

MINUTES OF MEETING  
STATE BOARD OF FINANCE

NOVEMBER 10, 2016

A meeting of the State Board of Finance of the State of Arkansas was held in the Conference Room, Office of the Treasurer of State, Suite 275, Victory Building, Little Rock, Arkansas, at 10:00 a.m., Thursday, November 10, 2016, pursuant to notice duly given to each member of the Board by the Chairman.

The following members were present:

Larry Walther, Director, Department of Finance and Administration  
Dennis Milligan, Treasurer of State  
Andrea Lea, Auditor of State  
Edmond Waters, Arkansas Securities Commissioner  
David Bell, Representing Governor Asa Hutchinson  
Susannah Marshall, Representing Candace Franks, Arkansas Bank Commissioner  
Cale Turner, Appointed Member  
Gabe Holmstrom, Appointed Member  
Keith Konecny, Appointed Member  
Al Harkins, Appointed Member

Others present were Jason Brady, Grant Wallace, Autumn Sanson, Ed Garner, Larry Tate, Melissa Corrigan, TJ Fowler, and Celeste Gladden of the Treasurer's staff; Paul Louthian of the Department of Finance and Administration; and Mike Wickline of the Arkansas Democrat Gazette.

Larry Walther served as acting Chairman in the absence of Governor Hutchinson and called the meeting to order with recognition of a quorum.

Minutes of the meeting held on August 4, 2016 were approved as distributed.

Chairman Walther recognized State Treasurer Dennis Milligan to present the Treasury Investment Performance Report for the First Quarter of Fiscal Year 2017. This Report is included in the Minutes as Attachment 1. Treasurer Milligan began by saying that in light of the recent election, he felt even more touched by the importance of public service, and thanked the members of the Board for their service to the state. He stated that he is very pleased to report the continued strength of the

portfolio. He said that in the first quarter of fiscal year 2017, the investment team entered into a new phase of operations. This phase focused on confirming the strategies put in place over the last 20 months. He said that with the Board's guidance and approval, the investment team has restructured the cash flow models, completely turned over the portfolio, entered into new investment areas, and moved from a passive to active investment management style. He stated that he has challenged the team to produce results similar to the past fiscal year, but that the main focus and top priority is to secure the safest investments for the state while maximizing returns. Treasurer Milligan highlighted a few events that occurred in the first quarter: the volatility of the price of oil, the impact of Brexit, and the uncertainty of the election. He reminded the Board that the Treasury entered into the calendar year with the possibility of multiple rate hikes that didn't occur. Treasurer Milligan then pointed the Board to the first slide of the presentation, the short-term portfolio, and said that 4.6 million dollars was receipted in the first quarter of this fiscal year. He said that the team experienced some near-record months in commercial paper, and saw an increase of 2 million dollars in the short-term portfolio compared to the first quarter of last fiscal year. He moved on to the second slide, the long-term, or mortgage backed securities portfolio, and said that in the first quarter 7.2 million was receipted, which is a 2 million dollar increase compared to last year. Treasurer Milligan pointed the Board to the third slide, which shows combined funds generated by both the short-term and the long-term portfolio, where a total of 11.8 million dollars was receipted. He then moved on to the fourth slide, which is a month-by-month comparison of combined totals. He stated that 7.8 million dollars was receipted last year in the first quarter, and this year 11.8 million was receipted for the first quarter, which is an overall increase of 4 million dollars. Treasurer Milligan stated that the final slide gives a historic view of the portfolio. The Treasurer told the Board that with the Governor and the legislature now looking to the office and the Board to produce revenue for matching highway funds and to also fill a long-term reserve account, he understands the enormous responsibility there is support these important initiatives. He stated that the year has started off in the right direction, though there will be

challenges ahead. He then asked Autumn Sanson to come before the Board to make additional comments about the portfolio report.

Ms. Sanson addressed the Board and explained that a large portion of the Treasury portfolio was kept liquid in anticipation of a federal rate hike. She said that this increase is now expected to happen in December, with the hike being priced into the market already, which allowed the team to purchase around 600 million dollars in mortgage backed securities to settle at the end of December. She told the Board that this move is going to reduce liquidity substantially. Ms. Sanson said that the investment team is continuing to look at short-term mortgage backed securities to replace commercial paper. She told the Board that there was a decline in returns, simply due to a large portion of the portfolio being in short-term commercial paper until it was determined that there was more value in making the longer term investments. She said that this has taken the better part of a year because of the distractions of Brexit and the election. She stated that the team feels as though there are more opportunities ahead, and will continue to improve and perform at a high level assisted by the upgrades to the modern investment and analytical software that are taking place in the Treasury. She asked the Board if there were any questions.

Al Harkins asked for the average maturity of the mortgage-back securities being purchased. Ms. Sanson responded that the average was 5-6 years. Mr. Harkins then asked how this would affect the average maturity of the whole portfolio. Ms. Sanson stated that Ed Garner would need to answer that when he arrived to the meeting as he is responsible for the long-term mortgage backed portfolio.

There being no further questions about the report, Chairman Walther asked for a motion from the Board to accept the Investment Performance Report into the record. The motion was made by Keith Konecny and seconded by Susannah Marshall. All members were in favor.

Next, Chairman Walther made a motion to establish that no funds are available for deposit into the State Board of Finance certificate of deposit investment program. The motion was seconded by Al Harkins. All members were in favor.

The Chairman then made a motion that the Board direct the Treasurer of State to purchase warrants for the succeeding quarter, January 1, 2017 – March 31, 2017, pursuant to Act 1088 of 2013, and to keep reasonable amounts in demand deposit accounts and money markets during the next quarter for the transactions of the day to day activities of the State. The motion was seconded by Edmond Waters. All members were in favor.

