

AGENDA

April 21st, 2020

2:00 P.M.

Board of Commissioners of Public Lands

101 E. Wilson Street, 2nd Floor

Madison, Wisconsin

Routine Business:

1. Call to Order
2. Approve Minutes – April 7th, 2020 (Attachment)
3. Approve Loans (Attachment)

Old Business:

4. Consideration and potential vote on changes to BCPL Investment Policy

New Business:

5. None

Routine Business:

6. Chief Investment Officer's Report
7. Executive Secretary's Report
8. Board Chair's Report
9. Future Agenda Items
10. Adjourn

AUDIO ACCESS INFORMATION

Toll Free Number: **(888) 291-0079**

Passcode: **6363690#**

Board Meeting Minutes
April 7th, 2020

Present via teleconference were:

Sarah Godlewski, Board Chair
Josh Kaul, Commissioner
Doug LaFollette, Commissioner
Joanna Beilman-Dulin

State Treasurer
Attorney General
Secretary of State
State Treasurer's Office

Present in person were:

Tom German, Executive Secretary
Mike Krueger, IT Manager
Richard Sneider, Chief Investment Officer

Board of Commissioners of Public Lands
Board of Commissioners of Public Lands
Board of Commissioners of Public Lands

Absent Board members:

None

ITEM 1. CALL TO ORDER

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

ITEM 2. APPROVE MINUTES – March 17th, 2020.

MOTION: Commissioner LaFollette moved to approve the minutes; Board Chair Godlewski seconded the motion.

DISCUSSION: None

VOTE: The motion passed 3-0.

ITEM 3. APPROVE LOANS

MOTION: Commissioner LaFollette moved to approve the loans; Board Chair Godlewski seconded the motion.

DISCUSSION: Mr. Sneider commented that the recently approved loans are standard and most of these loans are loans that have been approved in the past and are being reapproved at the lower interest rate of 2.75%, rate approved by the Board about a month ago.

Commissioner Kaul asked about the difference in interest rates. Why are some of the loans 2.75% vs. 2.5%? Is the difference in interest rate a reflection on the duration of the loan or the time of the application for the loan?

Mr. Sneider explained that it is affected by both. The interest rate is dependent on the duration of the loan, 5-year loans are currently at 2.5% and loans recently approved between 6 and 10 years are at a rate of 2.75%. The interest rate is locked at the current rate structure at the time the application is requested for a period of 60 days. If our rates go down during the processing of the loan, BCPL gives the borrower the option to restart the loan at the lower rate. Some borrowers take advantage of the lower rate and some do not because of time considerations.

Commissioner Kaul asks if BCPL staff makes this rate difference clear to borrowers.

Mr. Sneider responds, yes, BCPL does make this clear to borrowers.

VOTE: The motion passed 3-0.

MOTION - The Board of Commissioners of Public Lands (BCPL) unanimously approved **\$7,135,216.00** in State Trust Fund Loans to support **11** community projects in Wisconsin.

Town of Black Creek / Outagamie County / Finance purchase of ambulance / \$275,852.00
Town of Bloomfield / Walworth County / Finance infrastructure improvements / \$1,500,000.00
Town of Eaton / Manitowoc County / Finance purchase of plow truck / \$169,040.00
Town of Ellington / Outagamie County / Finance purchase of fire truck / \$700,000.00
Town of Emmet / Marathon County / Finance truck purchase / \$150,000.00
Town of Lakeside / Douglas County / Finance purchase of tractor/brusher / \$90,000.00
Town of Maple / Douglas County / Finance purchase of dump truck / \$200,000.00
Town of Mercer / Iron County / Finance purchase of fire truck / \$308,824.00
City of Mosinee / Marathon County / Finance water tower repainting / \$141,500.00
Village of Plover / Portage County / Finance street and other projects / \$3,500,000.00
Town of Winchester / Vilas County / Finance purchase of plow/patrol truck / \$100,000.00

ITEM 4. LOAN RATE ADJUSTMENT

DISCUSSION: Board Chair Godlewski presented the new loan rates. She explained that the market has been up and down over the last couple of weeks and with the onset of COVID there is a unique strain on the market and the new loan interest rates are a precautionary measure to protect the State Trust Fund Loan Program.

Mr. Sneider explained that BCPL reduced interest rates to a lower market rate about a month ago but there had been some liquidity problems in the market, with one issue causing disruption in long term municipal loan rates. BCPL felt that the trust fund loan program could be at risk if large municipalities proposed large loans which could potentially use up BCPL's liquidity. BCPL wants to make sure that the loan program remains viable for its customers. One way to do this is to raise interest rates for long term loans and to impose a soft cap of \$5 million dollars per loan and requiring the investment committee to approve those larger loan applications before moving forward with the loan process.

Board Chair Godlewski stated that as the Trust Fund Loan Program continues, it would be interesting to see if there will be more lending to communities regarding COVID. Board Chair Godlewski shared she has been having conversations with county and municipal treasurers and one of their issues is the extension for property tax payments. Some communities have taxes due in April and with the extension of that, their taxes are now due in July. Some communities are worried about making their school distribution in May. Many of these communities receive their tax money in April and make their school distribution payment in May. Some have discussed possible cash flow issues and would like to know if the Trust Fund Loan Program could be an option for a bridge loan situation. In addition, the State of Wisconsin over the weekend declared an emergency under the FEMA guidelines. Communities can now apply for community disaster loans, but the disbursement can take a while to get to these communities. The State Trust Fund Loan Program may be a good option for these communities while they wait for their Federal funds to come in. The precautions we take here will help protect and sustain the program in a fiduciary manner.

Commissioner Kaul asked if the rates were changed by the investment committee March 27th.

Executive Secretary German explained that the changes were made in accordance with the current delegation from the Board, with the Executive Secretary acting in concert with the Board Chairman based on the recommendation of the investment committee on that date.

Board Chair Godlewski shared that the investment committee meets every other week and talks about the rates because

BCPL wants to make sure it is competitive with the market. The market is constantly changing and as a result BCPL must adapt its rates to stay competitive but also to make sure that it is upholding its fiduciary responsibility, so people do not take advantage of the program.

Commissioner Kaul asked if the adjusted rates have been efficient given the current market.

Mr. Sneider responded, yes, it is.

Board Chair Godlewski asked Executive Secretary German to clarify if the Board will need to ratify the new loan rates and approve the soft cap of the 5 million.

Executive Secretary German replied that that is correct.

Board Chair Godlewski read the proposed resolution.

MOTION: Commissioner Kaul moved to ratify the proposed resolution; Commissioner LaFollette seconded.

VOTE: The resolution is approved 3-0.

ITEM 5. CONSIDERATION AND POTENTIAL VOTE ON SPECIAL COMMON SCHOOL FUND EARNINGS DISTRIBUTION

DISCUSSION: Board Chair Godlewski provided some background about the need for the special distribution. She explained that we are in unprecedented times as we navigate COVID-19 in Wisconsin, and this requires unprecedented action. The virus and the steps that have been taken to contain it have had an impact on our beneficiaries, public schools and the children. Board Chair Godlewski has been talking with teachers and with media specialists about how they have been doing everything they can with distance learning tools, but they do not have all the resources they need. Board Chair Godlewski shared that she spoke with an individual at WEMTA about how stressed media specialist and librarians are as they support students' eLearning needs. She explained that there is a digital divide and children do not have all the resources and technology they need. She shared that she had a discussion with Superintendent Taylor. The Superintendent said she is doing all she can but there is so much more that is needed. Board Chair Godlewski commented that in conversations with Executive Secretary German, Mr. Sneider and the investment committee it was agreed that BCPL has a responsibility to our beneficiaries and that it is prudent for BCPL to take action in a historical way because its beneficiaries need extraordinary help. The investment committee discussed what would be fiscally prudent if BCPL provided a special distribution for schools and whether this distribution would impact the fund for future distributions. During this discussion, an increase in the 2020 distribution of \$5.25 million was agreed upon. BCPL is uniquely positioned to make a positive difference for its beneficiaries during this crisis. Media specialists, now more than ever, need these funds for hot spots, eBooks and distance learning tools. Board Chair Godlewski urges the Board to pass this distribution so BCPL can make a prudent difference to its beneficiaries.

Executive Secretary German commented he had been in contact with DPI and that communication is something that makes BCPL's relationship with its beneficiaries different. In other states, once the money leaves the hands of the land commission and goes to the money managers, the conversation with beneficiaries tends to stop but because BCPL has a close relationship with its beneficiaries it has a more acute understanding of what their needs are. That is why BCPL thinks it is important it consider what it could do in this situation. Taking a closer look, several factors had to come into play, first communication with the beneficiaries, secondly being prudent and cautious in the management of the fund. Even though there have been significant losses suffered by other endowments and funds, BCPL's principal is only down less than 2%. BCPL took a hard look at how the additional distribution would affect its funds and impact its plans for diversification while still providing the libraries and schools with additional funding. BCPL is constantly looking at how the fund is performing. Given all the chaos it is wonderful that BCPL is able to do this and Executive Secretary German would like to thank everyone personally for their work on this.

Mr. Sneider shared that as of the end of the last fiscal year, June 30, 2019, BCPL had approximately 3 million dollars in the Common School Fund smoothing account. The target for this account is calculated at 50% of the following years distribution. The smoothing account's balance was targeted to be 19.1 million dollars at fiscal year end, but BCPL had

over 20 million dollars in the smoothing account at the end of the year. The supplemental distribution would utilize \$3 million from this smoothing account and should not have a significant negative impact on expected future distributions.

Board Chair Godlewski asked for clarification about the date the distribution is to be given to DPI. Is it April 15th?

Executive Secretary German replied, yes and Denise is planning on making the distribution before April 15th. He was not sure the exact date but explained that it will be there before the 15th.

Board Chair Godlewski added when DPI receives the money it will turn around and deploy it right away. She shared that media specialists across the state have said they have a lot of ways they can use these funds to help with their eLearning needs. They have assured her it is relief that when provided would be used quickly.

Commissioner LaFollette commented that he is surprised the schools need a supplemental distribution given that the previously planned distribution of \$38 million was already a record distribution. Commissioner LaFollette commented that he understands that schools are still in session but was surprised by the need for additional funds because he thought schools were not incurring the expenses they normally would in classroom teaching and thought those funds could be used for the additional tools. Commissioner LaFollette further commented that although he was surprised by the request, he was in favor of providing such a supplemental distribution.

Board Chair Godlewski commented that one of the things that librarians and media specialists need to purchase are eLearning or distant learning tools, hot spots for kids and eBooks.

