

# TEXAS STATE UNIVERSITY SYSTEM



## **Investment Policy for Operating Funds and Endowment Funds November 2016**

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## **Texas State University System Investment Policy**

### I. PREFACE

This Policy is the approved Investment Policy for Operating Funds and Endowment Funds of the Texas State University System. Texas State University System ("TSUS") refers to System Administration, Lamar University, Sam Houston State University, Sul Ross State University, Texas State University, Lamar Institute of Technology, Lamar State College-Orange, Lamar State College- Port Arthur, and Sul Ross State University - Rio Grande College.

### II. POLICY AND OBJECTIVES

#### A. OPERATING FUNDS

It is the policy of TSUS to invest operating funds in compliance with the "Prudent Person Standard" as defined by Texas Education Code §51.0031(d). The Investment Policy for Operating Funds and Endowment Funds ("Policy") of TSUS is designed to fulfill the following objectives with respect to Operating Funds:

- Provide security of invested principal;
- Provide liquidity for operating requirements which may be reasonably anticipated;
- Manage interest-rate and market risk;
- Maximize total return within established risk constraints; and
- Provide for diversification of investment assets.

To meet these objectives, TSUS will base investment decisions on short-term, intermediate-term, and long-term needs dictated by cash flow analyses of present and anticipated future financial requirements.

This Policy applies to the following operating funds held by TSUS:

- Current Funds (Unrestricted and Restricted);
- Loan Funds;
- Bond Funds;
- Plant Funds;
- Board-Designated Reserves; and
- Agency Funds

These funds may be held in investments authorized by this Policy (based on liquidity needs or bond covenants) or in authorized depositories as required for day-to-day operations within any fund group. A component is not required to liquidate investments that were authorized investments at the time of purchase unless so directed by the Board. Funds held in banking institutions are covered by the TSUS *Depository Funds Policy*.

Pursuant to Texas Government Code §2256.005, this Policy shall be reviewed and updated annually and presented to the Board for adoption by resolution. Copies of the Policy will be forwarded on an annual basis by each component investment officer to any entity (except

TexPool) with which the component conducts investment transactions. Such entities will be required to acknowledge in writing receipt of the Policy and to attest that they have implemented reasonable procedures and internal controls to comply with provisions contained within the Policy. The Vice Chancellor for Finance will distribute the Policy to and obtain the acknowledgement from TexPool on behalf of the Texas State University System and its components and will do likewise for any entity, including investment advisors, conducting investment transactions on behalf of the System Office.

Operating funds covered under this Policy are classified as:

**Short-Intermediate Term Funds**

Funds needed to meet operating requirements (within the budget year) as well as funds not designated as Long-Term. These Funds may be used within the operating year and are typically invested in investments with high quality and ready access to liquidity.

**Long-Term Funds**

Funds that comprise a core holding that are not intended to be spent during any budget period. These funds are typically invested in a similar manner to Endowment Funds, with similar risk and reward metrics. Long-Term Funds may not exceed 35% of all Operating Funds exclusive of Bond Proceeds Funds; as determined annually based on the Ending Market Values as of August 31 of each year (fiscal year end).

**Bond Proceed Funds**

Funds obtained by the issuance of debt for a stated purpose. Bond proceeds may be invested in a manner consistent with the requirements and restrictions stated in the applicable Bond Covenants, but typically not longer than three years. Bond Proceed Funds are to be invested following the same guidelines as Short-Intermediate Term Funds.

**B. ENDOWMENT FUNDS**

Endowment funds may include, but are not limited to, gifts of property, stock, and real assets, donated to TSUS to provide funding for scholarships, fellowships, professorships, academic chairs, and other uses as specified by the donors. It is the policy of TSUS to invest endowment funds in compliance with the Uniform Prudent Management of Institutional Funds Act (UPMIFA), Texas Property Code Chapter 163.

Funds functioning as endowments (commonly referred to as quasi-endowments) are resources that the governing board, rather than the donor, has determined are to be retained and managed like an endowment. Principal and income of these funds may be utilized at the discretion of the governing board. Resources that the governing board sets aside to function as an endowment may be unrestricted or restricted by an agent outside the institution.

Funds which by their nature are long term and have or potentially may have endowment qualities, for example Charitable Gift Annuities, may be invested with the endowment to the extent permitted by law and the individual charitable documents.

The endowment funds may be invested as authorized by this Policy and, for short periods, be placed in authorized TSUS depositories for the processing of receivables and disbursements.

This Policy is designed to fulfill the following objectives with respect to Endowment Funds:

- provide security of invested principal;

- provide for appreciation of principal;
- provide a continuing and dependable cash payout within market constraints;
- provide for planned liquidity for anticipated cash flow purposes;
- manage market risks;
- maximize overall total return within the established risk constraints; and
- provide for diversification of investment assets.

