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Jonathan Barry, *Executive Secretary*

## AGENDA

August 9, 2017  
2:00 P.M.

Board of Commissioners of Public Lands  
101 E. Wilson Street, 2<sup>nd</sup> Floor  
Madison, Wisconsin

### Routine Business:

- 1) Call to Order
- 2) Approve Minutes – July 25, 2017 (Attachment)
- 3) Approve Loans (Attachment)

### Old Business:

None

### New Business:

None

### Routine Business:

- 4) Future Agenda Items
- 5) Executive Secretary's Report (Attachments)
  - Investment Transaction Report – August 3, 2017
  - Quarterly Investment Report – Second Quarter 2017
- 6) Adjourn

## AUDIO ACCESS INFORMATION

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**BOARD MEETING  
AUGUST 9, 2017**

**AGENDA ITEM 2  
APPROVE MINUTES**

Attached for approval are the minutes from the July 25, 2017, board meeting.

Board Meeting Minutes  
July 25, 2017

Present were:

Doug La Follette, Commissioner	Secretary of State
Matt Adamczyk, Commissioner	State Treasurer
Brad Schimel, Board Chair	Attorney General
Jonathan Barry, Executive Secretary	Board of Commissioners of Public Lands
Tom German, Deputy Secretary	Board of Commissioners of Public Lands
Richard Sneider, Loan Analyst and Chief Investment Officer	Board of Commissioners of Public Lands
Vicki Halverson, Office Manager	Board of Commissioners of Public Lands

**ITEM 1. CALL TO ORDER**

Board Chair Schimel called the meeting to order at 2:00 p.m.

**ITEM 2. APPROVE MINUTES – JULY 5, 2017**

**MOTION:** Commissioner La Follette moved to approve the minutes; Board Chair Schimel 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. Christmas Mountain Sanitary District Sauk County Application #: 02017212 Purpose: Finance sanitary sewer projects	Sanitary District Rate: 4.00% Term: 20 years	General Obligation	\$650,000.00
2. Clayton Polk County Application #: 02018003 Purpose: Purchase dump truck	Village Rate: 3.50% Term: 10 years	General Obligation	\$160,000.00
3. Janesville Rock County Application #: 02018009 Purpose: Finance fire protection	Town Rate: 3.00% Term: 1 year	General Obligation	\$300,000.00
4. Johnson Marathon County Application #: 02018014 Purpose: Refinance grader loan	Town Rate: 3.00% Term: 5 years	General Obligation	\$220,000.00

5.	Maxville Buffalo County Application #: 02018011 Purpose: Finance roadwork	Town Rate: 3.00% Term: 5 years	General Obligation	\$45,000.00
6.	Phelps Vilas County Application #: 02018012 Purpose: Finance road projects	Town Rate: 4.00% Term: 15 years	General Obligation	\$700,000.00
7.	Phelps Vilas County Application #: 02018013 Purpose: Refinance BCPL loan #2009255	Town Rate: 3.50% Term: 10 years	General Obligation	\$354,039.93
8.	Richland Richland County Application #: 02018001 Purpose: Purchase squad cars	County Rate: 3.00% Term: 4 years	General Obligation	\$120,000.00
9.	Richland Richland County Application #: 02018002 Purpose: Finance capital projects	County Rate: 3.50% Term: 10 years	General Obligation	\$1,390,421.00
10.	Salem Pierce County Application #: 02018010 Purpose: Finance bridge replacement	Town Rate: 3.00% Term: 5 years	General Obligation	\$270,000.00
11.	Sheboygan Sheboygan County Application #: 02017213 Purpose: Finance TID #16 development incentive	City Rate: 3.50% Term: 10 years	General Obligation	\$400,000.00
12.	Sugar Camp Oneida County Application #: 02018005 Purpose: Purchase land; construct ambulance building	Town Rate: 3.50% Term: 10 years	General Obligation	\$300,000.00
13.	Verona Area Dane County Application #: 02018007 Purpose: Finance school projects	School Rate: 3.00% Term: 5 years	General Obligation	\$5,000,000.00
14.	Wautoma Waushara County	Town Rate: 3.00%	General Obligation	\$60,000.00