Commissioner Kaul commented that he understands that schools are taking on additional costs because while they have fixed costs, they are needing to incur new costs. Schools need to make sure students who do not have access to remote learning, are able to get the tools to access that technology. These are new fixed costs that were not anticipated in their budget. Commissioner Kaul believes this is a great idea. He would also like to continue the conversation with the schools. He understands the reasoning behind being careful about not allowing our smoothing fund balance to go too low but hearing from schools about the costs they have he understands their need for resources is greater now than it has been, and BCPL is here to help them. He adds that it is a very important use of these funds and BCPL needs to assess if additional funds are appropriate.

Board Chair Godlewski commented that BCPL has a very good relationship with DPI and should continue to strengthen that relationship and follow its asset allocation and appropriately plan for this distribution and continue to make sure BCPL is here to support its beneficiaries. Board Chair Godlewski shares that she is happy that the investment committee was able to meet and come up with the plan for the distribution of 5.25 million.

MOTION: Board Chair Godlewski moved to ratify the proposed resolution; Commissioner Kaul seconded.

Commissioner Kaul requested an edit to the proposed resolution. Specifically, after the paragraph that begins “Now be it resolved...”, the following paragraph references a section in the BCPL’s investment policy. He would like that section to be added to the proposed resolution.

Executive Secretary German commented that he agrees the paragraph reads as if it refers to a specific section. He explained that at the time he wrote the proposal he believed that the reference was to a specific section identified by a numbered or letter in the investment policy, however, it is not and recommends the word section be removed.

Commissioner Kaul changes his proposed amendment to the policy to simply strike the word ‘section’ from that paragraph.

Board Chair Godlewski agreed to the amendment and stated that it will be changed in the proposal.

VOTE: The resolution is approved 3-0.

ITEM 6. PRESENTATION OF PROPOSED CHANGES TO THE BCPL INVESTMENT POLICY

Board Chair Godlewski commented that the BCPL has been working very hard on the new policy over the last few months and it is a very good policy and will guide BCPL's future investments. She highlighted specific portions. First, she comments about governance. In the new policy, governance is further clarified as to the rules and responsibilities of how BCPL manages the 1.2 billion dollars and how BCPL coordinates the fiduciary responsibilities of the commissioners. Second, the new policy redefines BCPL's investment philosophy. It takes into consideration today's financial environment to keep up with the best practices and clarifies what its fiduciary duties are, especially these three parts: 1.) asset allocation and diversification; 2.) clarify the importance of transparency; and, 3.) reaffirm the history and commitment to Wisconsin. She also comments on the risk section of the policy and how specific factors such as environmental, social and government impacts play into the role of BCPL's fiduciary duties.

Mr. Sneider commented he believes BCPL's investment policy is improved because of these changes. He adds that it is BCPL's responsibility to improve its policy as it moves forward and as the market changes.

Secretary LaFollette commented the major change in the new policy is that more authority is given to the investment committee and less to the Board.

Executive Secretary German commented that in some areas he agrees but it is not the case in as many areas as it may seem. Executive Secretary German shared that he is cognizant of that and believes that BCPL is being careful to balance the authority in an appropriate way.

Secretary LaFollette commented about the end of the document. He said he sees that in almost all BCPL's funds the allocations are different than what the previous policy allows. He asks about the adjustments to those allocations.

Executive Secretary German explained that BCPL will be readjusting the allocations and BCPL is moving away from fixed income. The market has changed so the asset allocation changes reflect the changes in the market and smoothing funds have more money in them so BCPL can afford to diversify funds more.

Secretary LaFollette shared his concern about BCPL moving toward more investment in the normal market and taking more risk.

Board Chair Godlewski responded to Secretary LaFollette's comment about governance and the change in authority of the investment committee. She explained BCPL now has a representative on the investment committee, that is new. Currently, the commissioners do not have a representative or a commissioner serving on the investment committee, but the new policy includes that.

Secretary LaFollette confirmed that the representative from the commissioners on the investment committee is Board Chair Godlewski.

Board Chair Godlewski agreed that it is her.

Commissioner Kaul commented that he would like a redlined version of the policy.

Mr. Sneider commented that he will provide a redlined copy to the commissioners.

Board Chair Godlewski explained that at the next meeting the board will discuss approving the new investment policy. She asks that any questions about the new policy be presented to Mr. Sneider and Executive Secretary German so the new policy can be approved at the next meeting.

Secretary LaFollette comments about the new allocations.

Board Chair Godlewski responded that further clarification of the asset allocations proposed can be provided by Mr. Sneider and Executive Secretary German. The asset allocation set forth is about investing so we can increase our long-term capital gain and build the principal of the fund, not just distribution.

Secretary LaFollette responded he understands the reason for the changes and recalls past conversations about the

changes but was surprised by the changes presented because he is more conservative and wants BCPL to be successful.

Board Chair Godlewski further commented that BCPL also has the smoothing fund to address any risks.

ITEM 7. CHIEF INVESTMENT OFFICER'S REPORT

Mr. Sneider shared that BCPL is moving forward with acquiring ETFs and Mutual Funds in accordance with our policy and BCPL has been accelerating that now that prices are more reasonable. He further explained the overall yield for BCPL's ETFs and Mutual Funds portfolio is 4.6% compared to early March which was 4%. When prices go down, yields go up which is good for beneficiaries moving forward.

ITEM 8. EXECUTIVE SECRETARY'S REPORT

Executive Secretary German shared what is happening at BCPL during this time of 'safer at home'.

- Deployed desktops, monitors, laptops and iPads to allow all BCPL employees to work remotely.
- Processed \$91 Million in payments on 1100 trust fund loans and 730 customers
- Processed over 50 State Trust Fund Loan applications
- Disbursed 13 Trust Fund Loans totaling \$5.7 Million
- Deployed \$40 million in investments in real estate funds.
- Deployed \$60 million in investments in Exchange Traded Funds (ETFs)
- Deployed \$600,000 in investments in previously committed venture capital (VI)
- Reconciled March financial statements
- Signed contracts for the sale of 133 acres of timber totaling \$134,000. (BCPL finished marking 80 of those acres for sale during this time as well).
- Conducted due diligence on 400 acres of school trust lands in Ashland and Iron Counties that may be sold or exchanged
- Conducted due diligence on thousands of acres of Forestland Group properties that BCPL staff is reviewing as proposed acquisitions for board consideration
- Transitioned to an updated automated continuous forest inventory system
- In addition to all the ongoing duties that shape our day to day work lives

He shared that BCPL was able to close the last phase of the Minocqua Timber land transaction. The exchange with the National Park Trust has been delayed on their end for a couple months but BCPL was able to close on the conveyance of four parcels that will ultimately go to the National Parks Service in return for 228 acres of timberland in Iron County. This transaction is a testament to Micah Zeitler's creativity and his perseverance. Thank you, Micah. The Oneida County part of the larger Minocqua Timber land transaction was the subject of an inquiry from State Senator Tiffany. The Senator cited the fact that the Town of Little Rice adopted "Coordination" resolutions and ordinances in 2010 and asked why BCPL did not comply with such. Executive Secretary German explains that he was aware that "Coordination" resolutions were a subject of serious controversy back then. At the time these resolutions and ordinances were adopted by the Town, former AG JB Van Hollen issued a published AG's opinion that such resolutions and ordinances had no effect. In Executive Secretary German's response to Senator Tiffany, he reaffirmed BCPL's commitment to transparency, stated he was unfamiliar with the specific documents and resolutions the Senator cited but did notify him that he was aware of the previous AG opinion on the topic and let him know that BCPL sought current guidance from DOJ on the matter.

Finally, the US Forest service appraiser kept her word and released the invitation to bid for the appraisals for the proposed land exchange. In the meantime, Micah has been working on the title issues surrounding the transaction. And while the transaction is still a long way from the finish line, this is a good indication that the transaction is progressing towards completion. Executive Secretary German thanked everyone for their hard work.

Board Chair Godlewski inquired about employees working remotely.

Executive Secretary German commented things are going well. BCPL is doing a staff meeting remotely every Tuesday morning at 10am to check in with everyone to see how people are doing personally and professionally. We are keeping the lines of communication open so that if one of us is working on something that touches somebody else that we are

staying abreast of each other. Executive Secretary German adds that he believes things are working pretty well.

Board Chair Godlewski inquired about Senator Tiffany. She asks if there is there anything the Board can or should do to assist in the Senator's inquiry.

Executive Secretary German commented that he has forwarded it to DOJ, the matter was assigned to an Assistant Attorney General and he is awaiting their guidance on the matter. He has provided DOJ with the 2010 AG's opinion along with other materials as well.

Board Chair Godlewski asked that Executive Secretary German keep the Board posted as that situation progresses.

Executive Secretary German agreed that he will.

ITEM 9. BOARD CHAIR'S REPORT

Board Chair Godlewski shared her appreciation by thanking the staff at BCPL, especially Rich, Tom and Denise, for everything they've done this last month. She acknowledges that the staff has been extremely busy and has really stepped up and delivered. She also thanks Doug and Josh for approving the special distribution. She shared that it is very eye opening from her communications with DPI and media specialists how these funds will make a difference across the state and she appreciates the support of the Board.

ITEM 10. FUTURE AGENDA ITEMS

No new future agenda items.

ITEM 10. ADJOURN

Commissioner Kaul moved to adjourn the meeting and added his appreciation of everyone for working on these issues; Commissioner LaFollette seconded Commissioner Kaul's sentiment and the motion. The motion passed 3-0; the meeting adjourned at 2:53 p.m.



Thomas P. German, Executive Secretary

Link to audio recording: <https://bcpl.wisconsin.gov/SharedDocuments/BoardMeetingDocs/2020/2020-04-07-BoardMtgRecording.mp3>

**BOARD MEETING
APRIL 21, 2020**

**AGENDA ITEM 3
APPROVE LOANS**

Municipality	Municipal Type	Loan Type	Loan Amount
1. Onalaska La Crosse County Application #: 02020133 Purpose: Finance capital budget expenditures	City Rate: 2.50% Term: 5 years	General Obligation	\$542,000.00
2. Summit Douglas County Application #: 02020134 Purpose: Finance purchase of dump truck	Town Rate: 2.50% Term: 2 years	General Obligation	\$80,000.00
3. Whitestown Vernon County Application #: 02020135 Purpose: Finance purchase of truck and equipment	Town Rate: 2.75% Term: 7 years	General Obligation	\$108,000.00
4. Gilman Pierce County Application #: 02020136 Purpose: Finance purchase of tractor	Town Rate: 2.50% Term: 2 years	General Obligation	\$33,523.00
5. Roxbury Sanitary District #1 Dane County Application #: 02020137 Purpose: Finance wastewater projects	Sanitary District Rate: 3.50% Term: 20 years	General Obligation	\$700,000.00
6. Roxbury Sanitary District #1 Dane County Application #: 02020138 Purpose: Finance wastewater lateral projects	Sanitary District Rate: 2.50% Term: 5 years	General Obligation	\$300,000.00
7. Fredonia Ozaukee County Application #: 02020139 Purpose: Finance WWTP project	Village Rate: 3.50% Term: 20 years	General Obligation	\$1,549,064.00
8. Dresser Polk County Application #: 02020140 Purpose: Finance water tower project	Village Rate: 3.50% Term: 20 years	General Obligation	\$650,000.00

Municipality	Municipal Type	Loan Type	Loan Amount
9. Mercer Iron County Application #: 02020141 Purpose: Finance purchase of plow truck	Town Rate: 2.75% Term: 10 years	General Obligation	\$161,787.00
TOTAL			\$4,124,374.00

BOARD MEETING

April 21, 2020

AGENDA ITEM 4

PROPOSED AMENDMENT AND RESTATEMENT OF INVESTMENT POLICY STATEMENT

RECITALS

- A. At the November 1, 2016 board meeting, the Commissioners approved adoption of the Investment Policy Statement (IPS) to guide the investment of BCPL-managed trust funds. The IPS was subsequently modified at the August 20, 2019 and December 3, 2019 board meetings.
- B. The BCPL Investment Committee (the “Committee”) has reached consensus on additional changes to such document.
- C. The Committee recommends that the Board now amend and restate the IPS as set forth below.