The long term objective of an endowment is to preserve the intergenerational equity of the endowment while providing an appropriate current spending policy. All endowment funds will be managed by the “Prudent Person Standard”.

### III. DELEGATION OF AUTHORITY AND RESPONSIBILITY

#### Board of Regents

The TSUS Board of Regents (the “Board”) retains ultimate responsibility for investments as fiduciaries of TSUS assets regardless of who is investing those assets. The Board is statutorily required to:

- Designate Investment Officers, at least annually, review and adopt this Policy, at least annually, review and adopt a list of qualified broker/dealers authorized to engage in investment transactions with TSUS,
- At least quarterly, receive and review investment reports prepared in accordance with this Policy, and
- Attend at least one training session as regards to Board responsibilities under the Act within six (6) months of assuming office as provided by the Higher Education Coordinating Board.

#### Investment Officers

The Chief Financial Officer (CFO) for System Administration and the CFO for each component are designated as Investment Officers for their respective entities by the Board. Additional Investment Officers may be designated by the Chancellor or the President of the component.

Investment Officers are responsible for investment management decisions and activities and all transactions undertaken, including the hiring/firing of Investment Manager(s) recommended by the Investment Consultants, and banking relationships. No officer or designee may engage in an investment transaction except as provided under terms of this Policy. No Investment Officer or employee of TSUS may accept anything of value from counter-parties or others in connection with investment transactions.

Each Investment Officer must attend five or more hours of investment training within six months of assuming the position and not less than once each state fiscal biennium. The Board acknowledges investment act training alternatives as provided through eligible sponsors recognized by the Texas State Board of Public Accountancy or CPE credits accepted by the CFA Institute will meet the training requirements.

The Investment Officer of each component shall prepare a report on compliance with the training requirements and deliver the report to the Vice Chancellor for Finance by November 15th of every odd-numbered year. The Vice Chancellor for Finance will provide to the Board a summary report on compliance with the training requirements as well as a report of any legislative changes

affecting TSUS investment activities not later than the 180th day after the last day of each regular session of the legislature.

### Investment Officer Disclosures

The following reporting requirements apply:

1. An Investment Officer related within the second degree by affinity or consanguinity to an individual seeking to sell an investment to TSUS shall file a statement disclosing that relationship;
2. An Investment Officer having a business relationship of any nature with an individual seeking to sell an investment to TSUS shall file a statement disclosing that relationship;
3. The disclosure shall be filed with the Board and the component President or with the Chancellor if the applicable Investment Officer is the CFO for System Administration.

### Investment Consultant

System Administration and the components may contract with an Investment Consultant registered under the Investment Advisers Act of 1940 (15 U.S.C. Section 80b-1 et seq.) to provide for investment oversight of the Operating and/or Endowment Funds. System Administration is responsible for the management of any investment consultant contract, including the solicitation and selection of the investment consultant. The initial contract may not be for a term exceeding six years and renewals or extensions of the contract must be made by order or resolution of the Board. The Investment Consultant must acknowledge in writing that they are a fiduciary to the Fund(s).

The Investment Consultant must certify to the receipt and review of this Policy and that it will act in accordance with the Policy; and it will provide the most recent copy of its Form ADV and ADV brochure as filed with the Securities and Exchange Commission to the CFO(s) for the component(s) that it advises.

The Investment Consultant's responsibilities are to the System Administration and the components it advises. Additionally, the Investment Consultant will:

- Assist in the development and implementation of investment policies, objectives, and guidelines to submit to the Board for approval at least annually.
- Review investment strategies and vehicles, including search, selection, and recommendation of investments to the Investment Officer.
- Prepare and present performance evaluation reports in accordance to established investment standards.
- Review contracts and fees for both current and proposed Investment Managers.
- Communicate investment policies and objectives to Investment Managers, monitor those strategies, and notify the Investment Officers of any significant changes in portfolio managers, litigation, or violation of securities regulations.

### Investment Manager(s)

System Administration and the components may contract with one or more Investment Managers registered under the Investment Advisers Act of 1940 (15 U.S.C. Section 80b-1 et seq. A contract made under authority of this subsection for Operating Funds must contain a

termination clause with a maximum 30 days' notice provision and may not be for a term longer than two years. A renewal or extension of the contract must be approved by the Board.

The Investment Manager(s) must certify to the receipt and review of this Policy; it will act in accordance with the Policy; and it will provide a copy of its most current Form ADV and ADV brochure as filed with the Securities and Exchange Commission to the CFO(s) for the component(s) that it advises (see Exhibit 1).

All Investment Managers have a fiduciary responsibility to make a good faith determination that commissions paid to a broker are reasonable and competitive. All Investment Managers shall treat the accounts they manage as discretionary accounts and have authority to act for Investment Officers. The Investment Managers have the authority to make investment decisions for the purpose of placing orders to effect any purchase, sale, exchange, liquidation or other investment of the assets in the accounts, within their asset class, and according to this Policy, without obtaining prior approval.

