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Thomas P. German, *Executive Secretary*

## AGENDA

October 4, 2022  
2:00 P.M.

Board of Commissioners of Public Lands  
101 E. Wilson Street, 2<sup>nd</sup> Floor  
Madison, Wisconsin

### Routine Business:

1. Call to Order
2. Approve Minutes – September 20, 2022 (Attachment)
3. Approve Loans

### Old Business:

4. None

### New Business:

5. Investment Policy changes
6. Carbon Credits

### Routine Business:

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

## AUDIO ACCESS INFORMATION

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Conference Line Number: **(608) 571-2209**  
Conference ID Code: **790 694 843#**

Board Meeting  
Minutes  
September 20, 2022

Present were:

- |                                           |                                        |
|-------------------------------------------|----------------------------------------|
| Sarah Godlewski, Board Chair              | State Treasurer                        |
| Doug LaFollette, Commissioner             | Secretary of State                     |
| Josh Kaul, Commissioner                   | Attorney General                       |
| Tom German, Executive Secretary           | Board of Commissioners of Public Lands |
| Richard Sneider, Chief Investment Officer | Board of Commissioners of Public Lands |
| Denise Nechvatal, Senior Accountant       | Board of Commissioners of Public Lands |
| Mike Krueger, IT Manager                  | Board of Commissioners of Public Lands |
| Thuy Nguyen, Office Manager               | Board of Commissioners of Public Lands |
| Emma Stutzman, Chief of Staff             | State Treasurer                        |

**ITEM 1. CALL TO ORDER**

Board Chair Godlewski called the meeting to order at 2:01 p.m.

**ITEM 2. APPROVE MINUTES – September 13, 2022**

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

**DISCUSSION:** None

**VOTE:** The motion passed 3-0.

**ITEM 3. APPROVE LOANS**

**MOTION:** Commissioner LaFollette moved to approve the loans; Commissioner Kaul seconded the motion.

**DISCUSSION:** Mr. Sneider commented that these are all typical loans. He pointed out that the loan to the City of Cedarburg for financing some business park infrastructure within their tax incremental district. BCPL has been receiving applications for some larger loans recently and those will be presented to the board over the next couple months.

**VOTE:** The motion passed 3-0

The Board of Commissioners of Public Lands (BCPL) unanimously approved **\$1,175,000.00** in State Trust Fund Loans to support **3** community projects in Wisconsin.

1. City of Amery / Polk County / Finance purchase of fire truck / \$320,000.00
2. City of Cedarburg / Ozaukee County / Finance purchase of DPW dump truck / \$240,000.00
3. City of Cedarburg / Ozaukee County / Finance TID Business Park Infrastructure / \$615,000.00

**ITEM 4. OLD BUSINESS**

None

## **NEW BUSINESS**

### **ITEM 5. MINOCQUA, PIER LAKE, CEDAR-40, ONEIDA COUNTY – SALE**

Executive Secretary German explained that this property is comprised of approximately 40 isolated acres which are completely surrounded by private land. There is no public access to the property and we do not anticipate being able to acquire public access in the foreseeable future. The property has some nice natural areas but staff has been unable to find any conservation party interested in acquiring the property for conservation efforts or a conservation easement. The best option is to put up the property up for sale as the owner of the surrounding property has indicated a willingness to submit a sealed bid to purchase the property.

Commissioner LaFollette inquired about logging on the land and the condition of the land.

Executive Secretary German commented that the land is mostly lowland and the timber on the property has relatively low value so it makes sense to sell the land.

### **ITEM 6. SUGAR CAMP, THUNDER LAKE ROAD-NORTH, ONEIDA COUNTY - SALE and**

### **ITEM 7. SUGAR CAMP, THUNDER LAKE ROAD-SOUTH, ONEIDA COUNTY – SALE**

Executive Secretary German described the Thunder Lake Road properties as bisected by Thunder Lake Road. Therefore, both properties have direct town road access and are suitable for residential development as other homes have been built in the area. While we do have other holdings in the general area, those other holdings are not contiguous and a considerable distance away. We are proposing to sell these properties separately because we're anticipating that will result in higher overall sales proceeds. The south property is on higher ground so it appraised higher than the other.

Commissioner LaFollette asked about potential buyers for the Thunder Lake Road properties and clarification on the motion to be made.

Executive Secretary German shared that there are several people interested in buying the properties so there will be competitive bidding. If the board approves the staff proposals, the properties listed as items five, six and seven will be sold via sealed bid auction. For item five, it's likely only the surrounding landowner will bid on it. For items six and seven, we anticipate several bids.

