

### **C.1.7 (Policy) Investments**

Responsible Department: Vice Chancellor for Finance and Administration

Board Adoption: 8-18-09

Last Board Action: 9-15-09 Update 09-04

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#### **General**

The Board of Trustees (“Board”) may purchase, sell, and invest funds under its control in investments authorized in the Public Funds Investment Act Chapter 2256, Texas Government Code (“PFIA”), in compliance with Board-adopted investment policies, and according to the standard of care prescribed in this written policy. *[Section 2256.005 (a)]* In the event of any discrepancy between this policy and the PFIA, the PFIA will prevail. Funds that are not considered “public” such as endowments and funds acting as endowments, which are not covered by the PFIA, will be managed in compliance with the Uniform Management of Institutional Funds Act (UMIFA) *[Texas Property Code Section 163.001]* and as described in the sections below, specifically applicable to endowment funds.

#### **Scope**

The provisions of this policy apply to the investment of its funds and all funds under the control of the Board:

- Operating Funds
- Debt Service Funds
- Debt Service Reserve Fund
- Construction Funds and Unexpended Plant Funds
- Endowment Funds and Funds Acting as Endowments (as described below)

#### **Objectives**

This investment policy emphasizes the safety of principal and liquidity, *[Texas Government Code Section 2256.005(2)]* and addresses investment diversification, yield, maturity and the quality and capability of investment management. The Board intends that investments will be purchased to hold until maturity; no investments will be made for the specific purpose of speculation of changes in market interest rates.

The investment objectives of the College District are in order of priority:

1. Assure the safety of the College District’s funds.
2. Maintain sufficient liquidity to provide adequate and timely operating funds.
3. Ensure the investment is marketable if the need arises to liquidate the investment.
4. Minimize risk of loss resulting from concentration of assets by diversifying investments as to maturity, instruments, and financial institutions where permitted under state law and provide for investments in authorized pooled and mutual funds.

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5. Attain a market yield consistent with safety and liquidity considerations.

#### **Delegation of Authority**

The Board retains ultimate responsibility as fiduciaries of the assets of the College District. The Associate Vice Chancellor of Finance and Fiscal Services is designated as the investment officer of the College District by Board authority delegated through the Chancellor. The investment officer shall be responsible for the investment of funds consistent with the investment policy adopted by the Board. The Associate Vice Chancellor of Finance and Fiscal Services may delegate management responsibility for daily investment transactions to the Comptroller (General Accounting) or Assistant District Treasurer. *[Texas Government Code Section 2256.005(f)]*

#### **External Management**

The Board may contract with an investment management or advisory firm registered under the Investment Advisors Act of 1940 (15U.S.C. Section 80-b1 et seq.) or with the State Securities Board to provide for the investment and management of its public funds under its control. The contracted period will be for a maximum of two years, and a renewal or extension of the contract must be made by the Board by resolution.

The Board will contract with a professional investment management firm or firms for investing endowment and similar funds, and the investment authority for those funds will be delegated to those firms subject to the applicable guidelines in this policy. The investment management firm must meet the following criteria:

- A minimum of \$500 million under management.
- A minimum of five years of verifiable results under AIMR standards.
- Outperform a suitable benchmark index, net of fees, at least 50% of the time during the period under review.
- Demonstrated stability of both personnel and accounts.

Additionally, the firm must disclose any significant litigation relating to the firm's integrity or abilities.

Subject to the provisions of the professional services contract, asset managers or advisory firms can be terminated by the Board at any time.

#### **Standards of Care**

All investments will be made with judgment and care, under prevailing circumstances, that a person of prudence, discretion, and intelligence would exercise in the management of his/her own affairs, not for speculation. *[Texas Government Code Section 2256.006(a)]*

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In determining whether an investment officer has exercised prudence with respect to an investment decision, the determination will be made taking into consideration: (1) the investment of all funds over which the officer had responsibility, rather than a consideration as to the prudence of a single investment; and (2) whether the investment decision was consistent with this investment policy. *[Texas Government Code Section 2256.006(b)]*

A College District investment officer who has a personal business relationship with a business organization offering to engage in an investment transaction with the College District shall file a statement disclosing that personal business interest. An investment officer who is related as determined by Texas Government Code Chapter 573, to an individual seeking to sell an investment to the College District will file a statement disclosing that relationship with the Board and with the Texas Ethics Commission.