For Investment Managers of Commingled funds and Mutual funds: Investment Officers must collect a copy of Commingled funds governing documents for each Commingled fund investment, and collect a Mutual Fund prospectus for each mutual fund investment.

TSUS requests that all orders for transactions of account assets be placed in such markets and through such brokers as shall offer the most favorable price, execution and commission cost of each order (best execution). All such orders must also be in compliance with this investment policy.

TSUS acknowledges that Investment Managers may in accordance with applicable law pay commissions to brokers that are higher than those that might be obtainable elsewhere in order to obtain research and other services provided by such brokers in the expectation to enhance the long-term value of the account. The Investment Officers shall try to negotiate the contract without the use of these soft dollar arrangements. In the event that the soft dollar arrangements remain as part of the contract, the Investment Manager(s) will report to the Investment Consultant and the Investment Officers at least annually, the Investment Managers' soft dollar practices and any soft dollar purchases. In addition, Investment Managers must demonstrate how the soft dollars were used solely for the benefit of the account which generated the soft dollars.

The use of soft dollars by an Investment Manager in the portfolio must be disclosed under the investment disclosure requirements section on the component's webpage.

### Investment Custodians

The Investment Custodians are responsible for the safekeeping of the Operating and Endowment Funds' assets. Their responsibilities are to:

- Provide timely (defined as within 6 business days of month end) and accurate reports detailing investment holdings, including, on a Trade Date accrual basis:
  - Statement of all securities and other assets held,
  - Statement of all receipts, sales, redemptions, and principal payments,
  - Statement of all distributions, expenses paid, purchases, and
  - Statement of all income, and
  - Establishing and maintaining separate accounts for each Investment Manager.

- Provide all normal custodian functions, including but not limited to:
  - Security safekeeping,
  - Collection of income,
  - Settlement of trades,
  - Collection of proceeds of maturing securities, and
  - Daily investment of available cash.

#### IV. STANDARD OF CARE

Pursuant to Texas Education Code §51.0031(d), the “Prudent Person Standard” shall be the standard used in all investment functions and shall be applied in the context of individual transactions as well as management of the overall portfolio. Accordingly, all investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, emphasizing the probable safety of their capital as well as the expected income to be derived.

All investments shall be consistent with this Policy. The Investment Officer shall not be held personally liable for a specific security's credit risk or market value change as long as actions were in accordance with this Policy, unexpected deviations were reported to the component President and the CFO for System Administration in a timely manner, and all appropriate actions were taken to control adverse developments.

#### V. INSTITUTIONAL INVESTMENT PROCEDURES

The Investment Officer(s) of each component shall establish written procedures supporting this Policy and promoting internal control. The procedures shall be directed towards preventing loss of funds due to fraud, employee error, misrepresentation, or imprudent actions.

The Investment Officers of the components shall establish and maintain (a) written administrative procedures and guidelines in support of this Policy for their respective component, (b) distribution formulae/procedures for the funds, and (c) internal controls in support of this Policy.

All components shall ensure the following specific controls, as further defined by this Policy, are incorporated into their operating procedures or the operating procedures of the Investment Managers.

- All securities will be settled delivery versus payment (DVP) into the component's depository or custodian bank,
- No securities will be safe-kept with a broker/dealer,
- Operating funds cash flow will be reviewed at a high level at least annually to determine investment strategy impact and projections,
- Every transaction will be documented for accounting information and security description,
- All transaction documentation will be completed within five business days of receipt,
- An investment ledger will be maintained for reconciliation with the general ledger, bank reports, and trade confirmations on a monthly basis, at a minimum,
- A monthly reconciliation of transactions and income will be made,
- A review of the portfolio will be made by all Investment Officers at least quarterly,
- Designated levels of signatory approval will be set,
- Investment reporting will be completed quarterly, and
- All transactions will have dual control and/or oversight and separation of responsibilities.



System Administration and each component may pursue an active portfolio management strategy for Endowment Funds with investments diversified by asset class and style. All Endowment Fund investment securities must be held under a custodial agreement and all Investment Managers must provide monthly statements to the Investment Officer. The Investment Officer and/or Investment Consultant will regularly monitor the contents of the portfolio, the available markets, and the relative value of competing instruments to adjust the portfolio in response to market conditions. Quarterly reviews of performance shall be made by the Investment Officers.

## VI. INVESTMENT STRATEGIES AND OBJECTIVES

### A. OPERATING FUNDS

Operating funds may be commingled at each component for investment purposes but will address the unique characteristics and needs of each fund group and classification of funds represented in the portfolio. Operating funds are constricted by expenditure plans and can serve a fiscal year or multiple year purposes.

The investment strategy for operating funds has as its primary objective assurance that anticipated liabilities are matched and adequate investment liquidity provided. The secondary objective is to create a portfolio structure which will experience minimal volatility while generating income.