Executive Secretary German asked the board to authorize the sale resolution in the board packet for items five, six and seven to be offered for sale via sealed bid sale at minimum acceptable bid of the appraised value.

**MOTION:** Commissioner Kaul moved to approve the resolutions for the sale of items five, six and seven; Board Chair Godlewski seconded the motion.

**VOTE:** The motion passed 3-0

### **ITEM 8. LAC DU FLAMBEAU, VILAS AND IRON COUNTIES – SALE**

The Lac du Flambeau Tribe has requested to purchase the school trust lands identified in items 8 and 9. The Tribe is using federal money for this transaction. The federal fiscal year ends on September 30<sup>th</sup> so, the tribe must enter into a binding agreement prior to that date in order to encumber the funds and prevent such funds from lapsing at the end of the fiscal year.

Executive Secretary German explained that he has split the Lac du Flambeau transaction into two different pieces. The first part of it is strictly a land sale and the second part is the settlement of conflicting claims to a particular parcel.

Because the settlement of claims will require the board to engage in discussion about legal claims, he has requested that discussion be held in closed session.

Executive Secretary German described the sale of land to the Lac du Flambeau tribe. BCPL and the tribe have had differences of opinion over the years in terms of who owns what in this area. Staff has worked with a local title company and the tribe to verify BCPL's ownership claims on the 886 acres and everyone has come to agreement on that. These properties are still within our consolidation zone and some of the parcels are productive timberland. However, the tribe believes that those parcels are required for tribal use, and BCPL staff agree that it makes sense to sell those parcels to the tribe. Please note that there are three separate appraisal certifications. This is because the appraiser felt that blocks of the parcels of land making up the 886 acres were distinct enough to warrant separate appraisal analyses. These lands are contiguous with lands the tribe currently owns and the parcel in the southwestern corner also abuts DNR land. Staff supports the sale of these lands to the tribe equal to the appraised value.

## **ITEM 9. LAC DU FLAMBEAU COMMISSIONER ORDER – CLOSED SESSION**

**CLOSED SESSION 2:24 pm to 2:48 pm**

**RECONVENE IN OPEN SESSION 2:49 pm**

**MOTION (Approve Item 8):** Board Chair Godlewski moved to approve the land sale resolution in board item eight (first paragraph of proposed board resolution), Commissioner Kaul seconded the motion.

**VOTE (Approve Item 8):** Motion passed 3-0 (Clarification needed. Motion needs to be restated)

**DISCUSSION:** Discussion is had about the motion made and the resolution.

Board Chair Godlewski clarified that her motion was solely to approve the proposed land sale.

Commissioner Kaul explained that in order for the sale to be done we must release the claims pertaining to item nine. Items eight and nine go hand in hand.

Board Chair Godlewski explained that the transactions were described as two separate transactions but they are actually happening together and the resolution is written with two separate paragraphs representing each part of the transaction. Commissioner Kaul requested to amend the second resolution paragraph. Commissioner LaFollette asked for further clarification on the finality of the sale.

Executive Secretary German commented that the resolutions are a step in the process. Passing the resolution authorizes staff to move forward to set up the transaction. No land changes hands until the land patents are properly executed and money is received by BCPL.

Commissioner LaFollette shared his desire to follow through with the sale to ensure the tribe has ownership of those lands.

Commissioner Kaul commented that the sale is dependent on the release of claims.

Commissioner LaFollette shared his concerns about a potential delay in the transaction could have a negative impact on the tribe.

Board Chair Godlewski stated that the resolution set forth in the first paragraph of board item number eight has now been approved. She shared that the timeline the tribe has set is incredibly important. The tribe needs the transaction completed by the end of September. While the timeline is important, she wants to make sure we are upholding legal requirements, as Commissioner Kaul had brought up.

Executive Secretary German explained that his intention was to discuss items eight and nine separately but have one document that addressed both of them together. The resolution was drafted in an effort to provide a seamless narrative for the board to follow. Both pieces of the resolution could be approved together however, Commissioner Kaul asked that the second paragraph in the resolution be amended to direct the Executive Secretary to work with the Wisconsin Department of Justice to ensure legal compliance. So, in essence, it could all be approved together with that friendly amendment.

Commissioner Kaul suggested that since item eight had already been approved, the board could amend item 9 and approve the resolution set forth in the second paragraph as modified by his requested friendly amendment.

**OFFICIAL VOTE (Approve Item 8):** Motion passed 2-0 (Commissioner LaFollette abstained)

**MOTION (Amend Item 9):** Commissioner Kaul moved to amend agenda item nine (the resolution set forth in the second paragraph of board item 8) to indicate that the release of claims should be done by BCPL staff working in coordination with the Department of Justice staff to ensure legal compliance; Board Chair Godlewski seconded the motion.

