2011 PFIA Legislative Changes

**HB 2226**
Numerous PFIA clarifications and changes. Effective immediately.

**HB 2346**
Authorize a port or navigation district to purchase, sell, and invest its funds and funds under its control in negotiable certificates of deposit. Effective September 1, 2011

**SB 1543**
Authorizes some independent school districts to purchase, sell, and invest its funds and funds under its control in corporate bonds with restrictions. Effective September 1, 2011

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**HB 2226**

SECTION 1. Section 2256.005(b), Government Code, is amended to read as follows:

(b) The investment policies must:
(4) include:

(F) procedures to monitor rating changes in investments acquired with public funds and the liquidation of such investments consistent with the provisions of Section 2256.021.

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**Analysis:**
- May require Investment Policy modification to establish credit rating monitoring procedures. Affected Obligations include:
  - Obligations of States (other than Texas), Agencies, Counties, Cities and Other Political Subdivisions [Section 2256.009(a)(5)]
    - Rated not less than A or its equivalent by at least one nationally recognized investment rating firm
  - Bankers’ Acceptances (Section 2256.012)
    - Accepted by a bank rated not less than A-1 or P-1 or an equivalent rating by at least one nationally recognized rating agency
  - Commercial Paper (Section 2256.013)
    - Rated not less than A-1 or P-1 or an equivalent by at least two nationally recognized rating agencies, or; Rated not less than A-1 or P-1 or an equivalent by one nationally recognized rating agency plus fully secured by an irrevocable letter of credit issued by a domestic bank
  - Mutual Fund [Section 2256.014 (b) and (c)]
    - Rated not less than AAA or its equivalent by at least one nationally recognized investment rating firm
    - Money Market Mutual Funds (MMMFs) are not required to be rated.
  - Investment Pools [Section 2256.016]
    - Rated not less than AAA or an equivalent rating by at least one nationally recognized rating service.
SECTION 2. Section 2256.007(d), Government Code, is amended to read as follows:

(d) An investment officer shall attend a training session not less than once each state fiscal biennium [in a two-year period] and may receive training from any independent source approved by the governing body of the state agency.

Analysis:
- Clarifies the two year training cycle start and end dates.
- Includes State Agencies, Institutions of Higher Education including Community Colleges.

SECTION 3. Sections 2256.008(a) and (b), Government Code, are amended to read as follows:

(a) Except as provided by Subsections (b) and (e), the treasurer, the chief financial officer if the treasurer is not the chief financial officer, and the investment officer of a local government shall:

(2) except as provided by Subsections (b) and (e), attend an investment training session not less than once in a two-year period that begins on the first day of that local government’s fiscal year and consists of the two consecutive fiscal years after that date, and receive not less than 10 hours of instruction relating to investment responsibilities under this subchapter from an independent source approved by the governing body of the local government or a designated investment committee advising the investment officer as provided for in the investment policy of the local government.

(b) An investing entity created under authority of Section 52(b), Article III, or Section 59, Article XVI, Texas Constitution, that has contracted with an investment management firm under Section 2256.003(b) and has fewer than five full-time employees or an investing entity that has contracted with another investing entity to invest the entity's funds may satisfy the training requirement provided by Subsection (a)(2) by having an officer of the governing body attend four hours of appropriate instruction in a two-year period that begins on the first day of that local government’s fiscal year and consists of the two consecutive fiscal years after that date.

Analysis:
- Clarifies that the local government and water district two year training cycle begins on the first day of that government’s fiscal year.
- This change is intended to make the monitoring process easier for the entity and coincides with their budget period when allocating funds for training.

SECTION 4. Section 2256.009(a), Government Code, is amended to read as follows:

(a) Except as provided by Subsection (b), the following are authorized investments under this subchapter:

(4) other obligations, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, this state or the United States or their respective agencies and instrumentalities, including obligations that are fully guaranteed or insured by the Federal Deposit Insurance Corporation or by the explicit full faith and credit of the United States;

Analysis:
- Clarifies that obligations that are fully guaranteed or insured by the Federal Deposit Insurance Corporation or have the explicit full faith and credit of the United States are allowed investments.
SECTION 5. Section 2256.010(b), Government Code, is amended to read as follows:

(b) In addition to the authority to invest funds in certificates of deposit under Subsection (a), an investment in certificates of deposit made in accordance with the following conditions is an authorized investment under this subchapter:

1. the funds are invested by an investing entity through:
   A. a broker that has its main office or a branch office in this state and is selected from a list adopted by the investing entity as required by Section 2256.025; or
2. the broker or the depository institution selected by the investing entity under Subdivision (1) arranges for the deposit of the funds in certificates of deposit in one or more federally insured depository institutions, wherever located, for the account of the investing entity;
3. the investing entity appoints the depository institution selected by the investing entity under Subdivision (1), an entity described by Section 2257.041(d), or a clearing broker-dealer registered with the Securities and Exchange Commission and operating pursuant to Securities and Exchange Commission Rule 15c3-3 (17 C.F.R. Section 240.15c3-3) [acts] as custodian for the investing entity with respect to the certificates of deposit issued for the account of the investing entity; and
4. at the same time that the funds are deposited and the certificates of deposit are issued for the account of the investing entity, the depository institution selected by the investing entity under Subdivision (1) receives an amount of deposits from customers of other federally insured depository institutions, wherever located, that is equal to or greater than the amount of the funds invested by the investing entity through the depository institution selected under Subdivision (1).