	Application #: 02018008 Purpose: Finance roadwork	Term 2 years		
15.	Whitelaw Manitowoc County Application #: 02018006 Purpose: Finance roadwork	Village Rate: 4.00% Term: 15 years	General Obligation	\$170,000.00
16.	Winchester Winnebago County Application #: 02018004 Purpose: Finance roadwork	Town Rate: 3.00% Term: 4 years	General Obligation	\$100,000.00
17.	Wisconsin Rapids Portage and Wood Counties Application #: 02018015 Purpose: Finance energy efficiency and capital improvement projects	School Rate: 3.50% Term: 10 years	General Obligation	\$11,500,000.00
		<b>TOTAL</b>		<b>\$21,739,460.93</b>

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

**DISCUSSION:** Commissioner Adamczyk stated that while he is opposed to all the loans, he was particularly opposed to the energy efficiency loan to the Wisconsin Rapids School District. He claimed that the “vast majority of people in Wisconsin Rapids have no clue this was going to happen and we’re doubling their debt without them knowing.” Board Chair Schimel replied that the school district board was increasing their debt, not the Commissioners. Chairman Schimel asserted that the BCPL’s responsibility is to lend money to local government entities for projects that meet the statutory obligation of “proper public purpose,” which this loan does. He added that it is outside the BCPL’s scope to assess the policies that local government entities employ when borrowing from the State Trust Fund Loan program.

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

**ITEM 4. PROPOSED LAND BANK SALE TO THE PUBLIC (S1702-GANDER LAKE ROAD; S1703-ROCKY LAKE ROAD; AND S1707-LEOLA DITCH)**

**MOTION:** Commissioner Adamczyk moved to approve the sale of the properties via sealed bid; Commissioner La Follette seconded the motion.

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

**NOW, THEREFORE BE IT RESOLVED**, that the Board of Commissioners of Public Lands authorizes the sale of the Properties pursuant to a sealed bid process. The minimum acceptable bid for each Property shall be the appraised value for such respective Property determined by the independent appraisers as set forth above. Such sales shall be conducted in accordance with Chapter 24 of the Wisconsin Statutes on such terms and conditions as the Executive Secretary determines to be reasonable and necessary. The Executive Secretary is authorized and directed to execute any documents reasonably necessary to complete such transactions.

**ITEM 5. PROPOSED LAND BANK SALE – DEPT. OF MILITARY AFFAIRS, VOLK FIELD PROPERTY, JUNEAU COUNTY (\$1704)**

**MOTION:** Commissioner La Follette moved to approve the sale of the property to the Department of Military Affairs; Commissioner Adamczyk seconded the motion.

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

**NOW, THEREFORE BE IT RESOLVED**, that the Board of Commissioners of Public Lands approves the sale of the Property to the Department of Military Affairs at the price of Thirty Thousand Dollars (\$30,000) in accordance with Chapter 24 of the Wisconsin Statutes on such terms and conditions as the Executive Secretary determines to be reasonable and necessary. The Executive Secretary is authorized and directed to execute any documents reasonably necessary to complete such transaction.

**ITEM 6. PROPOSED LAND BANK PURCHASE – AMERICAN TIMBERLAND, LLC, ONEIDA COUNTY (P1702)**

Executive Secretary Barry explained that the purchase of this property meets four criteria of the land bank legislation: improve and protect public access to BCPL Trust Lands, improve management efficiencies on Trust Lands, provide productive timberland that will result in revenues to the Trust Funds, and reduce forest fragmentation.

Commissioner Adamczyk said that forest fragmentation should not be a concern of the BCPL but rather something that the WI DNR should address. Board Chair Schimel replied that being good stewards of the Board's assets (i.e., the Trust Funds and Trust Lands) *was* their responsibility. Enhancing the value of the Trust Lands in the manner Executive Secretary Barry described allows staff to manage them efficiently while at the same realizing cost savings.

Commissioner La Follette expressed concern about the communication the State Treasurer has had with legislators and whether those communications are appropriate as they relate to the actions of the BCPL. He asked the State Treasurer for copies of all communications – emails, written or text messages – with legislators that he has had over the last three months. Commissioner Adamczyk replied that he had been in contact with some legislators who shared his opposition to the proposed Land Bank purchase. Commissioner La Follette went on to report that he had recently received a letter from six legislators asking him to vote no on the purchase, which he suspected was a result of Commissioner Adamczyk's communication with them. Commissioner Adamczyk said he was within his right to contact legislators and work against matters that were before the Board. He said he would forward his communications to the other Commissioners.

