

Board Meeting Minutes  
July 5, 2016

Present were:

Doug La Follette, Commissioner  
Matt Adamczyk, Commissioner  
Brad Schimel, Board Chair  
Jonathan Barry, Executive Secretary  
Tom German, Deputy Secretary  
Richard Sneider, Loan Analyst and  
Chief Investment Officer  
Vicki Halverson, Office Manager  
Brian Hellmer  
Mark Ready

Secretary of State  
State Treasurer  
Attorney General  
Board of Commissioners of Public Lands  
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Board of Commissioners of Public Lands  
UW – Madison School of Business  
UW – Madison School of Business

**ITEM 1. CALL TO ORDER**

Board Chair Schimel called the meeting to order at 2:02 p.m.

**ITEM 2. APPROVE MINUTES – JUNE 20, 2016**

**MOTION:** Board Chair Schimel moved to approve the minutes; Commissioner La Follette seconded the motion.

**DISCUSSION:** None.

**VOTE:** The motion passed 3-0.

**ITEM 3. APPROVE LOANS**

Executive Secretary Barry reported that the loans had been reviewed for proper public purpose.

<u>Municipality</u>	<u>Municipal Type</u>	<u>Loan Type</u>	<u>Loan Amount</u>
1. Bayfield Bayfield County Application #: 02016207 Purpose: Finance water main and street projects	City Rate: 3.50% Term: 20 years	General Obligation	\$101,706.79
2. Bayfield Bayfield County Application #: 02016208 Purpose: Finance water main project	City Rate: 3.50% Term: 20 years	General Obligation	\$140,000.00
3. Bayfield Bayfield County Application #: 02016209 Purpose: Refinance BCPL loan #2016020	City Rate: 3.50% Term: 13 years	General Obligation	\$90,138.36
4. Bayfield Bayfield County Application #: 02016210 Purpose: Refinance BCPL loan #2016023	City Rate: 3.50% Term: 18 years	General Obligation	\$94,693.72

5.	Bayfield Bayfield County Application #: 02016211 Purpose: Refinance BCPL loan #2016017	City Rate: 3.50% Term: 19 years	General Obligation	\$712,599.10
6.	Green Lake Green Lake County Application #: 02016214 Purpose: Purchase industrial park land	City Rate: 2.50% Term: 5 years	General Obligation	\$175,000.00
7.	Harrison Calumet and Outagamie Counties Application #: 02016213 Purpose: Purchase snow plow truck	Village Rate: 2.50% Term: 5 years	General Obligation	\$250,000.00
8.	Ontario Vernon County Application #: 02016206 Purpose: Finance street project	Village Rate: 2.50% Term: 5 years	General Obligation	\$25,000.00
9.	Pleasant Springs Dane County Application #: 02016217 Purpose: Finance road projects	Town Rate: 2.50% Term: 1 years	General Obligation	\$75,000.00
10.	Waupaca Waupaca County Application #: 02016212 Purpose: Finance 2016 capital projects	City Rate: 3.00% Term: 6 years	General Obligation	\$545,000.00
11.	West Allis - West Milwaukee, Et. Al. Milwaukee and Waukesha Counties Application #: 02016215 Purpose: Finance capital improvement projects	School Rate: 3.00% Term: 10 years	General Obligation	\$3,000,000.00
<b>TOTAL</b>				<b>\$5,209,137.97</b>

**MOTION:** Board Chair Schimel moved to approve the loans; Commissioner La Follette seconded the motion.

**DISCUSSION:** Commissioner Adamczyk expressed concern that loan customers are allowed to refinance existing State Trust Fund Loans (STFL) with a new loan in order to capture lower interest rates.

Commissioner La Follette asked if this has to be allowed and if a STFL can be refinanced more than once. Executive Secretary Barry replied that it does not have to be allowed and loans can be refinanced more than once. He added that customers are required to borrow additional funds in order to refinance an existing loan. While the policy could be reviewed and evaluated, not allowing STFLs to be refinanced in-house could result in a loss of income to the portfolio if customers refinance with another lending institution.

**VOTE:** The motion passed 2-1. Commissioner La Follette and Board Chair Schimel voted aye; Commissioner Adamczyk voted no.

#### **ITEM 4. DISCUSS DRAFT INVESTMENT POLICY AND ASSET ALLOCATION MODEL**

Board Chair Schimel introduced Brian Hellmer and Mark Ready from the UW-Madison School of Business and thanked them for their input and assistance in helping the Board's staff develop an investment policy and asset allocation model.

Executive Secretary Barry said that BCPL was granted prudent investment authority by the legislature in 2015. In order to utilize this authority in a careful and prudent manner, the Board must adopt an investment policy. He added that staff was not asking for the Board's approval at the meeting but rather allow time for them to review the draft policy and submit questions and suggestions. Perhaps within a month the Board would be ready to approve a final policy.

Richard Sneider explained that an investment policy would:

- guide future investment decision-making because the Prudent Investment Standard allows for more investment options;
- provide a guide for all future investments and ensure long-term prudence by current and future Commissioners and agency staff;
- create the opportunity for the Board to earn capital gains while reducing risk by establishing a "smoothing fund;" and
- put more Trust Fund principal to work, thereby increasing earnings for the beneficiaries.