**MOTION (Approve Item 9):** Board Chair Godlewski moved to approve the resolution to agenda item 9 as amended by Commissioner Kaul; Commissioner Kaul seconded the motion.

**VOTE:** Motion passed 2-0 (Commissioner LaFollette abstained)

#### **ITEM 10. CHIEF INVESTMENT OFFICER'S REPORT**

None

#### **ITEM 11. EXECUTIVE SECRETARY'S REPORT**

None

#### **ITEM 12. BOARD CHAIR'S REPORT**

None

#### **ITEM 13. FUTURE AGENDA ITEMS**

None

#### **ITEM 14. ADJOURN**

Board Chair Godlewski moved to adjourn the meeting; Commissioner LaFollette seconded the motion. The motion passed 3-0; the meeting adjourned at 3:03 p.m.



Thomas P. German, Executive Secretary

Link to audio recording:

<https://bcpl.wisconsin.gov/Shared Documents/Board Meeting Docs/2022/2022-09-20 BoardMtgRecording.mp3>

**BOARD MEETING  
OCTOBER 4, 2022**

**AGENDA ITEM 3  
APPROVE LOANS**

Municipality	Municipal Type	Loan Type	Loan Amount
1. New Berlin Waukesha County Application #: 02023023 Purpose: Finance Phase II of Recreation Facility	City Rate: 4.50% Term: 2 years	General Obligation	\$13,970,000.00
2. Jump River Taylor County Application #: 02023024 Purpose: Finance roadwork	Town Rate: 4.50% Term: 4 years	General Obligation	\$62,312.40
3. Big Round Lake Pro & Rehab Dis Polk County Application #: 02023025 Purpose: Finance alum treatment	Lake District Rate: 4.75% Term: 20 years	General Obligation	\$1,800,000.00
	<b>TOTAL</b>		<hr/> <b>\$15,832,312.40</b>

**BOARD MEETING  
OCTOBER 4, 2022**

**AGENDA ITEM #5  
PROPOSED CHANGES TO BCPL IPS**

**RECITALS**

- A. The Board of Commissioners of Public Lands initially adopted an Investment Policy Statement (“IPS”) on November 1, 2016 which governed the investment of the school trust fund assets that are managed by BCPL and provided respective asset allocations to diversify such trust fund investments.
- B. The IPS required BCPL to regularly review the IPS and adopt changes appropriate to the current circumstances and market conditions.
- C. At the outset of implementing the IPS, BCPL’s trust assets were invested primarily in fixed income instruments and the IPS provided guidance for the transition of the portfolios from fixed income concentration to diversified portfolios. BCPL has now diversified its trust fund portfolios appropriately.
- D. The time has come to again review the IPS and asset allocations for the respective trust funds and BCPL staff and the BCPL investment committee have proposed changes to the IPS and asset allocations. A short summary of the material proposed changes is attached here as Exhibit A.
- E. BCPL staff and the BCPL Investment Committee recommend that the Board adopt the changes to the IPS which are highlighted (redlined) on attached Exhibit B.

**NOW, THEREFORE BE IT RESOLVED**, that the Board of Commissioners of Public Lands approves the proposed changes to the Investment Policy Statement and respective asset allocations as set forth on the attached Exhibit B. Such changes shall become effective on this date.

*Attachments:*

*Exhibit A – Summary of proposed changes*

*Exhibit B - Investment Policy Statements (redlined)*

# Exhibit A

## Summary of Recommended Changes to BCPL Investment Policies October 4, 2022

### Executive Summary

BCPL Investment Guidelines and Investment Policy Statements (IPS) contain a scheduled requirement for formal review of the IPS every two (2) years, and a review of the asset allocation policy every year.

The IPS was last modified on May 4, 2021. The summary below includes all substantive changes recommended by the BCPL Investment Committee (IC) for Board approval.

Recommendations to the IPS include expanding the authority of the IC to develop and implement an on-going program to sell State Trust Fund Loans (STFLs). This program will be designed to strengthen the STFL program and improve staff ability to manage the investment portfolios. Selling STFLs provides staff with an alternative to restricting the availability of STFLs during times when cash available for investment is insufficient to meet loan demand.

The asset allocation policy has been under review by the IC since the beginning of 2021, and this summary includes recommended adjustments to the target asset allocation models for both the Common School Fund and Normal School Fund. These adjustments were refined with the assistance of BlackRock following studies detailing projected risk-adjusted rates of return and the stability of future income distributions of BCPL-managed portfolios.