The intention is to match investments with projected cash flow and liquidity needs. TSUS may pursue an active versus a passive portfolio management strategy. That is, securities may be sold before they mature if market conditions present an opportunity for a net positive horizon fiscal benefit from the trade, or to manage a market downturn.

The Investment Officer and/or Investment Consultant will continuously monitor the contents of the portfolio, the available markets, and the relative value of all authorized, competing instruments to adjust the portfolio in response to market conditions.

### B. ENDOWMENT FUNDS

The Endowment performance objective is to grow the market value of assets net of inflation, spending, and expenses, over a full market cycle (generally defined as a three to five year period) without undue exposure to risk. The Endowment is particularly risk-adverse to the probability of not meeting the total return goal. Liquidity must be considered and sufficient to meet the spending needs and expenses.

The total return goal can be achieved while assuming acceptable risk levels commensurate with "market volatility." To achieve the total return goal, the endowment's assets will be invested to generate appreciation and/or dividend and interest income.

The Endowment is expected to endure into perpetuity. Inflation is a key component in the performance objective. The long-term risk of not investing in growth securities outweighs the short-term volatility risk. As a result, the majority of assets should be invested in equity or equity-like securities. Fixed income securities lower the short-term volatility of the portfolio and provide income stability, especially during periods of weak or negative equity markets. Other asset classes are included to provide diversification and incremental total return.

The cash payout requirement for Endowment Funds is significant and continuous. The portfolio shall be diversified to diminish risks associated with particular securities, market sectors, or industries with an excessive impact on the funds.

## VII. INVESTMENT GUIDELINES

### A. OPERATING SHORT-INTERMEDIATE TERM FUNDS

Refer to APPENDIX 1 for Investment Guidelines for Operating Short-Term portfolios. This includes Diversification parameters, approved allocation ranges, and Prohibited Investments.

### B. OPERATING LONG-TERM FUNDS

Refer to APPENDIX 2 for Investment Guidelines for Operating Long-Term portfolios. This includes Diversification parameters, approved allocation ranges, and Prohibited Investments.

### C. ENDOWMENT FUNDS

Refer to APPENDIX 3 for Investment Guidelines for Endowment portfolios. This includes Diversification parameters, approved allocation ranges, and Prohibited Investments.

## VIII. REBALANCING

Since asset allocation is a critical component of Investment Portfolio returns, it is desirable to review the investment portfolio as follows:

Operating Funds: At least quarterly, more frequently as necessary

Endowment: At least annually, more frequently if necessary.

In the event any individual asset class falls outside the allocation range specified in the appropriate Appendix, rebalancing should be performed in a prudent manner.

The appropriateness of Asset Allocation ranges will be reviewed annually.

## IX. SAFEKEEPING

All securities, including collateral bought under a repurchase agreement, but excluding investment pool funds, certificates of deposit, and mutual funds, shall be settled on a delivery versus payment (DVP) basis. All securities shall be held by System Administration's or the component's depository bank, as applicable, or an independent third party custodian approved by the System Office. All securities will be held in the name of System Administration or the component, as applicable. No broker/dealer shall be used for safekeeping purposes.

The third party custodian of TSUS-owned assets shall be required to issue an original safekeeping trust statement to the System Administration or the component, as applicable, on a timely basis describing the specific instrument, coupon, maturity, par, CUSIP, and other pertinent information. The safekeeping receipt shall clearly identify ownership by System

Administration or the component, as applicable.

## X. SECURITIES LENDING

Participation in securities lending programs are prohibited under this Policy.

## XI. FINANCIAL DEALERS AND INSTITUTIONS

- A. If a business organization (including investment pools and investment management firms under contract) is not utilized, then the transaction requires the use of one or more broker/dealers.
- B. All Investment Officers who invest directly will maintain a list of the broker/dealers that they use, and keep on file all certifications collected under sections XI. C and XI. D below.
- C. Investment Officers are responsible for confirming that all the broker/dealers they utilize conform with compliance requirements and procedures established by the CFO for System Administration to include the following:
- Brokers/dealers must complete a questionnaire (see Exhibit 2) supplying basic firm and broker contact and delivery information,
  - Brokers/dealers may be affiliated with a Texas bank, designated by the New York Federal Reserve Bank as "primary dealers" or qualify as regional dealers under the Securities and Exchange Commission's "Uniform Net Capital Rule",
  - Brokers/dealers must be FINRA (Financial Institutions Regulatory Authority),
  - Brokers/dealers must be registered with the Texas Securities Commission, and;
  - Brokers/dealers must provide the written certification detailed below.
  - Broker/dealer agreements cannot exceed two years in duration, expiring end of day November 30, consistent with Board of Regent consideration of the Investment Policy.
- D. Certification: Upon request, an Investment Officer shall present to any firm or person seeking to engage in an Operating Fund investment transaction with TSUS a written copy of this Policy This includes business organizations, brokers/dealers, and banks. 40-act funds, Commingled funds, and registered Exchange Traded Funds are excluded from the certification process; the Investment Officer must obtain the fund prospectus for each Mutual Fund/ETF investment and the investment documents for each Commingled fund investment. The prospectus should be collected annually, the Commingled investment documents are collected at the time the investment is made.