Analysis:
- Expands the sources of CDARS-type deposits by: (may require investment policy modification)
- Allowing investments through a Broker that has a main or branch office in this state and is on the qualified broker/dealer list approved by the governing body, and meets specific registration requirements.
- Reciprocal deposit language has been removed.

SECTION 6. Section 2256.011(a), Government Code, is amended to read as follows:

(a) A fully collateralized repurchase agreement is an authorized investment under this subchapter if the repurchase agreement:
1. has a defined termination date;
2. is secured by a combination of cash and obligations described by Section 2256.009(a)(1); and
3. requires the securities being purchased by the entity or cash held by the entity to be pledged to the entity, held in the entity's name, and deposited at the time the investment is made with the entity or with a third party selected and approved by the entity; and

Analysis:
- Clarifies that “cash” is eligible in combination with obligations described by Section 2256.009(a)(1) to secure a repurchase agreement. (May require investment policy modification). Language as previously written was an operational restriction to many repurchase agreement providers. This change will facilitate broader participation from investor community when governmental entities are looking to enter into a flexible repurchase agreement.
SECTION 7. Section 2256.016, Government Code, is amended by amending Subsections (a), (c), and (f) and adding Subsections (i), (j), and (k) to read as follows:

(a) An entity may invest its funds and funds under its control through an eligible investment pool if the governing body of the entity by rule, order, ordinance, or resolution, as appropriate, authorizes investment in the particular pool. An investment pool shall invest the funds it receives from entities in authorized investments permitted by this subchapter. An investment pool may invest its funds in money market mutual funds to the extent permitted by and consistent with this subchapter and the investment policies and objectives adopted by the investment pool.

(c) To maintain eligibility to receive funds from and invest funds on behalf of an entity under this chapter, an investment pool must furnish to the investment officer or other authorized representative of the entity:

(I) the yield and expense ratio of the pool, including a statement regarding how yield is calculated;

(f) To be eligible to receive funds from and invest funds on behalf of an entity under this chapter, a public funds investment pool created to function as a money market mutual fund must mark its portfolio to market daily, and, to the extent reasonably possible, stabilize at a $1 net asset value. If the ratio of the market value of the portfolio divided by the book value of the portfolio is less than 0.995 or greater than 1.005, portfolio holdings shall be sold as necessary to maintain the ratio between 0.995 and 1.005. In addition to the requirements of its investment policy and any other forms of reporting, a public funds investment pool created to function as a money market mutual fund shall report yield to its investors in accordance with regulations of the federal Securities and Exchange Commission applicable to reporting by money market funds.

(j) If the investment pool operates an Internet website, the information in a disclosure instrument or report described in Subsections (b), (c)(2), and (f) must be posted on the website.

(k) If an investment pool offers fee breakpoints based on fund balances invested, the investment pool in advertising investment rates must include either all levels of return based on the breakpoints provided or state the lowest possible level of return based on the smallest level of funds invested.

Analysis:
- Clarifies and expands specific investment pool requirements. (May require investment policy modification).
- Clarifies that pools can only use money market mutual funds whose authorized investments are consistent with their own investment policy and authorized investments.
- Money market mutual funds are eligible investments for investment pools.
- Investment pools must include a statement on how yield is calculated.
- Investment pools functioning as a MMMF must report yield in accordance with SEC regulations.
- If the investment pool operates a website it must provide all information required in the offering circular 2256.016(b), monthly newsletter 2256.016(c)(2), and standardized SEC 7 day net yield 2256.016(f) on their website.
- Investment pools must provide an annual audited financial statement.
- Investment pools must disclose fee breakpoints or state the lowest possible level of return based on the smallest level of funds invested.
SECTION 8. Section 2256.019, Government Code, is amended to read as follows:

Sec. 2256.019. RATING OF CERTAIN INVESTMENT POOLS. A public funds investment pool must be continuously rated no lower than AAA or AAA-m or at an equivalent rating by at least one nationally recognized rating service [or no lower than investment grade by at least one nationally recognized rating service with a weighted average maturity no greater than 90 days].