#### **Training**

Board members and investment officers will attend at least one training session relating to the person's responsibilities conducted by the Texas Higher Education Coordinating Board within six months after taking office or assuming duties. Training shall include education in investment controls, security risks, strategy risks, market risks, diversification of investment portfolio and compliance with the Public Funds Investment Act. The Associate Vice Chancellor of Finance and Fiscal Services, the Comptroller (General Accounting), and the Assistant District Treasurer will attend a training session at least once every two years from a recognized and independent source. *[Texas Government Code Section 2256.007]*

#### **Internal Controls**

Internal controls will be established by the investment officer to prevent the loss of public funds through collusion. There will be a division of responsibilities between the Associate Vice Chancellor of Finance and Fiscal Services, Comptroller (General Accounting) and the Assistant Treasurer for internal control purposes, such that the purchases and sales made by one of these investment officers will be confirmed in writing by a different investment officer.

The investment officer will establish a process for a compliance audit at least once every two years by the College District's internal auditor or by a private auditor, the results of which are reported to the state auditor *[Texas Government Code Section 2256.005 (n)]*

#### **Investment Strategies**

The Board will adopt a separate written investment strategy for each type of account under its control, describing the investment objectives of each. *[Texas Government Code Section 2256.005(d)]*

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#### **Operating Funds**

The objective of these funds is to maintain adequate liquidity to meet daily operating cash needs. All security types listed in the “*Authorized Investments-Operating Funds*” section of this policy are considered suitable investments for the investment of Operating funds. Safety of principal and availability of adequate liquidity take priority over yield. The College District will diversify assets by security type, issuer and maturity date through separately purchased investments, through investments in approved pools or a combination of both in order to minimize overall risk. The investment strategy for the District’s Operating funds shall be accomplished by purchasing high quality, short- to medium-term securities. The dollar-weighted average maturity for operating funds shall be two years or less. Callable securities may be purchased in this fund group when there is a yield advantage over noncallable treasury securities of comparable duration based on both the call date and the stated final maturity date. Investment in public funds investment pools which function as a money market mutual fund is assumed to have maturity of one day for calculation purposes. For the portion of current fund investments representing the fund balance, the stated final maturity for an individual security can be up to five years from the date of purchase, while for the remaining portion, the stated final maturity for an individual security may not exceed two years from the date of purchase.

#### **Debt Service Funds**

Investments in debt service funds are governed by the bond covenants, and investment strategies for debt service funds shall assure investment liquidity adequate to cover the debt service obligation on the required payment date. Securities are purchased to meet specific bond payment dates. All security types listed in the “*Authorized Investments-Operating Funds*” and “*Authorized Investments-Debt Service Funds*” sections of this policy are considered suitable investments for the investment of Debt Service funds. Safety of principal shall take priority over yield. Adequate liquidity is required only to fund each debt service payment. The College District will seek diversification by security type, and issuer in order to minimize overall risk. Securities purchased shall not have a stated final maturity date which exceeds the debt service payment date.

#### **Debt Service Reserve Funds**

Investment of debt reserve funds is governed by the bond covenants. Generally, all security types listed in the “*Authorized Investments-Operating Funds*” and “*Authorized Investments-Debt Service Funds*” sections of this policy are considered suitable investments for the investment of Debt Service Reserve funds. Safety of principal shall take priority over yield. There is no need to maintain cash liquidity in a Reserve fund. The College shall seek diversification by security type and issuer name in order to minimize overall risk.

Investment strategies for debt service reserve funds shall generate a dependable revenue stream to the appropriate debt service fund from securities with a low degree of volatility. Except as may be required by the bond ordinance specific to an individual issue,

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securities should be of high quality, with short- to intermediate-term maturities. Stated final maturity of any individual security in the debt service reserve fund shall not exceed the final installment payment date of the debt issue.

#### **Construction Funds and Unexpended Plant Funds**

Investment strategies for construction funds and unexpended plant funds assure that anticipated cash flows are matched with adequate investment liquidity. All security types listed in the “*Authorized Investments-Operating Funds*” and “*Authorized Investments-Debt Service Funds*” sections of this policy are considered suitable investments for the investment of Construction Funds and Unexpended Plant Funds, but if the funds are proceeds from bond issuances, the covenants from the issue govern the investment activity. Safety of principal shall take priority over yield. Care shall be taken to provide adequate liquidity to fund forecasted expenditures. The College District will seek diversification by security type and issuer when purchasing individual securities, but may invest all of the proceeds of a single bond issue into a single investment if that investment type allows for cash withdrawals on demand. These portfolios should include at least ten percent in highly liquid securities or investment in public funds investment pools which function as a money market mutual fund to allow for flexibility to meet unanticipated project outlays. The stated final maturity dates of securities held should not exceed the estimated project completion date.

#### **Endowment Funds and Funds Acting as Endowments**

The College District created an endowment fund to provide funds for student scholarships and other College District expenses. In addition, there are funds which are not true endowments but are considered “acting as endowments” which, collectively with true endowments, are referred to as endowment funds or as endowments. Endowment funds are not covered by the PFIA, and will be managed in compliance with the UMIFA [*Texas Property Code, Section 163.001*] and as described below. The UMIFA describes the concept of “historic dollar value” and allows for endowment spending based on historic dollar value and the total return of the endowment.

Annual transfers from the endowment to scholarship and other College District accounts shall be recommended by the administration to the Board through the normal budget process.

Investment authority for the endowment funds and other similar funds functioning as endowments is generally described in the Texas Education Code [*Section 130.007*]. The investment performance goals on endowment and similar funds are: (1) to achieve a total rate of return at least equal to the spending rate, plus long-term inflation, and the costs of managing the investment fund, and (2) the income stream from investments to increase in order to preserve the purchasing power of the endowment income.

The Board will engage professional asset managers to manage its endowment assets. Investment managers have discretion to manage the assets in each portfolio to best achieve the investment objectives and goals set forth in this policy and the investment manager agreement and any manager-specific guidelines the administration may devise.

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Each manager will agree to exercise the judgment and care under the circumstances then prevailing that a person of ordinary prudence, discretion, and intelligence exercises in the management of the person's own affairs.

An investment consultant will be retained by the College District to perform the following services for the endowment:

- recommend new investment policies or changes to the investment policy and operating procedures;
- recommend appropriate benchmarks for each manager, asset class and the composite portfolio.
- recommend strategic and tactical asset allocation;
- deliver quarterly reports to the Associate Vice Chancellor of Finance and Fiscal Services to evaluate manager and portfolio performance. The report shall include performance (return and risk) comparisons to appropriate market indices, the Endowment's Custom Benchmark, the Consumer Price Index and appropriate manager universes;
- deliver an annual report to the Board;
- evaluate incumbent and prospective investment managers;
- monitor the asset allocation in compliance with the targets set in the investment policy;
- recommend the engagement of new managers and the termination of managers, as required, and
- provide endowment-related information, special studies and continuing education to the administration and the Board.

The Associate Vice Chancellor of Finance and Fiscal Services, assisted by the investment consultant, is responsible for tactical asset allocation and monitoring performance of each investment manager and the composite portfolio. The Associate Vice Chancellor of Finance and Fiscal Services may delegate administrative responsibility for the endowment to the Comptroller (General Accounting) or Assistant District Treasurer.

For purposes of measuring portfolio and manager progress, a time horizon of no less than five years is considered. Decisions based on shorter or longer periods are permitted at the discretion of the Board.

The total return of the endowment shall be evaluated against a custom benchmark which reflects the approximate asset allocation of the endowment. Each asset manager will be evaluated by the consultant against appropriate benchmarks and peer comparisons.

Retention and termination of investment managers and advisors are subject to the College District's policies and procedures governing professional service contracts. Selection will be based on a reasoned analysis of the managers' resources, personnel, process and past performance.

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#### **Authorized Investments-Operating Funds**

The Board may purchase, sell, and invest its funds and funds under its control in investments described below, in compliance with its adopted investment policies and according to the standard of care set out in this policy.

The following securities are authorized investments under this policy:

- Obligations of the United States, including letters of credit, or its agencies and instrumentalities;
- Direct obligations of the State of Texas or its agencies and instrumentalities;
- Other obligations, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, the State of Texas or the United States or their respective agencies and instrumentalities;
- Obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent;
- Certificates of Deposit and FDIC-insured Share Certificates issued by a depository institution that has its main office or a branch office in Texas. may be purchased without limit from a domestic bank if the amount is insured by the FDIC or is fully collateralized by the authorized investments in this section with a market value of at least 100% of the amount;
- Collateralized Repurchase Agreements must have a defined termination date and be secured by obligations described by Section 2256.009(a)(1) of the Texas Government Code and requires the securities being purchased to be pledged to the College District, held in the College District's name and deposited at the time the investment is made; and, is placed through a primary government securities dealer, as defined by the Federal Reserve or a financial institution doing business in the State of Texas;
- Bankers' Acceptances; 270 day or less stated maturity from date of issuance and accepted by a bank rated at least A-1 and P-1 or equivalent by a Nationally Recognized Statistical Rating Organization ("NRSRO");
- Commercial Paper. Paper must have a stated maturity of 270 days or less and be rated at least A-1 and P-1 or rated at least A-1 or P-1 or equivalent by a single NRSRO and fully secured by an irrevocable letter of credit issued by a domestic bank;
- No-Load Money Market Mutual Fund. Fund must be regulated by the SEC; have a dollar-weighted average stated maturity of 90 days or less; and include in its investment objectives the maintenance of a stable net asset value of \$1 for each share. Investment amounts are subject to limitations in the Code;

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- No-Load Mutual Fund. Fund must be registered with the SEC; have an average weighted maturity of less than two years; be invested exclusively in obligations approved by this policy; be continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than AAA or its equivalent; and conform to the requirements set forth in Section 2256.016 of the Texas Government Code relating to the eligibility of investment pools to receive and invest funds of investing entities.
- Public Fund Investment Pools. Public funds investment pools must be specifically authorized by the Board through resolution, and are subject to the limitations of PFIA Section 2256.016.

#### **Authorized Investments - Debt Service/Reserve/Construction Funds**

In addition to the authorized investments above, with the exception of No-Load Mutual Funds, bonds proceeds may be invested in the following:

- Guaranteed Investment Contracts (“GICs”) having a defined termination date to no longer than five years from the date of bond issuance, secured by U.S. Government direct or agency obligations.
- Flexible Repurchase Agreement (“Flex Repo”) with a defined termination date, collateralized at 102% with authorized securities.

#### **Authorized Investments-Endowment and Similar Funds**

The Board sets the following strategic allocation for the endowment:

Equities	50%–80%
Bonds, Cash/Cash Equivalents	20%–50%

The market value of investments for the total endowment shall remain within the ranges above except for minor deviations no greater than 5% due to fluctuations in market value or current spending. Monitoring the allocation is the responsibility of the investment consultant. In the event of a deviation, the investment officer shall communicate with the consultant to effect an appropriate reduction. Significant deviations from the approved ranges will be reported to the Board at its next regular meeting.

The endowment portfolio shall be well diversified as to asset class and the number of issues within each class with the view of reducing portfolio volatility. Care shall be taken to select asset classes which have a history of being uncorrelated. No more than five percent of the total endowment and similar funds (cost basis) may be invested in the securities of any one corporation. No more than one percent of the outstanding stocks of a single corporation may be included in the College District portfolio. No more than 20 percent of the total endowment and similar funds (cost basis) may be invested in any one industry. In addition to the authorized investments outlined in the previous sections, the following additional types of securities are authorized for the investment of endowment and similar funds under the control of the Board:

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- Preferred and common stock of corporations incorporated within the United States. Stocks must be listed on an exchange registered with the Securities and Exchange Commission or on the National Association of Securities Dealers Automated Quotes (NASDAQ). Convertible Notes and Bonds;
- Convertible Preferred Stocks;
- American Depository Receipts (ADR's) of Non-U.S. Companies;
- Bonds, debentures or obligations issued by corporations, associations or other institutions domiciled in the United States with a rating of at least A or equivalent by two NRSROs;
- Derivative securities are defined as synthetic securities whose price and cash flow characteristics are based on the cash flows and price movements of other underlying securities. The Board takes a conservative posture on derivative securities in order to maintain its risk-averse nature. Since it is anticipated that new derivative products may be created, it is not the intention of this policy to list specific derivatives that are allowed or prohibited from investment. The Investment Manager(s) will seek permission from the Audit, Budget and Finance Committee to include derivative investments in the endowment portfolio. The investment manager(s) will present information as to the expected return and risk characteristics of such investment vehicles and their expected contribution to the endowment.

Prohibited transactions include, but are not limited to:

- Short Selling;
- Margin Transactions; and
- Non-margin transactions which have the effect of creating leverage.