All Investment Officers must collect from the Qualified Representative of the business organization or the broker offering to engage in an investment transaction a signed certification (see Exhibit 1) to the effect that the business organization, registered principal, or broker has:

1. Received and reviewed this Policy and
2. Acknowledged that the business organization has implemented reasonable procedures and controls in an effort to preclude investment transactions conducted between TSUS and the organization that are not authorized by this Policy except to the extent that this authorization is dependent on an analysis of the makeup of the entire portfolio or requires an interpretation of subjective portfolio standards.

3. Agreed to provide to the component, the System Office, and the Investment Consultant retained by the System Office (if any) all monthly data and schedules necessary to accurately prepare the required reporting for the System Office with 6 business days of month end.

Investment Officers may not acquire or otherwise obtain any investment from a person, bank or firm that has not provided this certification.

Nothing in this section relieves the investing entity of the responsibility for monitoring the investments made by the investing entity to determine that they are in compliance with this Policy.

## XII. INVESTMENT REPORTING AND MONITORING

### A. OPERATING FUNDS

Investment Officers shall cause to be prepared and review a written report of investment transactions for all investments not less than quarterly. The report is to be submitted to the CFO for System Administration or designee and any respective component President by the end of the next month following the end of each quarter.

Component investment reports and a consolidated report (compiled by the CFO for System Administration or designee) shall be submitted to the Board through the Finance and Audit Committee in the format prescribed by Sec. 2256.023 of the Public Funds Investment Act, the General Appropriations Act, and requirements promulgated by other oversight agencies.

The reports must:

1. Describe in detail the investment position of the component on the date of the report;
2. Be prepared jointly by all Investment Officer(s) of the component;
3. Be signed by each Investment Officer(s) of the component;
4. Contain a summary statement of each pooled fund group or managed account using trade date accounting with accruals for each outside managed account, fund, or portfolio that contains:
  - ( a ) Beginning Market Value (defined as trade date with accruals) for the reporting period;
  - ( b ) Ending Market Value (defined as trade date with accruals) for the reporting period;
  - ( c ) Net Total Return for the reporting period, calculated net of all investment management fees where applied;
  - ( d ) Fully accrued Interest Income for the reporting period;
5. For each investment not held in a managed account, in addition to 4 a, b, c and d above, state the Book Value and Market Value of each such investment separately by the Operating account which holds it for the reporting period categorized by the type of asset and fund type invested;
6. State the maturity date of each separately invested asset that has a maturity date (liquid positions will carry next day end dates);
7. State the compliance of the investment portfolio of the component as it relates to the investment strategy expressed in this Policy; and relevant provisions of the

Act.

8. State the performance investment return in comparison to the established benchmarks as established by this Policy. Investment returns are to be calculated net of fees, using the performance reporting methodology found in the Global Investment Performance Standards Handbook published under the guidance of the CFA Institute  
<http://www.cfainstitute.org/ethics/codes/gipsstandards/Pages/index.aspx>

The Global Investment Performance Standards (GIPS Standards) is a set of standardized, industry-wide ethical principles that provides guidance on how to calculate and report investment results.

Market prices are to be obtained from an independent, published source such as the Wall Street Journal, a custodian bank, a recognized financial website (such as Bloomberg), and/or through a contractual arrangement with a pricing service. Asset prices are not to be obtained from the broker/dealer having sold TSUS the asset being priced.

## B. ENDOWMENT

Investment Officers shall cause to be prepared and review a written report of investment transactions for all endowment funds not less than quarterly. The report is to be submitted to the CFO for System Administration or designee and any respective component President by the end of the next month following the end of each quarter.

This report will be consolidated into a system-wide summary report to be submitted to the Board through the Finance and Audit Committee in the format prescribed by CFO for System Administration.

The reports must:

1. Be signed by the Investment Officer,
2. State the compliance of the portfolio to the investment strategy expressed in this Policy,
3. Provide Ending Market Values of the portfolio, including, at a minimum, Ending Market Value of each asset class all on a trade date full accrual accounting basis,
4. Actual Total Portfolio return calculated net of investment management fees where applicable of the reporting quarter and the fiscal year to date which includes actual Net Market return for each asset class. Investment returns are to be calculated net of fees, using the performance reporting methodology found in the Global Investment Performance Standards Handbook published under the guidance of the CFA Institute:  
<http://www.cfainstitute.org/ethics/codes/gipsstandards/Pages/index.aspx>.  
The Global Investment Performance Standards (GIPS Standards) is a set of standardized, industry-wide ethical principles that provides guidance on how to calculate and report investment results.
5. State a rate of return comparison to the established benchmarks of each asset class (indicate each benchmark that is used), and a weighted benchmark based on the asset allocation for the entire portfolio. The total portfolio benchmark should include the weights used to reflect that benchmark.