Analysis:
- Removes the “Investment Grade” pool language in 2256.019 to make it consistent with 2256.016 (h). It does not impact any active or current pool.

SECTION 9. Section 2256.023(b), Government Code, is amended to read as follows:

(b) The report must:

(4) contain a summary statement[, prepared in compliance with generally accepted accounting principles,] of each pooled fund group that states the:

(A) beginning market value for the reporting period;

(B) additions and changes to the market value during the period;

(5) state the book value and market value of each separately invested asset at the [beginning and] end of the reporting period by the type of asset and fund type invested;

Analysis:
- Clarifies specific investment report requirements. May require investment pool modification).
- Removes GAAP language due to accounting issues with interim (quarterly) statement
- Removes addition and changes to market value due to appearances of gains and losses.

HB 2346

SECTION 1. Subchapter A, Chapter 2256, Government Code, is amended by adding Section 2256.0203 to read as follows:

Sec. 2256.0203. AUTHORIZED INVESTMENTS: PORTS AND NAVIGATION DISTRICTS. (a) In this section, "district" means a navigation district organized under Section 52, Article III, or Section 59, Article XVI, Texas Constitution. (b) In addition to the authorized investments permitted by this subchapter, a port or district may purchase, sell, and invest its funds and funds under its control in negotiable certificates of deposit issued by a bank that has a certificate of deposit rating of at least 1 or the equivalent by a nationally recognized credit rating agency or that is associated with a holding company having a commercial paper rating of at least A-1, P-1, or the equivalent by a nationally recognized credit rating agency.

Analysis:
- Expands investment options for Ports and Navigation Districts. (Will require investment policy modification) and may conflict with the Public Funds Collateral Act.
- Ports and Navigation Districts may purchase negotiable certificated of deposit with rating criteria.
SECTION 1. Subchapter A, Chapter 2256, Government Code, is amended by adding Section 2256.0204 to read as follows:

Sec. 2256.0204. AUTHORIZED INVESTMENTS: INDEPENDENT SCHOOL DISTRICTS.

(a) In this section, "corporate bond" means a senior secured debt obligation issued by a domestic business entity and rated not lower than "AA-" or the equivalent by a nationally recognized investment rating firm. The term does not include a debt obligation that:

(1) on conversion, would result in the holder becoming a stockholder or shareholder in the entity, or any affiliate or subsidiary of the entity, that issued the debt obligation; or

(2) is an unsecured debt obligation.

(b) This section applies only to an independent school district that qualifies as an issuer as defined by Section 1371.001.

(c) In addition to authorized investments permitted by this subchapter, an independent school district subject to this section may purchase, sell, and invest its funds and funds under its control in corporate bonds that, at the time of purchase, are rated by a nationally recognized investment rating firm "AA-" or the equivalent and have a stated final maturity that is not later than the third anniversary of the date the corporate bonds were purchased.

(d) An independent school district subject to this section is not authorized by this section to:

(1) invest in the aggregate more than 15 percent of its monthly average fund balance, excluding bond proceeds, reserves, and other funds held for the payment of debt service, in corporate bonds; or

(2) invest more than 25 percent of the funds invested in corporate bonds in any one domestic business entity, including subsidiaries and affiliates of the entity.

(e) An independent school district subject to this section may purchase, sell, and invest its funds and funds under its control in corporate bonds if the governing body of the district:

(1) amends its investment policy to authorize corporate bonds as an eligible investment;
(2) adopts procedures to provide for:
   (A) monitoring rating changes in corporate bonds acquired with public funds; and
   (B) liquidating the investment in corporate bonds; and
(3) identifies the funds eligible to be invested in corporate bonds.

(f) The investment officer of an independent school district, acting on behalf of the district, shall sell corporate bonds in which the district has invested its funds not later than the seventh day after the date a nationally recognized investment rating firm:
   (1) issues a release that places the corporate bonds or the domestic business entity that issued the corporate bonds on negative credit watch or the equivalent, if the corporate bonds are rated "AA-" or the equivalent at the time the release is issued; or
   (2) changes the rating on the corporate bonds to a rating lower than "AA-" or the equivalent.

(g) Corporate bonds are not an eligible investment for a public funds investment pool.

Analysis:
- Establishes specific criteria for the investment in corporate bonds. May impact eligible collateral in the Public Funds Investment Act.
- Minimum rating of at least AA- or the equivalent
- Stated final maturity less than or equal to 3 years from the purchase date.
- Limited to invest up to 15% of its monthly average fund balance, excluding bond proceeds, reserves and debt service funds.
- Restricts investment of less than or equal to 25% of the corporate bond portion of the investment portfolio in any one issuer.
- Requires timely liquidation if issuer is placed on negative credit watch or losses the minimum credit rating.
- Investment pools are not allowed to invest in corporate bonds.