### Loan Sale Program (Pages 9-10)

There have been many occasions in past years when cash available for investment was considered inadequate to meet current loan demand. During these times, BCPL restricted the availability of STFLs in both the size and number of loans that any borrower could obtain from BCPL. These restrictions harmed the program by introducing on-going uncertainties regarding loan availability. Statutes were added more than 30 years ago to allow BCPL to sell STFLs in order to address these issues.

Potential benefits from creating a program that packages and sells loans to other investors include:

1. The STFL program would be strengthened through continuity. Loans of all sizes would always be available to our borrowers, even if there was a spike in loan demand when the cash available for new investment was low.
2. Selling loans would provide BCPL staff with additional flexibility in the management of Trust financial 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



3. Selling loans provides an opportunity to increase distributable income through servicing fees charged to investors that purchase STFLs. It is critical that Borrowers would perceive no change in the program, and all loan servicing (including all written and other communications, payment processing, etc.) would continue to be done by BCPL staff. BCPL would charge a fee to loan purchasers for collecting and remitting loan payments and other services.
4. Proceeds from loan sales could be reinvested in new loans or other investments.

**The following language has been inserted on pages 9-10 of the amended IPS:**

“Upon prior approval from the Board of the general outline of the proposed structure of the sale of Trust Fund Loans, the Investment Committee is authorized to develop and execute an on-going program to sell Trust Fund Loans. This program shall be designed to maintain and improve the strength and resilience of the State Trust Fund Loan Program, increase distributable income earned by the Trust Funds, and improve the ability to manage portfolio assets in accordance with approved Strategic Asset Allocations.”

**Legacy Portfolios** (former pages 7-10, 13, 19, 28-29)

Due to declining relevance over time, language regarding our transition from legacy portfolios that contained only fixed-income assets has been removed. Historic asset allocation tables have also been removed to simplify the document and focus on current and future timeframes.

**Land Management** (pages 11-12)

Added language provided by the BCPL Senior Forester regarding land management strategies.

**Inflation** (pages 23-24, 29)

Updated inflation data within both the CSF and NSF sections, which clarified the divergence of CPI - Educational Books and Supplies (CSF) and CPI - Education (NSF) with the standard measure of CPI. Long-term annual inflation assumptions were maintained at 4%.

**Asset Classes** (pages 26, 31)

Added Preferred Stock asset class to domestic equities.

Removed the term ‘Real Assets’ from the Asset Class Real Assets/Infrastructure.

**Portfolio Constraints** (page 30)

Added NSF constraint regarding fund size.

**Changes to Target Asset Allocations:**

See following pages, with all changes shown in **RED**.

## Common School Fund Target Asset Allocations

Asset Class	Target Allocation (old)	Target Allocation (new)	Range (old)	Range (new)
Public Debt				
State/State Agency/Municipal Bonds	5%	5%	0% to 30%	0% to <b>20%</b>
U.S. Treasury/Agency Bonds	0%	0%	0% to 30%	0% to <b>20%</b>
U.S. Treasury Inflation Protected	0%	0%	0% to 10%	0% to 10%
Corporate Bonds	10%	<b>5%</b>	0% to 30%	0% to <b>20%</b>
Private Debt				
BCPL State Trust Fund Loans	30%	<b>25%</b>	20% to 50%	<b>10% to 30%</b>
Other Private Debt	10%	<b>15%</b>	0% to 20%	<b>10% to 30%</b>
<b>Total Fixed Income</b>	55%	<b>50%</b>		
Public Equities				
Preferred Equities	n/a	<b>5.0%</b>	n/a	<b>0% to 10%</b>
Domestic Equities	7.5%	7.5%	5% to 30%	5% to <b>20%</b>
Global Equities	7.5%	7.5%	5% to 20%	5% to 20%
Alternatives				
Private Real Estate	20%	20%	5% to 25%	<b>10% to 30%</b>
Infrastructure	5%	<b>4%</b>	0% to 10%	0% to 10%
Private Equity/Venture Capital	5%	<b>4%</b>	0% to 10%	0% to 10%
<b>Total Equities and Alternatives</b>	45%	<b>48%</b>		
<b>Cash</b>	0%	<b>2%</b>	0% to 10%	0% to 10%