Market prices are to be obtained from an independent, published source such as the Wall Street Journal, a custodian bank, a recognized financial website (such as Bloomberg), and/or through a contractual arrangement with a pricing service. Asset

prices are not to be obtained from the broker/dealer having sold TSUS the Asset being priced.

### XIII. BENCHMARKS

The performance of each TSUS component will be measured against a customized blended index. The index will be developed and reviewed each November by a committee of three TSUS Investment Officers or their appointed representatives in consultation with the Investment Consultant. All performance returns shall be stated net of investment management fees. Other applicable indexes matching the specific allocation of the funds (for example international mutual funds or equities) shall be detailed in the component's procedures and included on all monthly and quarterly reporting as a benchmark for these investments.

### XIV. AUDITS

#### A. Operating Funds

- i. TSUS shall have a compliance audit of management controls on investments per the Public Funds Investment Act and adherence to this Policy at least once every two years. The audit shall be performed by the Office of Audits & Analysis or by a private auditor and the results of the audit shall be reported to the Board and the State Auditor not later than January 1 of each even-numbered year.
- ii. If a component invests in other than money market mutual funds, investment pools or accounts offered by its depository bank in the form of certificates of deposit or money market accounts, the reports prepared by the investment(s) officers shall be reviewed at least annually by an independent auditor, and the results reported to the Board.

### XV. INVESTMENT POLICY ADOPTION AND CERTIFICATION

This Policy shall be reviewed and adopted annually by the Board. The Policy adopted by the Board shall record any changes made to either the investment policy or investment strategies.

**APPENDIX 1**  
**INVESTMENT GUIDELINES FOR OPERATING SHORT-INTERMEDIATE TERM FUNDS**

**A. LIQUIDITY**

The intention of the Operating Short-Intermediate Term Funds portfolio is to provide necessary Liquidity to operations. A minimum of **5%** of the Operating Short-Intermediate Term Funds portfolio must have Daily Liquidity; additionally a minimum of **20%** of the Operating Short-Intermediate Term Funds portfolio must be accessible within Trade Date plus 3 days. Components must meet these minimum requirements and are free to exceed them as they see prudent.

**B. CREDIT QUALITY**

Unless specified elsewhere, Credit Ratings recognized by this policy may only be issued by the agencies of Standard and Poor's, Fitch, and/or Moody's. For definition purposes, Non Rated securities will be considered as Below Investment Grade.

The Average Credit Quality of the entire Short-Intermediate Term Funds Portfolio is to be greater than or equal to **A-**, as defined by S&P (**A-** by Fitch, **A3** by Moody's).

The Minimum Credit Quality of any investment must be **Investment Grade** at the Time of Purchase.

**C. WEIGHTED AVERAGE MATURITY**

The Weighted Average Maturity of the entire Short-Intermediate Term Funds Portfolio is to be less than or equal to **36 Months** as calculated by the Custodian and/or the Investment Consultant. There is no maximum Maturity of any single security.

**D. DIVERSIFICATION REQUIREMENTS**

- i. For Mutual Funds and Exchange-Traded Funds (ETFs): Maximum of **10%** ownership of the units outstanding of a single Fund or ETF.
- ii. No more than **40%** of the Portfolio may be invested in a **single** Mutual Fund or Manager EXCEPT for cash management and Fixed Income funds sponsored by organizations exempt from Federal Income taxation under Section 501( f ) Internal Revenue Code of 1986 (25 U.S.C. Section 501( f )-- currently Commonfund and TIAA-CREF. These funds must meet the requirements outlined in this Appendix Sections B and C.

**E. SOFT DOLLAR REPORTING**

If Soft Dollars are used in the account, a Quarterly report of Soft Dollar usage is required to be delivered to the Component Investment Officer.

**F. PROHIBITED INVESTMENTS AND ACTIVITIES**

Investments and activities that are not expressly prohibited in this Appendix are considered allowable by this Policy.

The following are prohibited transactions and securities for TSUS components. Any change in this list shall require amendment of this Policy and adoption by the Board.

- i. TSUS may not purchase or sell financial futures, options, interest rate swaps, or forward rate agreements.
- ii. TSUS may not engage in adjusted trading or short sales.
- iii. TSUS may not purchase residual interests in CMOs/REMICs or mortgages servicing rights. Specific securities that may not be purchased are:
  1. Inverse CMO floaters
  2. Principal only CMOs
  3. Interest only CMOs
- iv. TSUS may not purchase 144-A or other private placement securities not registered with the SEC.
- v. Non-US Dollar denominated securities are prohibited in Operating Short-Intermediate Fund portfolios. Foreign securities issued and priced in US. Dollars are allowed.
- vi. The use of Margin or leverage in Operating Short-Intermediate Term Funds Portfolios is prohibited.
- vii. The purchase of Equities in Operating Short-Intermediate Term Funds Portfolios is prohibited.