Chairman Walther then recognized Autumn Sanson to present the next several agenda items. First, the report of new broker/dealers. Ms. Sanson told the Board that the Treasury has two new broker/dealers to add to the approved list: Brean Capital and Citibank. The Chairman asked for a motion to approve. The motion was made by Edmond Waters, seconded by Al Harkins, and all members were in favor.

Next, Ms. Sanson gave an update to the Board regarding the Safekeeping RFQ. She reminded that Board that in the last meeting the Board was informed that the Treasury had outgrown the current safekeeping agent and that an RFQ process had begun to find a new one. She said that the Treasurer's office received four qualified bids, and after carefully analyzing and scoring those firms, the investment team made a recommendation to the Treasurer who approved and accepted Bank of America's bid. She said that the office is currently working with on a contract with Bank of America and hopes to be operational by no later than January 1<sup>st</sup>, 2017.

The Chairman then asked Ms. Sanson for an update on proposed legislation for repurchase agreements and the ROI distribution date change, which is the next agenda item. She reminded the Board that in the last meeting, the Board approved proposed legislation to help clarify statute tied to the future opportunities to invest in repurchase agreements. She stated that, also, because of the way mortgage backed securities pay, the Treasurer's office received approval to change the date of the ROI distribution, eliminating the need for a monthly true-up and second distribution after monthly MBS factors are published. She told the Board that Senator Bruce Maloch had Bureau of Legislative Research put those requests into legislative draft form. Ms. Sanson stated that since then, internally it

has been discussed that the calculation of the return on investment needs to reflect the daily balance of each interest bearing fund. She said that the investment team will also be making be making that technical change in the legislation as well. She explained that by modernizing the distributions, earnings will be more accurately reported. Ms. Sanson told the board that the investment team is currently working closely with the Worker's Compensation Commission, the Tobacco Settlement Commission, and the Arkansas Development Finance Authority to provide rates that are above and beyond what has been provided in years past, however the Treasury cannot keep up with the demand without the upgrades in the investment and analytical software that is taking place.

Chairman Walther asked the Board if there were any questions regarding these two updates. There were not. The Chairman then recognized Ms. Sanson again to go over the final agenda item, a report on the Money Management Trust Fund.

Ms. Sanson began by reviewing the information that the Board was sent prior to the meeting. This information is included in the Minutes as Attachment 2. She told the Board that the State Treasury Money Management Trust Fund was established in 1997 as a vehicle to be used by state agencies, county governments, municipalities, and school districts for enhancing investment opportunities and earnings of idle cash funds. She said that cash managers who may have been limited by small amounts of funds available for investment or by complexities of today's investment environment can take advantage of the volume and expertise of the State Treasury. She explained that Act 1179 of 1997 provides authorization for various entities to invest in the fund: state agencies may invest cash funds; any city, county, school district, or community college may invest; any department, instrumentality or agency of these entities; and the State Treasury may invest in the Money Management Trust Fund. Ms. Sanson continued by saying that the investment team is requesting approval for proposed legislation that will affect the fund. The first change would mimic the changes being proposed in Treasury law, concerning the date of distribution and the method of calculating the ROI. The next change involves the clarification of fees. She explained that the Money Management

Trust Fund currently has an investment policy, approved by the State Board of Finance, that allows charges to be assessed for expenses and management. The word “fees” would be added to the wording of the statute. In addition, fees would be set by the State Board of Finance and not the Treasurer’s office. Ms. Sanson told the Board that other state treasuries were polled through the National Association of State Treasurers to see how many charged fees and how much was charged, and the consensus was 5 basis points. She said that based on these results, the investment team is asking the Board to approve those same fees for the pool and asking that an interest bearing Treasury fund be established for those proceeds to be used specifically for data processing and operations. Ms. Sanson stated that the last clarification that needs addressed is the title of the fund. She said that there is a discrepancy throughout the Act as to the title and there needs to be consistency. She asked the Board if there were any questions.

Several questions were asked and answered regarding the operation of the fund, current participation in the fund, and balance of the fund. After some discussion, it was asked why four-year colleges and universities are not included in the list of eligible participants. Some discussion took place as to why this may have occurred. Chairman Walther recommended that while drafting proposed legislation that some attention should be given to this issue, so as not to prohibit these entities from participating. The Chairman then proposed that the Board give the Treasurer’s office approval to move forward with legislation and for it to be presented to the legislature at the appropriate time. Auditor Lea commented that she felt the legislation is good but expressed some discomfort in approving legislation she had not seen yet, and that she would like to see a final draft once it is available. Jason Brady then addressed the Board and stated that the proposed legislation is in the preliminary stages, and that the Treasurer’s office is looking for the Board to give permission for the language to be drafted. Chairman Walther asked for a motion of support for the Treasurer’s office to pursue legislation, and once it is drafted it should be provided it to the Board of Finance members. The motion was made by Keith Konecny and seconded by Andrea Lea. All members were in favor.

The Chairman asked for any other business to come before the Board. Ms. Sanson stated that since Ed Garner has arrived to the meeting, he could answer the question earlier posed by Mr. Al Harkins, regarding the average life of the Treasury portfolio. Mr. Garner responded that about 3.5-4.5 years is the average life at the projected payment speeds. He stated that this range is the best performing part of the yield curve in the current market environment.

There was no further business. Chairman Walther informed the Board that the next meeting will be February 9<sup>th</sup> and 10 a.m. The meeting was then adjourned.

ATTEST:

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Secretary of the State Board  
of Finance of the State of Arkansas

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Acting Chairman of the State Board  
of Finance of the State of Arkansas

Secretary's Note: All documents pertaining to the issues considered are filed in the permanent records of the State Board of Finance.