

SUBJECT: Allowing certain public entities to use investment advisory firms

COMMITTEE: Pensions and Investments — committee substitute recommended

VOTE: 8 ayes — Greenberg, Tillery, Bonnen, Clark, George, Rangel, Salinas, Williams
0 nays
1 absent — Telford

WITNESSES: For — Wayne Halbert, Texas Irrigation Council; Dean Robbins, Texas Water Conversation Association
Against — None
On — Susan Anderson, Public Financial Management, Inc.; Mark Price, County Treasurers Association of Texas; Carol Ann Smith, State Auditor’s Office; Dennis Waley, Government Treasurers of Texas

DIGEST: CSHB 3009 would amend the Government Code to authorize the governing body of a local government, state agency, or a nonprofit corporation acting on behalf of a local government or a state agency to contract with a registered investment advisory firm to invest and manage public funds or other funds under the entities’ control. Investments by the advisory firm would have to comply with the governing board’s investment policies and with the “prudent person” investment standard.

The investment advisory firm would have to be registered under the federal Investment Advisers Act of 1940 or with the State Securities Board. A contract made under this authority could not be for a term longer than two years, and any renewal or extension would have to be made by the governing body of the investing entity by order, ordinance, or resolution.

Investment policy. CSHB 3009 would add conforming language concerning contracts with investment advisory firms to Government Code, sec. 2256.005, which deals with requirements for adoption and disclosure of an investing entity’s investment policies, strategies, and officers. Employees of an

investment advisory firm with which an investing entity had contracted could be considered staff of the investing entity for the purpose of being designated the investment officer. The investing entity's governing body would retain ultimate fiduciary responsibility for the funds managed by the investment advisory firm. The investing entity would have to forward a written copy of its investment policy to an investment advisory firm under contract to invest or manage the investing entity's portfolio.

State audit. CSHB 3009 would require that a state agency arrange for a compliance audit of management controls on investments and adherence to its policies at least once every two years, under procedures and requirements specified by the bill. A state agency that forwarded its investment assets to the state comptroller for investment would not be subject to the state auditing requirements.

Investment training. CSHB 3009 would require the treasurer, chief financial officer, and investment officer of a local government to attend at least eight hours of investment training by an independent source within 12 months of taking office. An individual or business that offered to sell investments to the investing entity would not be considered an independent source. If the local government had assets of less than \$2 million on any day in its fiscal year and if it invested only in U.S. obligations, direct state obligations, or financial instruments such as certificates of deposit or share certificates, or in a local government investment pool meeting certain restrictions, the treasurer, chief financial officer, and investment officer would have to attend only four hours of training once every two years.

CSHB 3009 would add bonds issued, assumed, or guaranteed by the State of Israel to the list of authorized investments for public investing entities and, if applicable, their investment advisors. It would remove the current restriction on investing more than 30 percent of the investing entity's monthly average fund balance in certain money market funds.

This bill would take effect September 1, 1999.

**SUPPORTERS
SAY:**

CSHB 3009 would improve the financial management of public investments by allowing local governments, state agencies, and their agents to contract with experienced investment advisory firms. These firms would be subject to the investment policies and strategies of the investing agency and to the strict

federal requirements for investment advisors. As a result, public funds would be invested prudently and efficiently and would be protected from speculation. Overall, the bill would promote efficiency and would allow state administrative resources that now are directed to managing public funds to be used for more pressing needs. More experienced financial managers could achieve higher yields on public investments for the benefit of all Texans.

The bill would set out specific state auditing requirements for public investments. It would change the reporting time to once every two years to give the investing entity more flexibility in choosing longer-term investments and to reduce the administrative costs of audits. It also would exempt from the auditing requirements smaller investing entities that have their public funds deposited in the state treasury. This exemption would eliminate double audit costs, which can be expensive for smaller entities.

The bill clearly states that ultimate responsibility for the management of public funds would remain with the governing board of the investing entity. The bill would further protect public funds by requiring investment training for local governments' financial officials. This would ensure that these officers receive continuing information on the latest financial instruments and portfolio management and would help these officials make prudent investments.

Investment in bonds issued by the State of Israel previously was approved by the Legislature. The bill would formally authorize the investment of public funds in such investments

**OPPONENTS
SAY:**

CSHB 3009 would authorize the investment of public funds by private investment advisors, which could result in a greater risk of speculative investment. While the governing board of an investing entity ultimately is responsible for the investments, the primary investment decisions would be made by outside advisers. Public funds should be invested by public officials.

CSHB 3009 expressly would authorize investment of public funds in bonds issued, assumed, or guaranteed by the State of Israel. Such designation of a specific country could create a precedent whereby other constituencies would promote the bonds of other countries designated as authorized investment. All

of the other authorized investments in this section are based on financial instruments issued and guaranteed by the U.S. government.

NOTES:

The original bill would have provided only that all state agencies and local governments are subject to Government Code, chapter 2256, relating to public funds investment, unless otherwise exempt, and would have required them to meet requirements of that chapter related to investment and accounting standards and compliance audits.