**APPENDIX 2  
INVESTMENT GUIDELINES FOR OPERATING LONG-TERM FUNDS**

A TSUS component may invest up to **35%** of the Market Value of its Total Operating Funds portfolio exclusive of Bond Proceeds in investments in this Appendix. Long-Term Funds are defined as 35% of All Operating Funds exclusive of Bond Proceeds Funds; the amount allocated to Long-Term Funds is re-calculated annually based on the Ending Market Values as of August 31 of each year (fiscal year end). Components are **not required** to participate in these Long-Term Funds Investment options and may elect to have no Operating Long-Term Funds.

Operating Long-Term funds are intended to be invested in a similar manner to Endowment funds, with additional restrictions in place. Consequently, this Appendix will refer to the Investment Guidelines for Endowment Funds, Appendix 3.

**A. DIVERSIFICATION**

This Policy recognizes two main Categories which Investments may be allocated: the Appreciation/Dividend Category and the Income Category.

The Appreciation/Dividend Category is defined as those Investments that are made primarily for Growth and Appreciation of the asset, with secondary allowances for Dividends earned on Equity and Equity-like securities.

The Income Category is defined as those Investments that are primarily for Cash Flow and Income generation from Bond and Bond-like securities.

**NOTE: Components must retain an Investment Consultant as defined in this policy to invest in the Appreciation/Dividend category. Agency Funds and Bond Funds may not be invested in Appreciation/Dividend category investments.**

Below is the Category Allocation Range.

Category	Minimum %	-	Maximum%
<b>Appreciation/Dividend</b>			
Domestic	0	-	50
<u>International</u>	<u>0</u>	<u>-</u>	<u>20</u>
<b>Total Appreciation/Dividend</b>	<b>0</b>	<b>-</b>	<b>50</b>
<b>Income</b>			
Domestic	50	-	100
<u>International</u>	<u>0</u>	<u>-</u>	<u>20</u>
<b>Total Income</b>	<b>50</b>	<b>-</b>	<b>100</b>
<b>TOTAL PORTFOLIO</b>	<b>100%</b>		

**B. INVESTMENTS, ACTIVITIES, PROHIBITIONS, AND EXCEPTIONS**

Investments and activities that are not expressly prohibited in this Appendix are considered allowable by this Policy.

All terms specified in sections B, C, and D of Appendix 3 **apply in this Appendix**, with the following additional limitations and prohibitions:

Prohibitions:

1. Non-US Dollar denominated bonds are prohibited
2. The direct or indirect use of derivatives, short sales, futures, options, private placements, limited partnerships, and otherwise illiquid investments is prohibited.

Additional Limitations:

1. No more than **20%** of the **Income Portfolio** may be rated below Investment Grade.
2. No more than **10%** of the **Total Portfolio** may be invested in Emerging/Frontier Markets, a sub-set of International.

**APPENDIX 3  
INVESTMENT GUIDELINES FOR ENDOWMENT FUNDS**

Policy asset allocation is the most single important decision for the Endowment Funds portfolio. A significant proportion of a portfolio investment behavior can be attributed to the asset classes/styles and the weighting of each asset class/style.

TSUS recognizes that investment risks can result from issuer defaults, market price changes, or various technical complications leading to temporary illiquidity. This risk is controlled through portfolio diversification. Investment Officer(s) shall diversify the portfolio(s) by market sector and maturity to minimize market risks.

**A. DIVERSIFICATION**

Diversification shall be considered within major market sectors so that various industries, maturities, markets, domestic and international factors are considered within the portfolio.

Asset Allocation is to be determined by each component as a result of their Required Rate of Return for the portfolio as defined by:

$$\text{Required Rate of Return} = \text{Spending Rate} + \text{Inflation} + \text{Endowment Expense rate.}$$

This Policy recognizes two main Categories which Investments may be allocated: the Appreciation/Dividend Category and the Income Category.

The Appreciation/Dividend Category is defined as those Investments that are made primarily for Growth and Appreciation of the asset, with secondary allowances for Dividends earned on Equity and Equity-like securities.

The Income Category is defined as those Investments that are primarily for Cash Flow and Income generation from Bond and Bond-like securities.

Below is the Category Allocation Range.