NOW, THEREFORE BE IT RESOLVED, that the Board of Commissioners of Public Lands hereby amends and restates the Investment Policy Statement as set forth on Attached Exhibit A.

State of Wisconsin
Board of Commissioners of Public Lands

School Trust Fund Investment Guidelines
and
Investment Policy Statements

An Investment Management Framework for State of Wisconsin School Trust Funds, including the Common School Fund, the Normal School Fund, the Agricultural College fund, and the University Fund.

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Appendix 1

CFA Institute Code of Ethics and Standard of Professional Conduct
CFA Institute Asset Manager Code of Conduct

DRAFT

SCHOOL TRUST FUND INVESTMENT GUIDELINES

Mission Statement, Authority, and Purpose

Introduction

The Board of Commissioners of Public Lands (BCPL) is the oldest state agency and the only agency created within the State Constitution. The forefathers of this State placed a high value on public education, and created this agency as an independent board to oversee the valuable federal land grants through a permanent trust created to benefit Wisconsin schoolchildren. Members of the Board have a fiduciary duty and must administer the trust solely in the interests of the beneficiaries.

The Wisconsin constitution includes language forming the BCPL, with membership comprised of three statewide elected constitutional officers: the Secretary of State, State Treasurer, and Attorney General. The BCPL is entrusted with the authority to manage the sale of those lands and resultant monies to benefit the education of current and future generations. It is widely believed that the School Trust Funds remain relevant today because the management of School Trust assets was somewhat protected from the political and budgetary pressures found in the legislative and executive branches of state governance.

The school trust lands and the proceeds from their sale, plus additional monies as directed by the State Constitution, have been placed into four distinct state trust funds (the School Trust Funds): the Common School Fund, Normal School Fund, University Fund, and Agricultural College Fund. The beneficiaries of the Common School Fund are K-12 public schools located in Wisconsin. Earnings from the investment of Common School Fund principal are currently directed to provide the sole state aid for the purchase of public school library media and resources. The University of Wisconsin is the beneficiary of the other three School Trust Funds managed by the BCPL.

Mission Statement

The mission of the BCPL is to manage the assets of the School Trust Funds in a manner that maintains significant, stable, and sustainable distributions to fund beneficiaries, and to manage all assets and programs entrusted to the Board in a prudent and professional manner, in accordance with the Wisconsin Constitution and applicable state law.

General Authority

The Wisconsin Constitution (Article X) entrusts the management and sale of school trust lands and the investment of funds arising therefrom to the BCPL. As most of the school trust lands are remnants of federal land grants, there are some federal statutes that effect such lands and resulting land sale proceeds. Chapter 24 of the Wisconsin Statutes governs school trust lands and trust funds managed by BCPL. Wisconsin Statutes Chapter 112 includes both the Uniform Fiduciaries Act and the Uniform Prudent Management of Institutional Funds Act, which govern the management of the School Trust Funds. Wisconsin Statutes Chapter 701 contains the Wisconsin Trust Code that governs the administration of Trust Funds within the state.

Investment Authority

The Wisconsin Constitution states that “...The Commissioners shall...invest all moneys arising from the sale of such lands ...in such manner as the legislature shall provide...”¹ This provision has been interpreted by the Wisconsin Supreme Court to mean that the State Legislature has the authority to specify the universe of investments available to the BCPL, but may not direct the BCPL to make any particular investment.

Prior to August 2015, the State Legislature limited the investment authority of the BCPL to certain fixed-income securities.

The enactment of Wisconsin Act 60 in August 2015 greatly expanded the investment authority available to the BCPL for management of the School Trust Funds. This statute included language replacing the previous list of authorized investments with the Prudent Investor Standard: “The board shall manage and invest moneys belonging to the trust funds in good faith and with the care an ordinary prudent person in a like position would exercise under similar circumstances, in accordance with the *Uniform Prudent Management of Institutional Funds Act*.”²

Purpose of This Policy

This Investment Policy Statement (Policy) governs the investment of assets for each of the four School Trust Funds of the State of Wisconsin. Prior to the enactment of Act 60, state statutes provided a de facto investment policy for the BCPL. Removal of these constraints allowed the transition of BCPL asset management into industry best practices starting with the creation of this Policy.

This policy is established to provide the framework for management of School Trust Fund assets and sets forth the investment objectives, philosophy, guidelines, and practices for the BCPL, staff, external investment managers (managers), and consultants. The Policy is intended to provide parameters to ensure long-term prudence and care in execution of the investment program, while allowing the flexibility to capture investment opportunities made available to staff and managers. The Policy shall also provide the standards by which the BCPL can evaluate staff, managers, investment consultants, custodians and other service providers.

No investment or action pursuant to an investment may be taken unless permitted by this Policy or by action of the BCPL, and any exceptions to this policy must be approved by the BCPL.

This Policy is supplemented by agency operating procedures and policies, along with language contained within contractual agreements between the BCPL and investment managers and other service providers.

Formal Review Schedule

The BCPL acknowledges that investments are subject to short-term volatility, but that maintaining a long-term outlook will provide better results for the investment of the permanent School Trust Funds. This long-term perspective will constrain impulsive and potentially harmful decision-making in reaction to short

¹ Article X, Section 8 - Wisconsin Constitution

² Chapter 24.61(2)(a) and 112.11(3) - Wisconsin Statutes

term market fluctuations and conditions. In order to preserve this long-term view, the BCPL has adopted the following formal review schedule:

<u>Formal Review Agenda Item</u>	<u>Formal Review Schedule</u>
Investment Guidelines	At least every two years
Investment Policy Statements	At least every two years
Asset Allocation Policy	At least annually
Total Fund Performance	At least quarterly
Asset Class Performance	At least quarterly
Investment Manager Performance	At least quarterly

Description of the School Trust Funds

Common School Fund

The Common School Fund is the largest trust fund managed by BCPL, and was established in the State of Wisconsin Constitution in 1848. This Fund was originally endowed with a federal land grant of the 16th Section of each Wisconsin township (nearly one million acres in total) for the purposes of education. Another grant of 500,000 acres, originally dedicated to 'internal improvements', was added to the Common School Fund due to a successful petition to the United States Congress by the forefathers of this state. Except for about 6,000 acres that remain in trust, all of the school trust lands from these original grants were sold to establish the Fund.

Principal has continued to grow because the Wisconsin Constitution provides that the Fund receive all monies and the clear proceeds of all fines and forfeitures (including unclaimed and escheated property) that accrue to the state.

Common School Fund Earnings are delivered each April (mid fiscal year) to the Department of Public Instruction, which then distributes the earnings as library aid to all public K-12 school districts in the state. These payments are currently directed to provide the sole state aid for the purchase of public school library media and resources. The Wisconsin Constitution provides each school district to receive a share of total distributable earnings based on the number of children aged 4 through 20 living in that district.

As of December 31, 2019, the Common School Fund had total (cost basis) financial assets of \$1.2 billion invested in the following security types:

Common School Fund Assets

Fixed Income		Cost Basis*
Public Debt		
State/State Agency/Municipal Bonds		\$192,702,982
U.S. Treasury/Agency Bonds		14,972,500
U.S. Treasury Inflation Protected Securities		--
Corporate Bonds		29,998,848
Private Debt		
BCPL State Trust Fund Loans		468,680,865
Other Private Debt		24,908,448
Total Fixed Income		\$731,263,643
Equities and Alternatives		
Public Equities		
Domestic Equities		40,967,170
Global Equities		44,006,250
Alternatives		
Private Real Estate		--
Real Assets/Infrastructure		--
Private Equity/Venture Capital		11,863,843
Total Equities and Alternatives		\$96,837,263
Cash		
State Investment Fund	Total Cash	\$330,984,794
TOTAL ASSETS		\$1,159,085,699
*Fund values are marked-to-market at end of each fiscal year.		

Remaining land assets of the Common School Fund total 5,955 acres. The following categories are not mutually exclusive, meaning that a single parcel may be included in more than one category and the sum of acres within each category will not equal total acreage:

Common School Fund Acreage	
Productive Timberland	3,240
Non-Timbered (primarily wetlands)	978
Land with Management Impediments	1,827

The management impediment category includes lands that have no legal access, or where logging is not economically feasible because of low timber value, small tract size or parcel remoteness.

Normal School Fund

At the time of Wisconsin's statehood, there was only one "school fund" established in the state constitution for the support and maintenance of both common (public K-12) and normal schools (teacher colleges). From this single fund, whatever trust assets or income not needed for common schools was to be used for the normal schools. In the early days of statehood, the legislature was primarily concerned with funding of the common schools and allocated few resources to normal schools.

In 1850, Wisconsin received a federal grant of more than three million acres of land pursuant to the Swamp Land Act. The proceeds from the sale of these lands were to be used for the purpose of drainage and reclamation of “swamp and overflowed lands” *to the extent necessary*. By 1865, the Wisconsin legislature was convinced that the State needed only half of those swamp lands for drainage purposes. The other half of the land grant was directed by the Constitution to the school fund. The legislature made the additional finding that the common schools did not need additional funding at that time so these lands and resulting sales proceeds would be used to endow the Normal School Fund. One year later in 1866, Wisconsin established its first Normal School in Platteville.

Nearly all of these original swamp lands were sold in the 1800s. The scattered parcels that remained within the Trust were difficult to sell because the parcels had little monetary value and/or severe management impediments, including the lack of legal access. Many of these impediments continue to affect the marketability of these lands, and the Normal School Fund retains ownership of 71,176 acres today.

Over the years, the normal schools became state teacher colleges and then state universities that were eventually folded into the University of Wisconsin System (UW). The UW, as the successor in interest of the original normal schools, is now the beneficiary of the Normal School Fund. Additions to principal come from the proceeds of timber sales.