**MOTION:** Commissioner La Follette moved to approve the purchase of the American Timberland property; Board Chair Schimel seconded the motion.

**DISCUSSION:** Commissioner Adamczyk objected to the purchase on the grounds that the property was only being purchased to provide access to 80 acres of Trust Lands with a small amount of timber. He also did not believe that the board had the constitutional authority to purchase land. He asserted that BCPL only had authority to sell the Trust Lands, especially since the Board hadn't purchased any land for 150 years prior to Land Bank Authority. Board Chair Schimel replied that the Constitution allows the Commissioners to manage the Trust Lands in the manner in which the legislature directs them to. He also pointed out that the agency did not purchase

land prior to Land Bank Authority because statutes did not allow it. He added that Commissioner Adamczyk was “dead wrong” in his assertion about the constitutionality of the Board purchasing land. Commissioner Adamczyk “completely” disagreed.

Commissioner Adamczyk questioned why the Board was in a rush to purchase the property and if a better price could be negotiated after three, four months or more. Board Chair Schimel pointed out that American Timberland would likely harvest the timber and subdivide the property if it was not sold as one large block. Executive Secretary Barry added that the benefits to purchasing this large block of property included timber revenue now and in the future, the ability to manage adjacent Trust Lands more efficiently, and the appreciation of the land itself.

Commissioner Adamczyk again asserted that the land was being purchased to only enhance 80 acres of isolated Trust Lands. Board Chair Schimel replied that he was either “intentionally ignoring the point” or missing the point, and it was not about the 80 acres he (Commissioner Adamczyk) kept referring to. He added that a potential land trade with the US Forest Service would further enhance and enlarge the block of Trust Lands adjacent to the proposed land purchase. Commissioner Adamczyk said that “a swap is fine if it blocks our land better” but was still opposed to this purchase.

Executive Secretary Barry said that timber revenues are higher on a larger block of Trust Lands because a logger’s organizational costs are the same whether the area logged is large or small. Because of this, they are willing to bid higher on a larger sized timber sale because it is more cost effective.

Board Chair Schimel said legislators from northern Wisconsin told him that they wanted BCPL lands managed in a way that increased the forestry industry and created jobs in that region. Commissioner Adamczyk claimed that he did not know of any legislators – Democrat or Republican – who supported the purchase. Board Chair Schimel replied that perhaps none would publicly express support because of the “political turmoil” Commissioner Adamczyk had brought to the matter and that he had not made it an “honest debate.” He went on to say that he resented Commissioner Adamczyk’s assertion that the “only conservative option” would be to vote against purchasing the land. Chairman Schimel noted that there is a conservative interest in this purchase because it would increase the value of the Board’s assets and grow the School Trust Fund for the beneficiaries.

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

#### **ITEM 7. FUTURE AGENDA ITEMS – LRB Draft #17-3986/P1**

Commissioner Adamczyk referred the Commissioners to a recent article where Executive Secretary Barry had made disparaging comments about him. Board Chair Schimel said that perhaps he had asked for it given the language Commissioner Adamczyk has used towards the staff and the public and private abuse he’s given staff. Commissioner Adamczyk replied that he wants the land and investments managed by other entities and could understand why staff would be resistant to that but he had “every right to push that.” Commissioner La Follette replied that while Commissioner Adamczyk has a right to vote his position, he does not have the right to harass staff, which makes it difficult for them to do their work and tasks the Board has assigned them. Executive Secretary Barry said that the article Commissioner Adamczyk was referring to was unfortunate and Secretary Barry accepted Commissioner Adamczyk’s complaint regarding the public comments.