Category	Minimum	-	Maximum
<b>Appreciation/Dividend</b>			
Domestic	40	-	75
<u>International</u>	<u>0</u>	<u>-</u>	<u>30</u>
<b>Total Appreciation/Dividend</b>	<b>45</b>	<b>-</b>	<b>85</b>
<b>Income</b>			
Domestic	10	-	55
<u>International</u>	<u>0</u>	<u>-</u>	<u>30</u>
<b>Total Income</b>	<b>15</b>	<b>-</b>	<b>55</b>
<b>TOTAL PORTFOLIO</b>	<b>100%</b>		

B. The following requirements are applied at the **Manager/Mutual Fund/Asset Class level**:

- i. A Minimum of **20** securities are to be held in a Portfolio or Fund.
- ii. If Soft Dollars are used in the account, a Quarterly report of Soft Dollar usage is required to be delivered to the Component Investment Officer.
- iii. EQUITY MANAGERS
  1. A Maximum of **40%** in any one **sector** UNLESS waived by the Component Investment Officer in writing.
  2. A Maximum of **10%** ownership of shares outstanding of a single Stock.
- iv. FIXED INCOME MANAGERS
  1. For International/Global Fixed Income managers, a Maximum of **40%** in any One Non-US Country.

C. The following requirements are applied at the **Total Portfolio level**:

- i. A Maximum of **20%** of the Total Portfolio may be held in Emerging/Frontier Market securities (Regardless of asset type)
- ii. Excluding Pooled funds, Mutual Funds, or Managed Accounts which are Multi-Strategy and Multi-Manager products, no more than **40%** of the Portfolio may be invested in a **single** Mutual Fund or Manager
- iii. FIXED INCOME
  1. A Maximum of **25%** of the **Fixed Income Portfolio** may be invested below Investment Grade. For definition purposes, Non Rated securities will be considered as Below Investment Grade.

D. PROHIBITED INVESTMENTS AND ACTIVITIES

Investments and activities that are not expressly prohibited in this Appendix are considered allowable by this Policy.

The following are prohibited transactions and securities. Any change in this list shall require amendment of this Policy and adoption by the Board.

- i. TSUS may not directly purchase or sell financial futures, options, interest rate swaps, or forward rate agreements.
- ii. TSUS may not engage in adjusted trading or short sales.

- iii. TSUS may not purchase residual interests in CMOs/REMICs or mortgages servicing rights. Specific securities that may not be purchased are:
  - 1. Inverse CMO floaters
  - 2. Principal only CMOs
  - 3. Interest only CMOs
- iv. TSUS may not purchase 144-A or other private placement securities not registered with the SEC unless such securities have CUSIPs, are daily priced, and are publicly traded over the counter or on a US exchange.
- v. EXCEPTIONS:

Under the advisement of an Investment Consultant as defined by this policy, a component may invest with managers who utilize derivatives, short sales, futures, options, private placements, limited partnerships ,and otherwise prohibited investments and instruments as long as the Endowment is a qualified investor for the product, the investment (as structured) does not expose the Endowment to risk of loss outside the actual invested amount, and the investments are supervised by an investment manager (no direct purchases).

Where possible, fund of funds and pools are vehicles of choice for alternative investments as they can provide for more diversification and additional layers of oversight. These investments, in total cannot comprise more than 20 % of the Endowment Portfolio.

Private Placements are allowed as long as the Endowment meets regulatory qualifications and no single issuer can represent more than 10% of the portfolio, with no single issue representing more than 5% of the portfolio.

EXHIBIT 1  
Texas State University System  
Investment Manager and Broker/Dealer Certification

This certification is executed on behalf of \_\_\_\_\_ (the Investor) and \_\_\_\_\_ (the Investment Manager or Broker/Dealer) as required by the Texas State University System Investment Policy (Investment Policy) in connection with investment transactions conducted between the Investor and the Investment Manager or Broker/Dealer.

The undersigned Qualified Representative of the Investment Manager or Broker/Dealer hereby certifies that:

1. The Investment Manager or Broker/Dealer Qualified Representative is duly authorized to execute this Certification on behalf of the Investment Manager or Broker/Dealer, and
2. The Investment Manager or Broker/Dealer Qualified Representative has received and reviewed the Investment Policy furnished by the Investor, and
3. The Investment Manager or Broker/Dealer will act in accordance with the Investment Policy , and has implemented reasonable procedures and controls in an effort to preclude investment transactions conducted between the Investment Manager or Broker/Dealer and the Investor that are not authorized by the entity's investment policy, except to the extent that this authorization is dependent on an analysis of the makeup of the entity's entire portfolio or requires an interpretation of subjective investment standards.
4. For Investment Managers only—a copy of the most recent ADV and ADV brochure has been provided to the Investor.

Investment Manager or Broker/Dealer **Qualified Representative**

\_\_\_\_\_  
Signature

Name (Printed)

Title

Date

EXHIBIT 2

Texas State University System

Broker/Dealer Questionnaire

Name of Texas State University System Component

Firm:

Date Established:

Main Office:

Representative:

Primary Dealer:

Qualified Historically Underutilized Business?

Seat on the NYSE?

Publicly Traded? Which Exchange?

Member NASD?

SIPC Insured?

Equity Position:

Annual Revenues:

Agency Selling Group Memberships:

Pertinent Rankings:

Representative Public Sector Clients:

Date of Investment Policy:

Date Certification Received by Component: