The commissioner may reduce the multiplier to maintain the AAA credit rating of the PSF. Changes to the multiplier made by the commissioner are to be ratified or rejected by the State Board of Education (SBOE) at the next meeting for which the item can be posted.*

- 11. 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-27)  
[Official agenda item #13]

The following individuals provided public testimony:

NAME: Thomas A. Sage  
AFFILIATION: Harmony Public Schools, KIPP Inc., IDEA Public Schools, Responsive Education Solutions

NAME: David Dunn  
AFFILIATION: Texas Charter Schools Association

NAME: Stacy Lawrence  
AFFILIATION: Uplift Education

Mr. Lopez presented this item. Mr. Lopez explained that the amendments would add language that would require charter schools to attain a certain level of academic proficiency before having access to the PSF Bond Guarantee Program (BGP). He also explained that the amendment would create a ranking system to prioritize BGP applications when capacity is over prescribed. Mr. Lopez provided a handout (Attachment B) detailing the impact of the amendments on current charter schools.

Shannon Housson, director of performance reporting, explained academic performance indicators and ratings that would impact charter schools' access to the PSF BGP.

Mr. Ratliff voiced concern over established charter operators having more access to the PSF BGP funds than less established charter operators.

Mr. Mercer questioned whether the already high standards needed to be raised even higher.

Mr. Bradley and Mr. Ratliff suggested that the amendments need more input from charter holders and may not be ready for a vote at this time. Ms. Hardy recommended that the commissioner hold stakeholder meetings and update the amendments according to those meetings.

The committee took no action.

The meeting of the Committee on School Finance/Permanent School Fund adjourned at 1:10 p.m.