Earnings are distributed to the University of Wisconsin throughout each fiscal year, and are currently dedicated to fund scholarships for UW-Madison and UW-Extension students as well as programs at UW-Stevens Point.

As of December 31, 2019, the Normal School Fund had total (cost basis) financial assets of approximately \$27.8 million invested in the following security types:

Normal School Fund Assets

Fixed Income	Cost Basis*
Public Debt	
State/State Agency/Municipal Bonds	5,833,386
U.S. Treasury/Agency Bonds	--
U.S. Treasury Inflation Protected Securities (TIPs)	--
Corporate Bonds	--
Private Debt	
BCPL State Trust Fund Loans	16,637,389
Other Private Debt	--
Total Fixed Income	\$22,470,775
Equities and Alternatives	
Total Equities and Alternatives	--
Cash	
State Investment Fund	\$5,372,420
Timber Sale Deposits	(54,053)
TOTAL ASSETS	\$27,789,141

*Fund values are marked-to-market at end of each fiscal year.

Remaining land assets of the Normal School Fund total 71,176 acres. The following categories are not mutually exclusive, meaning that a single parcel may be included in more than one category and the sum of acres within each category will not equal total acreage:

Normal School Fund Acreage	
Productive Timberland	28,403
Non-Timbered (primarily wetlands)	20,388
Land with Management Impediments	21,698

As with Common School Fund lands, the management impediment category includes parcels with no legal access, or where logging is not economically feasible.

University Fund

In both 1838 and 1854, Congress granted to the Territory of Wisconsin the equivalent of two townships, or 72 square miles of land, to be sold to support a university. Wisconsin sold nearly all these lands shortly after obtaining title, and made no provision for adding to this fund. For many years, the principal balance has remained static and invested only in fixed income securities. Interest earnings are distributed annually to the University of Wisconsin.

As of December 31, 2019, the University Fund had total financial assets of \$234,130 invested as follows:

University Fund Assets

Fixed Income	Cost Basis*
Public Debt	State/State Agency/Municipal Bonds
Private Debt	BCPL State Trust Fund Loans
	Total Fixed Income
Cash	
	State Investment Fund
TOTAL ASSETS	\$234,130

*Fund values are marked-to-market at end of each fiscal year.

Land assets of the University Fund consist of a single remaining parcel of 37 deeded acres. The majority of the parcel is submerged, with the remainder predominantly wetlands.

University Fund Acreage	
Productive Timberland	0
Non-Timbered (primarily wetlands)	37
Land with Management Impediments	37

Agricultural College Fund

The Agricultural College Fund was established with an 1862 act of Congress granting land to create a permanent endowment to support “colleges of agriculture and mechanical arts” in each state. The Morrill Act gave rise to land grant colleges across the nation by providing that each state was entitled to 30,000 acres of land for each member of Congress. Wisconsin had eight Congressional representatives at that time, so received title to 240,000 acres of land under this law. Wisconsin sold all these lands shortly after obtaining title, and made no provision for adding to this fund. The principal balance of the Agricultural College Fund remains fixed at the amount originally received for these lands, and the BCPL makes an annual distribution of earnings to the University of Wisconsin.

As of December 31, 2019, the Agricultural College Fund had total financial assets of \$305,282 invested as follows:

Agricultural Fund Assets

Fixed Income		Cost Basis*
Public Debt	State/State Agency/Municipal Bonds	\$59,047
Private Debt	BCPL State Trust Fund Loans	\$224,645
Total Fixed Income		\$283,692
Cash		
State Investment Fund		\$21,589
TOTAL ASSETS		\$305,282
*Fund values are marked-to-market at end of each fiscal year.		

Roles and Responsibilities

The BCPL

The Board of Commissioners of Public Lands is the primary body charged with overseeing investment activities relating to the Funds. The three elected members of the BCPL include the Secretary of State, State Treasurer, and State Attorney General. Commissioners are fiduciaries subject to certain statutory and common law duties and standards, and must administer the trust solely in the interests of the beneficiaries.

The BCPL is responsible for the prudent investment of all assets and programs entrusted to the Board, in accordance with the Wisconsin Constitution and applicable federal and state laws. The BCPL is responsible for establishing and maintaining all policies and guidelines by which the Funds are managed, and by which the Executive Secretary and Investment Committee operate. The BCPL relies on the Executive Secretary, Investment Committee, agency staff, and managers to properly administer the Funds and implement strategies for the investment of Trust assets.

Board Chair

The members of the BCPL are responsible to elect one member as Board Chair. The Board Chair facilitates meetings and works collaboratively with the Executive Secretary to set goals and objectives for the agency.

Executive Secretary and Agency Staff

The Board of Commissioners of Public Lands appoints an Executive Secretary to act on its behalf. The Executive Secretary has a primary responsibility to manage the school trust funds and assets under the control of the BCPL as provided by law. In addition to the Executive Secretary, agency staff includes the Deputy Secretary/Legal Counsel, Chief Investment Officer, Forest Supervisor, Senior Accountant/Financial Manager, and five fulltime staff.

Investment Committee

The Board of Commissioners of Public Lands hereby appoints as voting members to the BCPL Investment Committee: the Board Chair (or Board Member designated by the Board Chair), Executive Secretary, Deputy Secretary/Legal Counsel, and the Chief Investment Officer. The Senior Accountant/Financial Manager shall also attend and contribute to all Investment Committee meetings. The Committee shall elect one member as Chair, who is responsible for creating the meeting calendar and agendas and facilitating meetings of the Committee.

The Investment Committee has the responsibility for implementing BCPL policy, selecting the custodian bank, choosing investment managers and commitment amounts, setting interest rates and other loan terms available through the BCPL State Trust Fund Loan program, and reporting to the BCPL regarding the performance of investment portfolios. Members of the committee may propose and advocate for any investment that falls within the Investment Policy Statement and Asset Allocation of any managed fund. All investments, along with any delegation of authority to invest on behalf of the BCPL, shall be made only following a majority affirmative vote of all Investment Committee members.

The Investment Committee shall determine and delegate all appropriate and necessary authorities to the Chief Investment Officer for executing approved investments in publicly traded securities.

Commitments to external managers for executing an investment strategy including only publicly-traded securities shall require a majority affirmative vote of all Investment Committee members.

Commitments to external investment managers for the management of investments that are not publicly traded shall require a majority affirmative vote of all Investment Committee members. In addition, unless a determination is made by the Investment Committee that a third party due diligence report is not required in any particular circumstance, these types of investments shall be made contingent on a due diligence report that is approved by the Investment Committee.

Investment Managers

Managers may be hired to provide specialized asset management capabilities, and will serve at the pleasure of the BCPL. Each manager will select, buy, and sell specific securities or investments within the parameters specified in their investment guidelines and in adherence to this Policy. Managers will construct and manage investment portfolios that are consistent with the investment philosophy and disciplines for which they were hired. Managers will provide performance reporting at intervals and in a format specified by the BCPL Investment Committee.

Custodian

A custodian bank shall be selected to safeguard Trust Fund financial assets. The custodian is responsible for collecting income and safely keeping all cash and securities, processing transactions, and providing accounting and investment reports to the Agency.

Conflicts of Interest

Commissioners, the Executive Secretary, Members of the Investment Committee, Managers, Consultants, and Custodians involved in the investment process will refrain from personal business activity that could conflict with the proper execution and management of investments within BCPL-managed trust funds, or that could impair their ability to make impartial recommendations and decisions. Potential conflicts of interest, or anything that might create an appearance of a conflict of interest, must be disclosed in writing to the Executive Secretary. Commissioners shall submit an Annual Statement of Economic Interest to the appropriate State of Wisconsin authorities and members of the Investment Committee are encouraged to do the same.

Adherence to CFA Institute Code of Ethics and Standards of Professional Conduct

The CFA Institute Code of Ethics and Standards of Professional Conduct and Asset Manager Code of Conduct comprise the current industry standards and best practices for the conduct of fiduciaries. These documents are attached as Addendum 1 to this policy. This investment policy hereby requires Commissioners, the Executive Secretary, and all Agency Staff to adhere to these standards.

Investment Philosophy

The Investment Philosophy captures investment and asset management principles that shall guide the BCPL in performing its fiduciary and statutory obligations. The following principles have been adopted to meet the investment objectives of the BCPL:

1. Asset Allocation

- a. Strategic asset allocation is a fiduciary duty and allocation across asset classes is the most important determinant of long-term total return and return variability.
- b. Each trust or fund invested by the BCPL shall have a strategic asset allocation and investment strategy that is appropriate given its specific requirements for return, risk, time horizon, and liquidity.
- c. Capital markets exhibit periodic inefficiencies that may be exploited through shorter-term tactical shifts in asset allocations to increase expected investment performance. The amount of any tactical allocation shall be limited to ranges specified within the approved asset allocation.

2. Diversification

- a. Diversification by asset class and within asset classes is a primary risk control element.
- b. The transition from the legacy portfolios of fixed-income securities to new asset classes and allocations will require special considerations to meeting the expectations of beneficiaries, including the maintenance and stability of annual income distributions. The establishment of targeted annual distributions coupled with segregated smoothing accounts is required to ensure the stability of future distributions.
- c. Prior to the implementation of this policy, the growth in fund principal had declined to levels near the long-term expected rate of inflation. To maintain purchasing power for future generations, capital gains on investments held one year and longer shall be added to the principal of each School Trust Fund. Interest income, dividends, and short-term capital gains shall be distributed to beneficiaries as required by law and precedence.

3. Fund Management and Transparency

- a. The cost of investment management is an important element of long-term investment returns, and costs are contained through lower-cost internal management, passive management approaches, external fee negotiations, and a focus on net performance.
- b. Over the long term, active management can add value at the asset class, sector, and security levels by exploiting market inefficiencies and their resulting valuation opportunities. Less efficient asset types and markets provide the best opportunities for active management.
- c. Management compensation shall be assessed and monitored so that the goals and interests of investment managers are properly aligned with those of fund beneficiaries.
- d. Fund and portfolio results are most appropriately measured against appropriate benchmarks. Evaluation of investment results should include analysis of both risk and return relative to the objectives and constraints of the managed funds. Peer comparisons are problematic due to differences in the objectives and constraints between the peer funds.

- e. Transparency of investment strategy and processes is an important element in maintaining the confidence and trust of beneficiaries and the public. The BCPL shall strive to provide transparency whenever possible.

4. History and Legacy

- a. Legacy land assets shall be managed to increase the quality and value of land holdings where possible, generate long-term capital gains through timber harvests utilizing industry-best sustainable timber management standards, and improve management efficiencies through the rearrangement of land assets into larger blocks with the sale of excess parcels.
- b. The BCPL State Trust Fund Loan Program, a direct lending program to Wisconsin municipalities and school districts since 1871, provides an important strategic advantage to BCPL asset management with superior risk and return characteristics.
- c. BCPL shall make reasonable efforts to seek investment opportunities within the State of Wisconsin to the extent practicable and subject to the fiduciary duty to act in the sole interests of the beneficiaries.