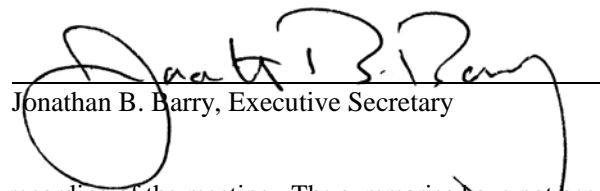
## ITEM 8. EXECUTIVE SECRETARY'S REPORT

Executive Secretary Barry referred the board to the Investment Transaction Report that was included in the board meeting packet. Secretary Barry noted that a certain bond investment house had recently analyzed government and agency bond issues in the last six months and found that BCPL had managed to acquire a significant position in the bonds bearing the highest coupon rates. Board Chair Schimel congratulated Rich Sneider on his acumen on such bond purchases.

## ITEM 9. ADJOURN

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

The meeting adjourned at approximately 3:00 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://doaftp1380.wi.gov/doadocs/BCPL/2017-07-25\\_BCPL-BoardMtgRecording.mp3](ftp://doaftp1380.wi.gov/doadocs/BCPL/2017-07-25_BCPL-BoardMtgRecording.mp3)



**BOARD MEETING  
AUGUST 9, 2017**

**AGENDA ITEM 3  
APPROVE LOANS**

<u>Municipality</u>	<u>Municipal Type</u>	<u>Loan Type</u>	<u>Loan Amount</u>
1. Clover Sanitary District #1 Bayfield County Application #: 02018020 Purpose: Finance sanitary system maintenance	Sanitary District Rate: 3.00% Term: 5 years	General Obligation	\$45,000.00
2. Kewaskum Washington County Application #: 02018018 Purpose: Finance road projects	Village Rate: 3.50% Term: 10 years	General Obligation	\$999,479.00
3. Madison Metropolitan Dane County Application #: 02018024 Purpose: Finance tennis court renovation	School Rate: 3.00% Term: 5 years	General Obligation	\$462,950.00
4. Mason Bayfield County Application #: 02018022 Purpose: Finance road projects	Town Rate: 3.50% Term: 10 years	General Obligation	\$260,000.00
5. Phillips Price County Application #: 02018021 Purpose: Construct digital fabrication laboratory	School Rate: 3.50% Term: 10 years	General Obligation	\$237,000.00
6. Phillips Price County Application #: 02018023 Purpose: Refinance BCPL loan #2011100	School Rate: 3.50% Term: 10 years	General Obligation	\$946,973.68
7. Plymouth Sheboygan County Application #: 02018017 Purpose: Purchase fire truck	Town Rate: 3.00% Term: 5 years	General Obligation	\$150,000.00
8. Withee Clark County Application #: 02018016 Purpose: Finance sewer liner installation	Village Rate: 3.00% Term: 2 years	General Obligation	\$25,000.00

Municipality	Municipal Type	Loan Type	Loan Amount
9. Wrightstown Brown and Outagamie Counties Application #: 02018019 Purpose: Finance TID land acquisition and capital projects	Village Rate: 3.50% Term: 10 years	General Obligation	\$824,772.00
<b>TOTAL</b>			<b>\$3,951,174.68</b>

**BOARD MEETING  
AUGUST 9, 2017**

**AGENDA ITEM 5  
EXECUTIVE SECRETARY'S REPORT**

Attached for review is the following report:

- Investment Transaction Report – August 3, 2017
- Quarterly Investment Report – Second Quarter 2017

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### Investment Transaction Report August 3, 2017

#### Bond Purchases

Issuer	Credit Rating	Trade Date	Par Value	Price Paid	Coupon	Call Date	Yield to Call	Maturity Date	Yield to Maturity
FFCB	Aaa	07/28	\$3,716,000	\$3,699,278	3.34%	09/22/17	6.52%	12/22/31	3.38%

#### Bond Sales

Since the last report, staff has not sold any bonds.

To date in 2017, net profit realized on the sale of bonds totals \$8 million, including \$7.7 million classified as long-term capital gains. As provided in the IPS, 75% of long-term capital gains are retained in the Common School Fund (CSF) smoothing fund. The remaining 25% of long-term capital gains, along with all short-term capital gains, are distributed to Trust Fund beneficiaries in the following year.

#### Current Holdings

#### Combined Trust Fund Bond Portfolios

Investment Type	8/03/17	7/19/17
Wisconsin and State Agency Bonds	\$162,628,631	\$162,628,631
Wisconsin Municipal and School Bonds	\$181,829,198	\$185,489,305
Treasury and Federal Agency Bonds	<u>\$172,275,388</u>	<u>\$178,030,110</u>
Total Bond Investments (at cost)	\$516,733,217	\$526,148,046
(at market value)	<u>\$526,789,172</u>	<u>\$536,017,432</u>
Unrealized Gains	\$10,055,955	\$9,869,386

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## Investment Report - Second Quarter 2017

### Executive Summary

BCPL investment performance continues to exceed benchmark returns. Risk-adjusted returns in the BCPL-managed portfolios had a yield **0.57% greater** than our benchmark. This difference in yield means that beneficiaries earned **\$1.55 million more** during the second quarter than would have been generated by an investment in the benchmark portfolio.

The above performance measure does not include **\$8 million in capital gains** realized through bond sales during the first half of 2017. Booking these profits had the immediate impact of reducing portfolio risk by converting 'paper gains' into cash, increasing the 2018 distribution to beneficiaries, and providing the initial funding of the Common School Fund (CSF) smoothing account in accordance with the Investment Policy Statement.

The BCPL Investment Committee continues to formulate plans for the methodical purchase of equity ETFs beginning upon a pull-back in public equity prices from current record levels. In other matters, due diligence continues regarding BCPL investments in the venture capital fund 4490 Ventures II and in a package of seasoned WHEDA apartment mortgage loans.

### Q2 Investment Highlights and Outlook

During the second quarter, interest rates moved within an expected range. Staff execution of a 'buy low and sell high' strategy has worked quite well, with market volatility utilized to benefit BCPL beneficiaries. In fact, one of our brokers researched all bonds sold by the federal agencies FFCB and FHLB in 2017 and compared that list to BCPL bond purchases. The research found that BCPL had purchased the five bonds with the highest interest rates, and purchased these five very heavily. With agency bonds sold worldwide, BCPL was fortunate to have aggressively purchased almost 80% of the top five bonds available. These five investments alone (totaling \$32.5 million) will provide an additional \$300,000 annual income to beneficiaries (compared to buying the five comparable bonds issued with the lowest rates).

Loan demand remains strong and relative yields on the loan portfolio continue to outperform investment alternatives. During FY2017, BCPL received \$238 million in loan applications, the highest total in many years and nearly 80% higher than the average over the past five years. The \$435 million invested in Trust Fund loans at the end of FY2017 had an average yield that was 1.66% higher than the comparable-maturity Treasuries. Trust Fund beneficiaries receive excellent risk-adjusted returns through these loan investments, as BCPL has never experienced a loan default in the 146 year history of the program.

### Summary and Benchmark Comparison

The overall expected yield of funds managed by BCPL was 3.28% at the end of third quarter, a slight decrease from the prior quarter. This expected yield does not include \$8 million in capital gains realized through bond sales during the first half of 2017.

The best measure for comparing investment performance against our benchmark is the SEC yield, which provides a standard methodology that is available for the mutual funds and bond indices that comprise our custom benchmark. The risk-adjusted yield of BCPL-managed portfolios remains 0.57% greater than benchmark returns.

## BCPL Investment Summary

### 2nd Quarter 2017

as of June 30, 2017

Portfolio Summary		Total Assets	Expected Yield <sup>1</sup>	SEC Yield <sup>2</sup>	Average Credit Quality <sup>3</sup>	Weighted Avg Maturity
Total BCPL Managed Financial Assets		\$ 1,087,910,339	3.28%	3.17%	Aa1	8.53
Benchmark Performance <sup>4</sup>				3.04%	A1	8.78
<b>BCPL Investments</b>						
	% of Total BCPL Managed Assets					
Bonds	45.23%	\$ 492,116,065	3.66%	3.44%	Aa2	13.94
BCPL State Trust Fund Loans	40.03%	\$ 435,480,543	3.65%	3.65%	Aa1	5.55
Cash and Cash Equivalents <sup>5</sup>	14.74%	\$ 160,313,731	0.90%	0.90%	Aaa	0.03
<b>Total BCPL Managed Investments</b>		<b>\$ 1,087,910,339</b>	<b>3.28%</b>	<b>3.17%</b>	<b>Aa1</b>	<b>8.53</b>
<b>Benchmark Components</b>						
	Weighting					
S&P Long Intermediate Term Taxable Municipal Bond Index <sup>6</sup>	60.00%		3.35%	3.86%	Aa3	9.74
S&P U.S. Treasury Bill Index <sup>7</sup>	10.00%		0.72%	0.72%	Aaa	0.09
Wisconsin Tax-Exempt Bond Mutual Funds (combined) <sup>8</sup>	30.00%	\$ 361,700,001	N/A	2.16%	Baa2	9.74
<b>Total Benchmark</b>		<b>100.00%</b>		<b>3.04%</b>	<b>A1</b>	<b>8.78</b>

Important Notes on Following Page

Prepared by Richard Sneider

**Notes to BCP L Benchmark Comparison:**

<sup>1</sup> **Expected Yield** is the weighted average yield to the redemption date for each bond, and assumes that issuers will redeem bonds at the earliest possible date, when it is in their best interest given current market interest rates. Also called 'yield-to-worst'; this number is equal to the lower of the 'yield to call' and 'yield to maturity' for each investment in the portfolio.

<sup>2</sup> **SEC Yield** - The SEC yield should not be confused with the expected yield on invested funds. The SEC yield will vary substantially with market conditions because it is calculated using the current market value of assets, and the value of fixed income assets fluctuates with market interest rates. For example, although interest payments produced by an individual bond remain constant following the issuance of the bond, the SEC yield on this bond will increase with market interest rates solely because the value of the bond decreases (Yield = Income/Value). If all bonds are held to maturity, the actual return to the investor would equal the "yield to maturity at cost". This calculation is not provided for benchmark components and is therefore not included in this comparison. Many investors prefer to use "yield to worst", which calculates the return using the lower of the "yield to call" and "yield to maturity". The most appropriate method to compare bond portfolios is to look at **Total Return**, which combines both income and changes in the market value of the underlying assets (see note 8 below). BCP L does not have the ability to use Total Return as a method of comparison because the Trust Fund Loan Portfolio has never been valued. Rather, the SEC Yield is used for comparison because it is a standardized methodology for calculating yield as required by the Securities and Exchange Commission for all mutual funds and provides a means to compare BCP L managed funds to a simple benchmark. The SEC Yield is a close approximation to the net yield to maturity of the fund using the current market value of the fund, and is calculated as the yield to the investor (after fund expenses and fees) during the previous 30 days assuming all bonds are held to maturity. The SEC Yield for the State Investment Fund is for the most recent month available.

<sup>3</sup> **Average Credit Quality** - Except for the BCP L loan portfolio, all average credit quality ratings shown equal the weighted average credit rating of individual securities held within each portfolio. A rating for the loan portfolio is provided to improve the ability to compare BCP L managed funds to other funds. The Aa1 rating presumed for the loan portfolio is considered reasonable, as there has not been a single default in the State Trust Fund loan program since inception in 1871, and BCP L has the statutory right and requirement to cure any future default by intercepting state aid otherwise due the borrower. Mutual Fund credit quality is provided by Morningstar. The global long-term rating scale of Moody's Investor Services begins at 'Aaa' for obligations judged to be of the highest quality, subject to the lowest level of risk. The ranking in order from highest to lowest quality then includes: Aa, A, Baa, Ba, B, Caa, Ca, and C. Ratings from Aa to Caa are modified with 1,2, or 3 to provide a high, middle and low ranking within each alphabetic category. 'Investment-grade' securities have ratings of Baa3 or higher.

<sup>4</sup> **Benchmark Components and Weighting** - Due to the unique set of BCP L authorized investments consisting primarily of the BCP L State Trust Fund Loan Program, and bonds issued by the State of Wisconsin and Wisconsin municipalities and school districts, there are no managed funds that perfectly match the characteristics of the BCP L portfolio. However, the chosen benchmark components provide the best opportunity to compare BCP L investments to funds managed by other professionals. The justifications of including individual benchmark components are provided below. Component weighting begins with an estimate of average liquidity levels required throughout the year, with additional factors including an estimate of the proportion between taxable and tax-exempt project funding, and the use of current taxable and tax-exempt bond yields in developing program interest rates.