#### **Selection of Financial Institutions and Broker/Dealers**

Purchase and sale of investment securities, other than the initial issue purchases, should be made through seeking competitive bids and offers from two or more dealer/brokers for each security, whenever possible (excluding transactions with money market mutual funds and public funds investment pools, which are deemed to be made at prevailing market rates). The Board must adopt and annually review a list of qualified dealer/brokers authorized to engage in investment transactions with the College District. *[Texas Government Code Section 2256.025]* A written copy of this investment policy shall be presented to any person seeking to sell to the College District an authorized investment. *[Texas Government Code Section 2256.005(k)]* A Qualified representative *[Texas Government Code Section 2256.002(10)]* of the business organization seeking to sell an authorized investment must execute a written instrument substantially to the effect that the registered principal has received and thoroughly reviewed the investment policy of the College District and acknowledged that the organization has implemented procedures and controls in an effort to preclude transactions that are not authorized by

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this policy. *[Texas Government Code Section 2256.005(k)]* Form [C.1.7.F](#) Texas Public Funds Investment Act Certification by Dealer may be used to satisfy this requirement.

#### **Safekeeping and Custody**

Securities and collateral will be held by a third party custodian designated by the Board and held in the College District's name as evidence by safekeeping records of the institutions with which the securities are deposited. All transactions, except those with an investment pool or mutual fund, will be settled on a delivery versus payment method. *[Texas Government Code Section 2256.005(4)(e)]*

#### **Collateralization**

The College District shall require full collateralization of all investments and funds on deposit with the College District's depository bank, other than investments, which are obligations of the U.S. government and its agencies and instrumentalities. In order to anticipate market changes and provide a level of security for all funds, the collateralization level shall be 100% percent of market value of principal and accrued interest on the deposits or investments less an amount insured by the FDIC. *[Texas Government Code Sections 2257.021, 022]*

#### **Monitoring Market Prices**

The market value of the portfolio will be obtained monthly from the investment advisor, the custodian bank, or the investment manager, as appropriate. Market value of pooled or mutual funds will be obtained from published sources, such as their websites.

#### **Non-compliance with Policy/Credit Downgrades**

It is not a requirement to liquidate investments that were authorized investments at the time of purchase *[Texas Government Code Section 2256.017]*; however the investment must be evaluated by the investment officer to determine if it is prudent to liquidate. Investments that are downgraded to less than the required minimum credit rating should be liquidated in a prudent manner. *[Texas Government Code Section 2256.021]*

#### **Reporting**

An investment report will be prepared on a quarterly basis by the investment officers(s) and the investment advisor and submitted to the Board. The report must state that it was generated in compliance with the Investment Policy and PFIA, be signed by all investment officers and will minimally include the following:

For separate investments: detailed investment position including type of asset, book and market value, maturity and accrued interest

For each pooled fund group or mutual fund: name of pooled fund, beginning and ending market value, changes and accrued interest

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For all investments: weighted average maturity and diversification

*[Texas Government Code Section 2256.023]*

Additionally, if an investment advisor is used, a report will be submitted at least quarterly by the investment advisor detailing the market value of the investments, utilizing a named, commonly accepted pricing source, and the performance of the investments. The pricing of mutual funds and pooled funds will be obtained directly from those institutions.

For endowment funds and funds acting as endowments, the investment consultant will prepare quarterly reports to the Associate Vice Chancellor of Finance and Fiscal Services to evaluate manager and portfolio performance. The report will include performance (return and risk), comparisons to appropriate market indices, the Endowment's custom benchmark, the Consumer Price Index and appropriate manager universes. The investment consultant will deliver an annual report to the Board.

#### **Policy Review**

This policy and strategies will be reviewed not less than annually by the Associate Vice Chancellor of Finance and Fiscal Services, the Audit, Budget, and Finance Committee, and the Board. The Board will adopt a written statement stating that it has reviewed the policy and strategies. *[Texas Government Code Section 2256.005(e)]*

A copy of this approved statement will be posted on the College District's website, provided to all investment dealers and investment managers doing business with the College District, and also shall be provided to other interested parties on request. Confirmation of receipt and review of this policy by persons employed by an organization providing investment services to the College District and who deal directly with College District accounts shall be received by the College District prior to the institution of such services. *[Texas Government Code Section 2256.005(k)]*

#### *Sources:*

Public Funds Investment Act, Texas Government Code Chapter 2256

Public Funds Collateral Act, Texas Government Code Chapter 2257

Uniform Management of Institutional Funds Act, Texas Property Code Chapter 163

[Form C.1.7.F Texas Public Funds Investment Act Certification by Dealer](#)

Legal Reference - TACC Policy Reference Manual

CAK(LEGAL) Appropriations and Revenue Sources: Investments