General Risk Objectives

The investment risk objective for the School Trust Funds is based on the following principles:

- An increase in risk shall be compensated through higher expected long-term portfolio returns.
- Risk can be mitigated through diversification of asset classes and investment approaches. Diversification takes advantage of the different responses to market, economic, and political conditions inherent within distinct asset classes. Diversification also limits portfolio exposure to individual sources of risk and reduces the variability of portfolio returns.
- The primary determinant of long-term investment performance is the strategic asset allocation.
- Capital markets exhibit periodic inefficiencies that may be exploited through shorter-term tactical shifts in asset allocations to increase expected investment performance. The amount of any tactical allocation shall be limited to ranges specified within the approved asset allocation.
- BCPL manages permanent trust funds with an extremely long investment time horizon, which increases the importance to understand and evaluate risks from environmental, social and governance factors.

The BCPL shall establish a long-term asset allocation policy for each fund that balances the return objective with the risk level that is appropriate for that fund. These policies provide for the appropriate level of diversification and allow for tactical allocations designed to take advantage of market inefficiencies. In determining the suitable risk levels, the BCPL has considered the purpose and characteristic of each fund; sources, amounts and timing of anticipated additions to fund principal; constitutional and statutory fund distribution requirements to beneficiaries; liquidity requirements; and general economic conditions.

General Constraints

Wisconsin Constitution

The Wisconsin Constitution requires that all Common School Fund and Normal School Fund income is distributed to beneficiaries, with principal balances to be maintained within the fund. Most other endowments distribute both interest and principal to meet the needs of beneficiaries, and pay out a fixed percentage of the beginning principal balance regardless of investment results. The inability of BCPL to distribute fund principal is critical to asset management policy, and requires that assets are managed differently than the peer group of endowments.

Beneficiary Dependence on Annual Distributions

Earnings from investment of the Common School Fund currently provide the sole state aid for the purchase of public school library media and resources. This dependence on the annual distribution has a significant impact on the management of the trust funds by reducing the acceptable amount of risk applicable to distributable income.

Earnings from investment of the Normal School Fund are distributed to the University of Wisconsin and are currently dedicated to fund scholarships for UW-Madison and UW-Extension students as well as programs at UW-Stevens Point. While this annual distribution is a small percentage of the total budget of the University, these monies remain an important source of funding for these scholarships and academic programs.

The Prudent Investor Standard

Wisconsin Statutes Section 112.11 requires the BCPL to manage and invest moneys in accordance with the *Uniform Prudent Management of Institutional Funds Act*, which states:

112.11 (3) STANDARD OF CONDUCT IN MANAGING AND INVESTING AN INSTITUTIONAL FUND

- (A) Subject to the intent of a donor expressed in a gift instrument, an institution, in managing and investing an institutional fund, shall consider the charitable purposes of the institution and the purposes of the institutional fund.
- (B) In addition to complying with the duty of loyalty imposed by law other than this section, each person responsible for managing and investing an institutional fund shall manage and invest the fund in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.
- (C) In managing and investing an institutional fund, an institution:
 - 1. May incur only costs that are appropriate and reasonable in relation to the assets, the purposes of the institution, and the skills available to the institution.
 - 2. Shall make a reasonable effort to verify facts relevant to the management and investment of the fund.
- (D) An institution may pool 2 or more institutional funds for purposes of management and investment.
- (E) Except as otherwise provided by a gift instrument, the following rules apply:
 - 1. In managing and investing an institutional fund, the following factors, if relevant, shall be considered:
 - a. General economic conditions.

- b. The possible effect of inflation or deflation.
 - c. The expected tax consequences, if any, of investment decisions or strategies.
 - d. The role that each investment or course of action plays within the overall investment portfolio of the fund.
 - e. The expected total return from income and the appreciation of investments.
 - f. Other resources of the institution.
 - g. The needs of the institution and the fund to make distributions and to preserve capital.
 - h. An asset's special relationship or special value, if any, to the charitable purposes of the institution.
2. Management and investment decisions about an individual asset shall not be made in isolation but rather in the context of the institutional fund's portfolio of investments as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the fund and to the institution.
 3. Except as otherwise provided by law other than this section, an institution may invest in any kind of property or type of investment consistent with this section.
 4. An institution shall diversify the investments of an institutional fund unless the institution reasonably determines that, because of special circumstances, the purposes of the fund are better served without diversification.
 5. Within a reasonable time after receiving property, an institution shall make and carry out decisions concerning the retention or disposition of the property or to rebalance a portfolio, in order to bring the institutional fund into compliance with the purposes, terms, and distribution requirements of the institution as necessary to meet other circumstances of the institution and the requirements of this section.
 6. A person that has special skills or expertise, or is selected in reliance upon the person's representation that the person has special skills or expertise, has a duty to use those skills or that expertise in managing and investing institutional funds.

State Statutes

The BCPL is a state agency with an operating budget that requires legislative approval. Historically funded through program revenues (investment earnings), beginning in FY2020 BCPL expenses are funded through State of Wisconsin General Purpose (Tax) Revenues.

The State Legislature also has the authority to specify the universe of investments available to the BCPL, although it may not direct the BCPL to make any particular investment. Statutes also provide the authority and general terms of the BCPL State Trust Fund Loan Program. While the School Trust Funds are protected within the State Constitution, the state legislature is a political body that controls the future course of agency policies and procedures.

The funds managed by the BCPL have been determined by the Supreme Court of the State of Wisconsin to be Trust Funds. Wisconsin Statutes Chapter 701 governs the administration of Trust Funds within the state. Wisconsin Statutes Section 701.0802(1) (Duty to Loyalty) specifies in that "A trustee shall administer the trust solely in the interests of the beneficiaries".

General Investment Guidelines and Restrictions

1. All investments made shall be subject to the quality and diversification restrictions established by the Prudent Investor Standard.
2. Assets may be held in commingled funds and/or privately managed separate accounts. Exposure through commingled funds, ETFs, and mutual funds shall be evaluated on a case-specific basis through analysis of the prospectus or offering document.
3. No more than 5% of the stock of any corporation may be owned by any School Trust Fund.
4. With the exception of debt instruments issued by the State of Wisconsin and the United States of America (including various agencies and government-sponsored enterprises including the Federal Farm Credit System), investments representing the debt or equity of any one company, institution, or real estate project shall not exceed 5% of the market value of any School Trust Fund.
5. Cash management will be controlled on a portfolio-wide basis, and managers are expected to remain fully invested in the types of securities for which they have responsibility, unless otherwise authorized.
6. The utilization of leverage is permitted in accordance with industry and market standards for permitted investments under this policy. Any use of leverage will be consistent with the strategy for which the BCPL hired the manager and controlled by the specific guidelines for that manager. BCPL may not borrow money without board authorization.
7. The BCPL recognizes that the Funds are exposed to currency risk through international equity, fixed income, and absolute return allocations. The BCPL prefers to utilize unhedged benchmarks and does not require managers to hedge the currency exposure in their portfolios.

Permitted Investments and Investment Strategies

The BCPL may invest in the following securities and investment activities as long as such investments comply with the Prudent Investor Standard. Unless otherwise prohibited by law, the investment may be acquired directly or through an investment vehicle including, but not limited to, exchange-traded-funds, mutual funds, limited partnerships, limited liability companies, trusts, or separately managed accounts.

Fixed Income

Public Debt

1. Bonds, notes or other obligations of the United States government, its agencies, government-sponsored enterprises, corporations, or instrumentalities for which the credit of the United States government is pledged for the payment of the principal and interest.
2. Bonds, notes or other obligations issued by any state, its agencies, municipalities, school districts, or other political subdivisions.
3. Bonds, notes, commercial paper or other obligations of any corporation organized and operating within the United States or within countries that comprise the Morgan Stanley Capital International All Countries World Index or other countries specifically permitted by the BCPL Investment Committee.
4. Debt obligations of non-U.S. governmental or quasi-governmental entities that may be denominated in foreign currencies.
5. Collateralized debt securities, including asset-backed and mortgage-backed securities that have an investment grade rating or have been specifically permitted by the BCPL Investment Committee.

Private Debt

1. Direct loans made to Wisconsin Municipalities and School Districts made through the BCPL State Trust Fund Loan Program.
2. Direct investment in any of the security types or issuers allowed under Public Debt, but with securities that are privately negotiated.
3. Funds consisting of commingled limited partnerships, trusts or other vehicles that invest either domestically or internationally in direct loans to corporations, bank loans, commercial or residential real estate mortgage loans, distressed debt or mezzanine debt issues.

Equities and Alternatives

Public Equities

1. Domestic Equities including investments in common or preferred corporate stocks and investment trusts domiciled in the U.S. and listed on the NYSE, AMEX or the NASDAQ exchanges or the ADRs of foreign stocks traded on these exchanges.
2. Global Equities including investments in common or preferred stocks of corporations domiciled in countries that comprise the Morgan Stanley Capital International All Countries World Index or other countries specifically permitted by the BCPL Investment Committee. External asset managers may execute foreign exchange contracts and invest in local country cash equivalents issued under the laws of permitted foreign countries and as permitted under the terms of their agreement with BCPL.

Alternatives

1. Private Real Estate including direct investment in real estate (subject to statutory limitations), in addition to investments in commingled limited partnerships, trusts or other vehicles that invest either domestically or internationally in the debt or equity of underlying real estate properties, portfolios of properties or operating companies within the real estate industry.
2. Real Assets/Infrastructure Funds consisting of commingled limited partnerships, trusts or other vehicles that invest either domestically or internationally in infrastructure, transportation, communication, water and wastewater, timber, commodities, and energy systems or properties.
3. Private Equity/Venture Capital Funds consisting of commingled limited partnerships, trusts or other vehicles that invest either domestically or internationally in corporate buyout, venture capital and special situation funds.

Cash

The BCPL will maintain cash positions in amounts necessary for liquidity, distributions to beneficiaries, and ongoing investment activities including risk reduction when appropriate.

1. State Investment Fund, which is managed by the State of Wisconsin Investment Board to provide next day liquidity and safety for funds held by the State, Wisconsin municipalities, and others.
2. Bond Anticipation Notes, Note Anticipation Notes, and Tax Revenue Anticipation Notes issued by Wisconsin School Districts and Municipalities.
3. Deposit Accounts and Certificates of Deposit with banks incorporated within the United States.
4. Money market accounts issued by an investment bank domiciled in the United States.

Return Objectives, Smoothing Accounts and Annual Distributions

The mission of the BCPL is to maintain significant, stable, and sustainable distributions to fund beneficiaries. Sustainability in this context means that BCPL will take a multi-generational approach to management of School Trust Fund assets, and will be accountable to both current and future beneficiaries.

The return objective of the BCPL will be to achieve the highest level of long-term investment returns compatible with the risk tolerance of the fund and prudent investment practices. At a minimum, the objective is to generate returns that allow the average annual income distribution provided to beneficiaries to increase at a rate equal to or above the appropriate long-term rate of inflation.

Establishment of Smoothing Accounts for the Common School Fund and Normal School Fund

Beneficiaries of the Common School Fund and the Normal School Fund are dependent on the distribution of Trust Fund income to fund operations. This is less true for the University Fund and Agricultural College Fund, whose beneficiary is the general fund of the University of Wisconsin (UW) and annual distributions of trust fund income are currently a very small portion of the UW budget.

For the Common School Fund and the Normal School Fund, the transition from a portfolio consisting solely of fixed income securities to an asset allocation model that increases expected investment returns will impact both the volatility of annual returns and funds available for distribution. The importance of stable annual distributions to the beneficiaries in this new environment of higher volatility necessitates the establishment of targeted annual distributions with associated smoothing accounts.

Amount and Funding of Smoothing Accounts

Segregated smoothing accounts have been established for both the Common School Fund and Normal School Fund from net investment income earned above the targeted annual distribution. The State Constitution does not allow the distribution of fund principal, making it necessary to establish these segregated smoothing accounts *from earnings*. The smoothing funds will be used to supplement the annual distribution to beneficiaries during years when distributable income does not meet the targeted annual distribution.

The market conditions that might cause a decline in distributable earnings could persist for several years, and the smoothing accounts must be sized to supplement distributions during this entire period. A prudent minimum amount to be maintained within the Common School Fund and Normal School Fund smoothing accounts is hereby established at 50% of the next targeted annual distribution at the end of each fiscal year.

The BCPL Investment Committee has the authority to increase the minimum amount to be held in the smoothing fund to a maximum 100% of the next targeted distribution amount. This action shall require the Investment Committee to make a determination that the increase is in the long-term best interest of beneficiaries.

Annual Distributions

The targeted annual targeted distribution will be the average annual net investment income earned over the prior five fiscal years (e.g. the distribution to be made in April 2020 is the average annual net investment income earned during the five years ending June 30, 2019). Net investment income is hereby defined as total interest, dividends and short-term capital gains less all costs incurred by BCPL in the management of the trust funds.

The following process shall determine the flow of net investment income during each fiscal year:

1. On October 1 of each fiscal year, the BCPL Senior Accountant/Financial Manager shall determine the following:
 - a. The targeted distributions for the current fiscal year for both the Common School Fund and Normal School Fund, calculated as average annual net investment income earned by each fund during the five years ending on the preceding June 30.
 - b. The minimum amount of each smoothing fund, calculated at 50% of the targeted distributions as defined above.
 - c. The current amount of each smoothing fund, defined as that fund's portion of Fund 763 appropriation 902 on the preceding June 30.
2. If the current amount of the smoothing fund is greater than the minimum amount of the smoothing fund, the Investment Committee may determine to add all or a portion of that difference to the targeted distribution for the current fiscal year.
3. Net investment income beginning on July 1 will be allocated in the following order:
 - a. Smoothing fund in amounts necessary to increase the current amount to the minimum amount;
 - b. Targeted distribution for the following April;
 - c. Smoothing fund.
4. If the net investment income available at the time of distribution is less than the targeted distribution, a transfer from the appropriate smoothing fund will supplement net investment income so that the amount of the fiscal year distribution is equal to the targeted distribution.

Additions to Fund Principal

Constitutional Additions to the Common School Fund

Article X, Section 2 of the State Constitution requires that:

“The proceeds of all lands that have been or hereafter may be granted by the United States to this state for educational purposes... and all moneys and the clear proceeds of all property that may accrue to the state by forfeiture or escheat; and the clear proceeds of all fines...for any breach of the penal laws, and all moneys arising from any grant to the state where the purposes of such grant are not specified... shall be set apart as a separate fund to be called "the school fund" ...⁴

As mentioned earlier, the Common School Fund was originally established with federal land grants totaling about 1.5 million acres. The fund has stayed relevant since statehood because the proceeds from the original land sales have been supplemented through the above constitutional provision. However, the

increase in the number of municipal courts, improved systems for returning unclaimed property, and changes in the state regulatory environment have combined to slow down the growth of fund principal in recent years.

This trend magnifies the importance that all sources of fines and forfeitures that accrue to the state are secured for the Common School Fund, as directed in the constitution. An important element of the fiduciary duty of the BCPL is that all reasonable measures are taken to ensure that funds that legally belong to the Common School Fund are so deposited, and that the BCPL challenges any diversion of such funds to the fullest extent possible.

Long-Term Capital Gains

Long-term capital gains (gains and losses on the sale of assets held one year or longer) shall be retained and added to the principal of each School Trust Fund at the time earned.

This policy continues a BCPL accounting standard that dates from the mid-1800s. In early BCPL history, BCPL-managed lands included both agricultural and timberland parcels. BCPL categorized the sale proceeds from seasonal crops (mostly hay) as income to be distributed to Trust Fund beneficiaries. However, the proceeds from timber sales were added to Trust Fund principal. These distinct treatments make sense in that the harvesting of seasonal crops does not normally deplete the value of a land asset, while timber harvests can have a significant and detrimental impact on land values. This principle is consistent with accounting standards for short-term and long-term capital gains. Short-term capital gains are generally treated like annual interest income, with no impact on the inherent value of the asset. Long-term capital gains are added to trust principal, because the distribution these gains could diminish the value of trust assets for future beneficiaries

Unique Elements of BCPL-Managed Funds

BCPL State Trust Fund Loan Program

Since first authorized by the State of Wisconsin legislature in 1871, the primary investment vehicle for the BCPL has historically been the State Trust Fund Loan Program, a direct lending program to Wisconsin municipalities and school districts. This program has provided funding for countless public projects throughout the state, and continues to be a major source of funding for economic development, local infrastructure, school improvements, and the purchase of vehicles and capital equipment. This program is highly valued by municipalities and school districts because there are no fees, the simplified borrowing process requires no third-party assistance, loan terms are flexible including prepayment without penalty, and interest paid is returned to communities across Wisconsin as public school library aid.

In addition to providing an important source of funding to Wisconsin communities, the loan program originates investment assets with very low default risk. In fact, there has not been a single loan default in the 149-year history of the program. One major reason for this success is that Wisconsin statutes require the BCPL to intercept state aid upon a borrower loan default. State funding of local expenditures is a major source of revenues for individual municipalities and school districts in Wisconsin, and this potential intercept provides a significant incentive for borrowers to stay current on BCPL loan payments.

The state aid intercept allows the BCPL to make loans to communities with lower credit ratings and expect full repayment of principal and interest when due. Trust Fund beneficiaries gain from expansion of the program to all communities within the state, without the additional costs and complexity that would be required with a full underwriting of borrower credit quality. Value is created because the statutory intercept provisions increase the potential credit rating on any loan to the State of Wisconsin equivalent of Aa1/AA+ regardless of the underlying credit quality of the borrower.

An analysis comparing the yields generated by the BCPL loan portfolio to corporate bonds indicates that the Trust Fund Loan Program generates excess returns, providing a substantial advantage to Trust Fund beneficiaries.³ Program yields are higher than would be expected in the open market for the level of underlying default risk. These excess returns provide an opportunity for BCPL to explore the possibility of creating an on-going source of capital gains and/or servicing income by selling loans on the secondary market. The creation of a pipeline for selling loans might also provide the BCPL with additional flexibility in the management of Trust assets. For example, if the total amount of outstanding loans exceeds the target allocation for that asset class, BCPL could sell excess loans rather than take actions designed to reduce loan demand.

Land Assets

The BCPL has managed State of Wisconsin School Trust Lands since statehood in 1848. Originally granted to Wisconsin from the Federal Government, School Trust Lands eventually totaled almost 4 million acres with the vast majority sold during the 1800s. The BCPL continues to manage approximately 77,000 acres that are concentrated within a nine county consolidation zone in North Central Wisconsin. About 6,000 acres are held in the Common School Fund, with 71,000 acres in the Normal School Fund.

Land assets play an important role in strategic asset allocation by providing diversification and inflation protection to the Trust Fund portfolios. At some point in the future, BCPL may want to reconsider the current asset allocation to timberland, but it is in the best interest of Trust Fund beneficiaries to take reasonable steps in maximizing the value of BCPL-managed land assets prior to any land sales.

Article X, Section 7 of the State Constitution created the BCPL to sell the lands granted to Wisconsin by the Federal Government and invest the proceeds within a trust to benefit public schools. Section 8 requires that these lands be appraised before sale, and allows the Board to withhold land from sale “when they shall deem it expedient.” Section 8 also provides that funds shall be invested “in such manner as the legislature shall provide”.

In 2006, the Wisconsin Legislature unanimously approved legislation with the moniker of “Land Bank Authority”, which provided limited authority to the BCPL to purchase replacement land assets. This law authorized BCPL to use the proceeds from the sale of School Trust Land sales solely for the purchase of replacement school trust lands when the BCPL determined that the purchase would improve timberland management, address forest fragmentation, or increase public access. The legislation capped the total acreage owned within the combined School Trust Funds, but allowed the BCPL to rearrange holdings into

³BCPL Board Meeting Agenda and Minutes - January 19, 2016. Item 5, Pages 2-3. “Analysis of Trust Fund Loan Program Yields”

more productive, accessible, and larger tracts that could be managed more efficiently. The law recognized the importance of maintaining land as an asset within the Trust Fund portfolios while also providing a mechanism to improve underperforming parcels.

Since that time, the BCPL has sold about 15,075 acres and purchased about 14,660 acres of replacement School Trust Lands. During the same period, BCPL has also exchanged a significant amount of land (1403 acres in and 2065 acres out). These replacement lands have improved the quality and value of the land portfolio by:

- Providing access to over 7,302 acres of previously landlocked parcels;
- Increasing timber revenues as newly acquired lands contain more upland acreage and timber; and
- Improving management efficiencies and economies of scale through blocking and creation of larger tracts.

Moving forward, the goal of BCPL land management is to accelerate the consolidation of remaining School Trust Lands into productive tracts of timberland. All parcels will be identified either for retention in the BCPL-managed portfolio or as excess land. Reasonable efforts will be taken to improve the marketability of excess lands that have curable defects or impediments to value. The sale of any parcel will be completed in a manner that maximizes the net present value of sale proceeds. Consolidation of land assets has been a goal of the BCPL for many years, and continued progress will require the dedication of agency resources and the availability of Land Bank Authority and other tools.

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State of Wisconsin School Trust Fund Investment Policy Statements

Common School Fund
Normal School Fund
University Fund
Agricultural College Fund

Common School Fund

Investment Policy Statement

Fund Purpose

The Common School Fund is a permanent trust fund established in 1848 within the State Constitution for the purpose of education. The beneficiaries consist of all K-12 public school districts located in Wisconsin, and earnings from investment of the Common School Fund are currently directed to provide the sole state aid for the purchase of public school library media and resources.

Funding Sources

This Fund was originally established with federal land grants totaling about 1.5 million acres. Except for about 6,000 acres that remain in trust, all lands from these original grants were sold to establish the Fund.

Principal has continued to grow because the State Constitution provides that the Common School Fund receive all monies and the clear proceeds of all fines and forfeitures (including unclaimed and escheated property) that accrue to the state.

Capital gains on investments held one year and longer are added to the principal of the Fund.

Distribution Policy

Interest income, dividends, and short-term capital gains are distributed to beneficiaries in accordance with the State Constitution and agency policy. Distributions shall adhere to the policy described in detail on page 19, with the targeted distribution at the 5-year moving average of fund net annual earnings during the prior five fiscal years.

A smoothing account shall be established from withheld earnings, with the minimum dollar amount to be determined on October 1st of each year at 50% of the next targeted distribution amount. The smoothing account shall be used to supplement the distribution during years when interest, dividends and short-term capital gains earned during the current fiscal year are lower than the targeted distribution.

The BCPL Investment Committee has the authority to increase the minimum amount to be held in the smoothing fund to a maximum 100% of the next targeted distribution amount. This action shall require a determination by the Investment Committee that the increase is in the long-term best interest of beneficiaries.

Investment Objective

The annual return objective will be to maximize expected earnings within acceptable risk parameters. The long-term goal is to increase fund principal and annual distributions at or above the appropriate long-term rate of inflation.

There are many measures of inflation published by the U.S. Bureau of Labor Statistics, but the appropriate measure of inflation that is most strongly related to the use of funds is CPI - Educational Books and

Supplies. First published by the U.S. Bureau of Labor Statistics in 1967, this index has grown at an average annual rate of 6.0% and has remained significantly higher than the overall inflation rate since inception:

Average Annual Rate of Inflation

	CPI Educational Books and Supplies	CPI	Common School Fund Avg Annual Fund Growth
1967-2019	6.0%	4.0%	7.2%
2000-2019	5.0%	2.1%	5.2%
2010-2019	3.6%	1.7%	3.7%

The Federal Reserve has been quite effective in maintaining inflation rates below their target of 2% since the early 1980s, and there is no reason to predict that effectiveness will change. There is also sufficient data that inflation within the subcategory of Educational Books and Supplies will continue to outpace general CPI moving forward. A prudent assumption for this policy is that long-term inflation in Educational Books and Supplies will average 4.0%.

The growth of Trust Fund principal at or above the long-term rate of inflation is required for equitable treatment of future generations. For the Common School Fund, this growth has historically come from fines, forfeitures and escheats that accrue to the State of Wisconsin

As shown above, the growth in Common School Fund principal has remained at or slightly above the appropriate rate of inflation over the past several decades. For two reasons, this fact is not likely to continue if fund growth is limited to the historic sources of fines, forfeitures and escheats. First, there are political and economic pressures on amounts contributed to the Common School Fund from these historic sources. Second, there is a natural difficulty in maintaining growth rates as any fund or other enterprise gets larger. Because historic sources of principal growth will not increase fund principal at or above the rate of inflation into the future, it will be necessary to rely on for fund investments to contribute to that growth rate with the addition of long-term capital gains.

A prudent assumption may be that financial assets need to contribute 1-2% of annual growth, and this requirement will likely grow over time. Sustaining this level of fund growth while producing the stable income stream necessary to fund beneficiary distributions will require a significant shift to asset classes able to generate long-term capital gains to supplement fund growth.

Portfolio Constraints

Wisconsin Constitution

The Wisconsin Constitution requires that all Common School Fund income is distributed to beneficiaries, with principal balances maintained within the fund. Most other endowments distribute both interest and principal to meet the needs of beneficiaries, and pay out a fixed percentage of the beginning principal balance regardless of investment results. The inability to distribute Common School Fund principal is critical to asset management policy, and requires that Common School Fund assets are managed differently than the peer group of endowments. The ability of the smoothing account to stabilize future distributable

income supports diversification into non-income-producing assets, but the extent of that diversification is limited when compared to endowments able to distribute fund principal.

Beneficiary Dependence on Annual Distributions

Earnings from investment of the Common School Fund are currently directed to provide the sole state aid for the purchase of public school library media and resources. This dependence has a significant impact on the management of the trust funds by reducing the acceptable amount of risk applicable to distributable income. The smoothing account mitigates, but does not eliminate, the impact of beneficiary dependence on investment management.

Liquidity

The BCPL State Trust Fund Loan Program provides excess investment returns for Trust Fund beneficiaries, and one goal of this policy is to provide sufficient liquidity to fund expected near-term loan demand . Annual loan disbursements for the past decade have averaged \$130 million, but required liquidity varies with market conditions including macro and seasonal loan demand. It is anticipated that future liquidity requirements for the loan program can be met thorough liquidity management and the sale of investments.

Legacy Assets and Investment Policy Transition

The Common School Fund must transition from the fixed-income portfolio mandated by prior statute to a diversified portfolio required by the recent implementation of the Prudent Investor Standard. The goal of this new policy will be to provide stable distributions in addition to capital gains that increase fund principal at or above the rate of inflation. The allocation to new asset classes will be systematic and determined by the confidence level in maintaining targeted distribution amounts to beneficiaries. In addition, the entry point into new asset classes must consider current available valuations within a historic context, with the timing of additional diversification benefits secondary to relative values. In addition, initial allocations within asset classes are likely to be tilted towards assets that produce distributable income.

Strategic Asset Allocation

The Common School Fund is a permanent endowment for education and therefore similar to endowments that have been established for institutions of higher learning throughout the United States. This peer group of College and University Endowments generally utilizes the common method of distributing a fixed percentage of both principal and interest each year regardless of investment results. Because constitutional constraints prevent the Common School Fund from distributing principal, the asset allocation of these endowments is considered useful only for long-range planning purposes. The immediate adoption of the full peer group allocation model would increase portfolio risks and reduce income available for distribution to unacceptable levels. This peer group, narrowed by size to include seventy-seven U.S. College and University Endowments with assets between \$500 million and \$1 billion, had an average asset allocation during 2018 as shown below:

Asset Class	2018 NACUBO Allocation*
Fixed Income	10%
Domestic Equities	22%
International Equities	22%
Real Estate	3%
Private Equity	8%
Venture Capital	3%
Other Alternative Strategies**	27%
Cash	5%

* 2018 NACUBO-Commonfund Study of Endowments with total assets from \$501 million to \$1 billion. Full study is available from the National Association of College and University Business Officers.

** Other alternative strategies include hedge funds, absolute return, market neutral, long/short, 130/30, event-driven, derivatives, energy and natural resources, commodities, managed futures, and distressed debt.

BCPL has several strategic advantages available for asset management, and Common School Fund asset allocations should be designed to maximize the impact of these strengths, which include:

- The BCPL State Trust Fund Loan Program;
- BCPL staff, which provides low-cost in-house expertise in the Wisconsin credit markets, fixed-income investing, real estate and forestry;
- Strong institutional and professional relationships with other state agencies and staff, including the State of Wisconsin Investment Board (SWIB); and
- Strong institutional and professional relationships with the University of Wisconsin and the Wisconsin Alumni Research Foundation (WARF) and staff.

Examples of capitalizing on these strengths include the collaboration between BCPL and experts from the UW-Madison School of Business to develop the initial target asset allocation in 2016, along with BCPL discussions with SWIB and WARF staff regarding commitments to Wisconsin-based venture capital funds.

Recognizing that a long-term target allocation utilizing new asset classes can take years to implement prudently, the Board delegates implementation of the strategic asset allocation policy to the BCPL Investment Committee including interim funding levels of asset classes and the setting of interim asset allocation targets and benchmarks. The Strategic Asset Allocation is reviewed at least annually by the Investment Committee, with recommended changes to be approved by the Board.

Based on the objective to contribute long-term capital gains to principal, along with long-term return expectations and risk tolerance, the BCPL has chosen the following strategic asset allocation policy for the Common School Fund:

Common School Fund Target Asset Allocation

Asset Class	Target Allocation	Range	Current Allocation 12/31/2019
Fixed Income	55%		62%
Public Debt			
State/State Agency/Municipal Bonds	5%	0% to 30%	17%
U.S. Treasury/Agency Bonds	0%	0% to 30%	1%
U.S. Treasury Inflation Protected Securities	0%	0% to 10%	0%
Corporate Bonds	10%	0% to 30%	3%
Private Debt			
BCPL State Trust Fund Loans	30%	20% to 50%	40%
Other Private Debt	10%	0% to 20%	2%
Equities and Alternatives	45%		9%
Public Equities			
Domestic Equities	7.5%	5% to 20%	4%
Global Equities	7.5%	5% to 20%	4%
Alternatives			
Private Real Estate	20%	5% to 25%	0%
Real Assets/Infrastructure	5%	0% to 10%	0%
Private Equity/Venture Capital	5%	0% to 10%	1%
Cash	0%	0% to 10%	29%

Rebalancing

Rebalancing is the term that describes the periodic movement of funds from one asset or asset class to another in order to realign assets to the strategic asset allocation target. Systematic rebalancing can reduce portfolio volatility and increase portfolio return over the long-term. However, frequent rebalancing resulting from excessively tight ranges can lead to unnecessary transaction costs.

The Investment Committee will be responsible for developing and implementing a rebalancing plan that is appropriate for existing market conditions, with a primary objective of minimizing transaction costs, market impact, opportunity costs and portfolio disruptions. To the extent possible, cash flows and revenues will be used to maintain the strategic target allocation.

Recognizing that at times it may be impractical or costly to reallocate assets when an upper or lower limit is breached, the asset class will be rebalanced to within its strategic asset allocation range as soon as is practically possible, subject to reasonable transaction costs.

Tactical Asset Allocation

Capital markets exhibit periodic inefficiencies that may be exploited through shorter-term tactical shifts in asset allocations to increase expected investment performance. The amount of any tactical allocation shall be limited to ranges specified within the approved asset allocation.

Benchmarks

The Board has selected the following benchmarks for the Common School Fund:

Asset Class	Benchmark
Fixed Income	S&P Taxable Municipal Bond
Domestic Equities	Russell 3000 Index
International Equities	MSCI ACWI Ex-USA Index
Real Estate	NFI-ODCE Property Index
Real Assets/Infrastructure	Strategy Dependent
Private Equity/Venture Capital	Strategy Dependent
Cash	S&P U.S. Treasury Bill Index

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Normal School Fund

Investment Policy Statement

Fund Purpose

The University of Wisconsin, as the successor of the original normal schools, is the beneficiary of the Normal School Fund. Distributions are currently directed by Statute to provide funding for UW student scholarships and program funding at the UW-Stevens Point.

Funding Sources

This Fund was originally established with federal land grants totaling about 1.75 million acres. Except for about 71,000 acres that remain in trust, all lands from these original grants were sold to establish the Fund. Additions to principal come from the gross proceeds of timber sales and capital gains on investments held one year and longer.

Distribution Policy

This fund was originally established for monies not needed by common schools, and is governed by the same constitutional language that constrains investment of the Common School Fund. Interest income, dividends, and short-term capital gains are distributed to beneficiaries in accordance with the State Constitution and agency policy.

Distributions shall adhere to the policy described in detail on page 19, with the targeted distribution at the 5-year moving average of fund net annual earnings during the prior five fiscal years. However, because there was a change in the funding mechanism for agency expenses in FY2020 (the funding of agency expenses was changed from program revenue to general purpose tax revenues), a transition policy is needed to eliminate the impact of this change on the calculation of the 5-year earnings average. Therefore, the calculation of targeted distribution through FY2024 will include Normal School Fund gross revenues (rather than net earnings) for years prior to FY2020.

A smoothing account shall be established from withheld earnings, with the minimum dollar amount to be determined on October 1st of each year at 50% of the next targeted distribution. The smoothing account shall be used to supplement the distribution during years when interest, dividends and short-term capital gains earned during the current fiscal year are lower than the targeted distribution.

The BCPL Investment Committee has the authority to increase the minimum amount to be held in the smoothing fund to a maximum 100% of the next targeted distribution amount. This action shall require a determination by the Investment Committee that the increase is in the long-term best interest of beneficiaries.

Investment Objective

The annual return objective will be to maximize expected earnings within acceptable risk parameters. The long-term goal is to increase fund principal and annual distributions to beneficiaries at or above the appropriate long-term rate of inflation.

There are many measures of inflation published by the U.S. Bureau of Labor Statistics, but the appropriate measure of inflation for these purposes should be strongly related to the use of funds. In the case of the Normal School Fund, the funds are used for programs and scholarships at the University of Wisconsin. The most appropriate inflation index is CPI – Education as published by the U.S. Bureau of Labor Statistics. This index has grown at an average annual rate of 4.9% since first created in 1993, well above the overall inflation rate (CPI) during this period:

	CPI - Education	CPI	Normal School Fund Avg Annual Fund Growth *
1993-2019	4.9%	4.0%	1.7%
2000-2019	4.7%	2.1%	1.9%
2010-2019	3.3%	1.7%	1.8%

*Fund balance for 2010 and 2019 is net of monies reserved for land bank purchases.

The Federal Reserve has chosen 2.0% as the long-term inflation target within the United States, and since the early 1980s has been quite effective in maintaining lower overall inflation rates. There is no reason to predict that the Federal Reserve will lose the ability to control future inflation, so it is reasonable to assume that overall long-term inflation (CPI) will remain near 2%. Should historical tendencies continue, inflation in education will outpace CPI moving forward. A prudent assumption for the Normal School Fund will assume long-term inflation for education at 4%.

The growth of Trust Fund principal at or above the long-term rate of inflation is required for equitable treatment of future generations. Since statehood, principal of the Normal School Fund had grown only through the sale of timber harvested from Trust Lands. As shown in the above table, net timber revenues have not provided sufficient growth in recent history for fund principal to keep pace with inflation.

However, the FY2020 switch to GPR (State of Wisconsin general purpose tax revenues) funding of agency expenses removes the need for investment income to cover agency expenses for timber and land management programs. This change reduces the need for stable income and allows the reallocation of assets from the prior policy that included only fixed income securities.

The goal for this new allocation of financial assets will be to supplement the long-term capital gains provided by timber revenues so that fund principal increases at or above the rate of inflation. Because timber revenues added no more than 1.7% annual growth over the past 25+ years, producing fund growth above the assumed 4% rate of inflation requires financial assets to contribute a minimum of 2.3% annual growth to fund principal. A prudent assumption would round that requirement up to 2.5%.

Sustaining supplemental growth of 2.5% from financial assets while producing the stable income stream necessary to fund designated UW scholarship and academic programs will require a significant shift to asset classes including equities and real estate.

Portfolio Constraints

Wisconsin Constitution

The Wisconsin Constitution requires that all Normal School Fund income is distributed to beneficiaries, with principal balances maintained within the fund. Most other endowments distribute both interest and principal to meet the needs of beneficiaries, and pay out a fixed percentage of the beginning principal balance regardless of investment results. The inability to distribute Normal School Fund principal is critical to asset management policy, and requires Normal School Fund assets to be managed differently than the peer group of endowments.

Beneficiary Dependence on Annual Distributions

Earnings are distributed to the University of Wisconsin and are currently dedicated to fund scholarships for UW-Madison and UW-Extension students as well as programs at UW-Stevens Point. While this distribution is a small percentage of the total budget of the University, these monies remain an important source of funding for these scholarships and academic programs. The current level of distributions is approximately 2% of the fund balance.

Liquidity

Liquidity is necessary only for the amount and timing of distributions.

Strategic Asset Allocation

Based on the objective to contribute long-term capital gains to principal, along with long-term return expectations and risk tolerance, the BCPL has chosen the following strategic asset allocation policy for the Normal School Fund:

Normal School Fund Target Asset Allocation

Asset Class	Target Allocation	Range	Current Allocation 12/31/2019
Fixed Income	30%		81%
Public Debt			
State/State Agency/Municipal Bonds	0%	0% to 20%	21%
U.S. Treasury/Agency Bonds	0%	0% to 20%	0%
U.S. Treasury Inflation Protected Securities	0%	0% to 10%	0%
Corporate Bonds	0%	0% to 10%	0%
Private Debt			
BCPL State Trust Fund Loans	30%	20% to 40%	60%
Other Private Debt	0%	0% to 10%	0%
Equities and Alternatives	70%		0%
Public Equities			
Domestic Equities	15%	10% to 30%	0%
Global Equities	15%	10% to 30%	0%
Alternatives			
Private Real Estate	40%	10% to 60%	0%
Real Assets/Infrastructure	0%	0% to 10%	0%
Private Equity/Venture Capital	0%	0% to 10%	0%
Cash	0%		19%

Rebalancing

Rebalancing is the term that describes the periodic movement of funds from one asset or asset class to another in order to realign assets to the strategic asset allocation target. Systematic rebalancing can reduce portfolio volatility and increase portfolio return over the long-term. However, frequent rebalancing resulting from excessively tight ranges can lead to unnecessary transaction costs.

The Investment Committee will be responsible for developing and implementing a rebalancing plan that is appropriate for existing market conditions, with a primary objective of minimizing transaction costs, market impact, opportunity costs and portfolio disruptions. To the extent possible, cash flows and revenues will be used to maintain the strategic target allocation.

Recognizing that at times it may be impractical or costly to reallocate assets when an upper or lower limit is breached, the asset class will be rebalanced to within its strategic asset allocation range as soon as is practically possible, subject to reasonable transaction costs.

Tactical Asset Allocation

Capital markets exhibit periodic inefficiencies that may be exploited through shorter-term tactical shifts in asset allocations to increase expected investment performance. The amount of any tactical allocation shall be limited to ranges specified within the approved asset allocation.

Benchmark

Recognizing that a long-term target allocation to alternative asset classes can often take a matter of years to implement prudently, the Investment Committee will review benchmarks to be adjusted as progress is made towards the long-term strategic asset allocation target.

The Board has selected the following benchmarks for the Normal School Fund:

Asset Class	Benchmark
Fixed Income	S&P Taxable Municipal Bond
Domestic Equities	Russell 3000 Index
International Equities	MSCI ACWI Ex-USA Index
Cash	S&P U.S. Treasury Bill Index
Real Estate	NFI-ODCE Property Index

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University Fund

Investment Policy Statement

Fund Purpose

The purpose of the University Fund is to support the University of Wisconsin.

Funding Sources

In 1838, Congress granted to the Territory of Wisconsin the equivalent of two townships, or 72 square miles of land, to be sold to support a university. In 1854, Congress granted an additional two townships of land to benefit a university. Most of these lands were sold soon after Wisconsin obtained title, and no provision was made in the law for adding to the principal of this fund.

Distribution Policy

All interest earnings, dividends and short-term capital gains are distributed to the University of Wisconsin.

Investment Objective

The return objective of the University Fund is to maximize long-term capital gains so that fund principal grows at levels higher than the rate of inflation. The Prudent Investor Standard is now available to guide management of fund assets and distribution of current income has very little impact on University of Wisconsin operations. Fund principal should be allowed to grow so that the University Fund may be relevant to future generations of University Wisconsin students.

Portfolio Constraints

Fund size limits the availability of alternative investments and the flexibility of the strategic asset allocation.

Strategic Asset Allocation

The beneficiary is not dependent in any manner from distributions of this fund, so the University Fund should be fully allocated in a manner to generate long-term capital gains. The small size of the Fund makes it efficient to utilize passively-managed equity mutual funds or ETFs that are focused on long-term capital gains.

Benchmark

The Board has selected the following benchmarks for the University Fund: Russell 3000 Index.

Agricultural College Fund

Investment Policy Statement

Fund Purpose

The purpose of the Agricultural College Fund is to support the University of Wisconsin.

Funding Sources

The Agricultural College Fund was established with an 1862 act of Congress that granted land to create a permanent endowment to support “colleges of agriculture and mechanical arts” in each state. The Morrill Act gave rise to land grant colleges across the nation by providing that each state was entitled to 30,000 acres of land for each member of Congress. Wisconsin had eight Congressional representatives at that time, so received title to 240,000 acres of land under this law. These lands were sold shortly after Wisconsin obtained title, and no provision was made in the law for adding to the principal of this fund.

Distribution Policy

All interest earnings and short-term capital gains are distributed to the University of Wisconsin.

Investment Objective

The return objective of the Agricultural College Fund is to maximize interest income within acceptable risk parameters.

Portfolio Constraints

The Agricultural College Fund is constrained to investment in government fixed-income securities by Section 4 of the Morrill Act of 1862.

Strategic Asset Allocation

The beneficiary has absolutely no dependence on distributions from the Agricultural College Fund, so it is appropriate to invest fully in Treasury Inflation Indexed Securities. The beneficiary would receive a small interest payment each year, and inflation would be added to principal to grow the fund over time. This strategy may provide for an impactful distribution in some future year.

Benchmark

The Board has selected the following benchmarks for the Agricultural College Fund: S&P U.S. TIPS 30 Year Index.

Addendum 1

CFA Institute Code of Ethics and Standard of Professional Conduct
CFA Institute Asset Manager Code of Conduct

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