<sup>5</sup> **Cash** - Cash and cash equivalents includes all investments in the State Investment Fund and Farm Credit adjustable rate notes, and all funds managed by ADM in FDIC-insured deposit accounts.

<sup>6</sup> **S&P Long Intermediate Term Taxable Municipal Bond Index** - This taxable municipal bond index is included as a benchmark component because it properly reflects the investment strategies of BCP L managed Trust Funds, including both the direct investment in taxable municipal bonds and the influence of taxable bond yields on the development of loan program interest rates. The S&P Long Intermediate Term Taxable Municipal Bond Index matches the weighted average maturity and duration of total BCP L managed funds fairly well, although BCP L maintains better average credit quality. This index is comprised of all taxable bonds issued by any state (including the Commonwealth of Puerto Rico and U.S. territories such as the U.S. Virgin Islands and Guam) with an investment grade rating (minimum S&P BBB- or Moody's Baa3), a minimum par amount of \$1 million, and remaining maturity between 5 and 15 years. Average credit quality level is not published by S&P, but was calculated at the weighted average rating of amounts held within the separate S&P AAA, AA, A, and BBB Rated Taxable Municipal Bond indices using a formula developed by Schwab Portfolio Center, the portfolio analysis software used by BCP L. Overall, a weighting of 60% is appropriate given the average levels of cash and tax-exempt investments held by the Trust Funds throughout the year.

<sup>7</sup> **S&P U.S. Treasury Bill Index** - The U.S. Treasury Bill Index represents the average cash position held by the Trust Funds throughout the year, and is included because BCP L maintains significant levels of liquidity needed to fund expected trust fund loan demand over the next 3-6 months. The amount of portfolio liquidity (cash) varies significantly throughout the year, and is impacted by factors including the interest rate environment, the absence of prepayment penalties within the loan program, and the statutory payment structure requiring annual loan payments on March 15 each year. The S&P U.S. Treasury Bill Index is a market weighted index that includes all U.S. Treasury Bills with maturities ranging from 0-12 months. Because an index is not a managed portfolio, but only a collection of securities within a specific set of criteria, management expenses are not included. Overall, a weighting of 10% for this benchmark component is appropriate given the average levels of cash held by the Trust Funds throughout the year.

<sup>8</sup> **Wisconsin Tax-Exempt Bond Funds** - Tax-exempt bond funds are included as a benchmark component for three reasons: BCP L invests directly in tax-exempt bonds when available at acceptable terms; a significant portion of loans made through the BCP L State Trust Fund Loan Program fund projects that would qualify as tax-exempt; and current tax-exempt bond yields are an important factor in the construction of loan program interest rates. There are three bond mutual funds that invest primarily in Wisconsin State and Municipal Bonds, investments that are similar to the securities approved for BCP L investment. These funds are sponsored by Wells Fargo, Nuveen and Nationwide Ziegler, and there are significant differences between the management of these mutual funds and BCP L trust funds. All three mutual funds are limited to tax-exempt investments, a universe of securities that generally provide lower yields than the taxable instruments favored by BCP L. On the other hand, all three of these funds invest substantial amounts in bonds that have considerable default risk including bonds issued by the Commonwealth of Puerto Rico, community development revenue bonds, hospital revenue bonds, and other bonds types not available within the risk parameters of the BCP L investment authority. Overall, a weighting of 30% for this benchmark component is appropriate given the level of Trust Fund investment in tax-exempt instruments and the influence of tax-exempt bond rates on the interest rates charged within the loan program.

<sup>9</sup> **Total Return Analysis** - A total return analysis including the periodic change in asset values in addition to earnings would provide a more comprehensive and accurate comparison between the returns generated by BCP L managed funds and our benchmark. However, total return analysis requires accurate asset valuation in order to provide a reasonable basis for measuring management performance. A significant portion of BCP L managed assets are invested in loans to municipalities and school districts through the BCP L State Trust Fund Loan Program. BCP L has never sold a trust fund loan and has always held these investments to maturity. There is currently no formula or model available to determine an accurate market value of the loan portfolio. Should BCP L sell loans in the future and establish a secondary market in BCP L State Trust Fund Loans, total return analysis may provide an improvement over the current method of yield comparison as the model for measuring BCP L investment performance against the appropriate benchmarks.