The draft investment policy presented to the Board was developed with the following in mind:

- beneficiaries rely on a stable, sustainable income distribution to support K-12 public school libraries;
- distributions to beneficiaries can only be made from income earnings as the State Constitution requires School Trust Fund principal be retained in the trust; and
- the rate of growth of the Common School Fund's principal from unclaimed property and fees, fines and forfeitures has declined, which impacts the amount of monies available for investing.

Executive Secretary Barry said that minimum annual earnings distributions of 3.5% of trust fund principal balances had been established as a target to meet beneficiaries' expectations. He asked Mr. Sneider to explain the smoothing fund. Mr. Sneider said that a segregated fund (i.e., smoothing fund) would be established using income earnings above the targeted 3.5%. These funds could then be used to supplement distributions during years when income does not meet the targeted annual distribution.

Commissioner La Follette inquired about the timing of the earnings distribution and whether retaining the earnings in the smoothing fund was permitted. Deputy Secretary German replied that while the state constitution requires that fund earnings be distributed annually, the distribution occurs mid-year so any earnings received after that time would be retained for future distribution. Mr. Sneider added that once the smoothing fund becomes fully developed, the distributable earnings might very well exceed the 3.5% target and would be based on distributions over the last five years.

The Commissioners, staff and professionals from the UW-Madison School of Business discussed the risk/return characteristics surrounding the expanded investment authority and how to mitigate the risks while generating returns.

Commissioner Adamczyk expressed his desire that SWIB (State of Wisconsin Investment Board) invest a portion of School Trust Funds for the Board and cited information indicating that their average return on investments over the past 20 years was 7.4%. His preference would be to limit investments in State Trust Fund Loans (STFL) and allow SWIB to invest those funds. Executive Secretary Barry said that the Board was providing a service to local governments and school districts with competitive rate loans while earning a good rate of return with very low risk. He added that the investment policy was necessary whether the School Trust Funds are invested by staff or SWIB.

Commissioner La Follette noted that there were two aspects to the July 5 meeting and those included whether the Board agreed with the draft investment policy and, if adopted, establishing an asset allocation model for investments. He asked staff what action the Board needed to take, if any. Board Chair Schimel replied that no action would be taken on the matter at this time and the Commissioners should review the policy further. The Board could take action at a future meeting, perhaps in a month.

Commissioner La Follette asked Brian Hellmer and Mark Ready for their comments. Mr. Hellmer said the draft policy takes advantage of the new investment opportunities allowed by the legislation while establishing a fund with limited earnings volatility from year-to-year. In regards to State Trust Fund Loans, the relationship between the earnings and risk in this investment is very favorable and having a portion of the portfolio's assets in this investment is desirable. While deposits to the Common School Fund from fees, fines and forfeitures, and unclaimed property have not kept pace with inflation, investing in instruments that result in capital gains would help to increase the principal of the Trust Funds.

The Commissioners discussed how best to diversify the fund investments and whether that would be managed by staff or an outside entity. Mr. Sneider said that cost is an important factor when retaining an investment firm to manage the Board's assets but a passively-managed index fund could be a cost effective alternative.

Board Chair Schimel noted that staff had record investment earnings over the last couple years in spite of the low interest rate environment. He asked what type of activity, other than low interest rates, would trigger the use of the smoothing account. Mr. Sneider replied that investing a significant portion of Trust Funds in non-incoming producing assets. Deputy Secretary German noted that 10-year Treasury bond interest rates are at an all-time low and the expanded investment authority provides additional options for investing in instruments that earn higher rates of return.

Commissioner Adamczyk said statutes allow for the sale of State Trust Fund Loans and asked about the logistics involved should the Board choose to sell them. Mr. Sneider said the loans could be packaged into a security and sold to an investor.

Commissioner Adamczyk said he had talked to officials in the Governor's office and Legislature about the possibility of BCPL investing in real estate; specifically, constructing or purchasing buildings that would house state agencies and then leasing the building to state agencies. Board Chair Schimel noted that any lease revenues would be offset by building maintenance costs. Asked if legislation had been drafted, Commissioner Adamczyk said no but he had discussions with a Legislator who would be willing to assist with that. The Commissioners and staff discussed the pros and cons of such a venture.

#### **ITEM 5. FUTURE AGENDA ITEMS**

None.

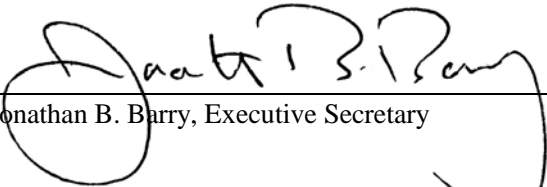
#### **ITEM 6. EXECUTIVE SECRETARY'S REPORT**

Nothing to report.

**ITEM 7. ADJOURN**

**MOTION:** Commissioner Adamczyk moved to adjourn the meeting; Commissioner La Follette seconded the motion.

The meeting adjourned at approximately 3:35 p.m.



Jonathan B. Barry, Executive Secretary

These minutes have been prepared from a recording of the meeting. The summaries have not been transcribed verbatim.  
Link to audio recording: [ftp://doafpt1380.wi.gov/doadocs/BCPL/2016-07-05\\_BCPL-BoardMtgRecording.mp3](ftp://doafpt1380.wi.gov/doadocs/BCPL/2016-07-05_BCPL-BoardMtgRecording.mp3)