## Normal School Fund Target Asset Allocations

Asset Class	Target Allocation (old)	Target Allocation (new)	Range (old)	Range (new)
Public Debt				
State/State Agency/Municipal Bonds	0%	0%	0% to 20%	0% to 20%
U.S. Treasury/Agency Bonds	0%	0%	0% to 20%	0% to 20%
U.S. Treasury Inflation Protected	0%	0%	0% to 10%	0% to 10%
Corporate Bonds	0%	0%	0% to 10%	0% to <b>20%</b>
Private Debt				
BCPL State Trust Fund Loans	30%	<b>0%</b>	20% to 40%	<b>0% to 20%</b>
Other Private Debt	0%	<b>35%</b>	0% to 10%	<b>10% to 50%</b>
<b>Total Fixed Income</b>	<b>30%</b>	<b>35%</b>		
Public Equities				
Preferred Equities	n/a	<b>5%</b>	n/a	0% to 10%
Domestic Equities	15%	<b>10%</b>	10% to 30%	5% to 20%
Global Equities	15%	<b>10%</b>	10% to 30%	5% to 20%
Alternatives				
Private Real Estate	40%	40%	10% to 60%	10% to <b>50%</b>
Infrastructure	0%	0%	0% to 10%	0% to 10%
Private Equity/Venture Capital	0%	0%	0% to 10%	0% to 10%
<b>Total Equities and Alternatives</b>	<b>70%</b>	<b>65%</b>		
<b>Cash</b>	<b>0%</b>	<b>0%</b>	<b>0% to 10%</b>	<b>0% to 10%</b>

## State of Wisconsin Board of Commissioners of Public Lands

### School Trust Fund Investment Guidelines and Investment Policy Statements

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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.

*As amended at the 05/xx/04/xx/2021-2022 BCPL Board Meeting*

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**Appendix 1**

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

# 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<sup>7</sup> 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..."<sup>1</sup> 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-specified categories of 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*."<sup>2</sup>

## 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

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<sup>1</sup> Article X, Section 8 - Wisconsin Constitution

<sup>2</sup> Chapter 24.61(2)(a) and 112.11(3) - Wisconsin Statutes



long-term perspective will constrain impulsive and potentially harmful decision-making in reaction to short 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>
<b>Investment Guidelines</b>	At least every two years
<b>Investment Policy Statements</b>	At least every two years
<b>Asset Allocation Policy</b>	At least annually
<b>Total Fund Performance</b>	At least quarterly
<b>Asset Class Performance</b>	At least quarterly
<b>Investment Manager Performance</b>	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~~less than 8,000 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~~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~~June 30, 2019~~2022~~, the Common School Fund had total (cost basis) financial assets of \$1.27 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
<b>Total Fixed Income</b>		<b>\$731,263,643</b>
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
<b>Total Equities and Alternatives</b>		<b>\$96,837,263</b>
Cash		
<del>State Investment Fund</del> <b>Total Cash</b>		<b>\$330,984,794</b>
<b>TOTAL ASSETS</b>		<b>\$1,159,085,699</b>
<small>*Fund values are marked to market at end of each fiscal year.</small>		

Remaining land assets of the Common School Fund total less than 8,005,955 acres classified as follows (some acres appear in more than one category, so total acreage is less than the sum of each category):-  
 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:

<u>Management Classification Common School Fund Acreage</u>	<u>Common School Fund Lands Description</u>	<u>Acres</u>
<u>Timber Base</u>	<u>Productive Timberland Upland forest scheduled for sustainable timber harvest activities</u>	<u>3,240 963</u>
<u>High Conservation Value</u>	<u>Upland forest acres not scheduled for harvesting Non-Timbered (primarily wetlands) due to inaccessibility or High Conservation status</u>	<u>9783 56</u>
<u>Forest Lowland</u>	<u>Wetland forest acres currently deferred from management activity due to poor timber markets or low volume/value</u>	<u>2,530</u>
<u>Non-Forest</u>	<u>Land with Management Impediments Non-forested acres likely never converted to forest due to excessively wet conditions or other impediments to forest growth</u>	<u>1,827 080</u>

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 less than 72,000 ~~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. Prior to the establishment of this policy, a ~~Additions to principal come from~~ were limited to the proceeds of timber sales.

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

As of ~~December 31, 2019~~ June 30, 2022, the Normal School Fund had total (cost basis) financial assets of approximately ~~\$27.829.3~~ \$27,789.3 million, ~~invested in the following security types:~~

**Normal School Fund Assets**

<b>Fixed Income</b>	<b>Cost-Basis*</b>
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	--
<b>Total Fixed Income</b>	<b>\$22,470,775</b>
<b>Equities and Alternatives</b>	
Total Equities and Alternatives	--
<b>Cash</b>	
State Investment Fund	\$5,372,420
Timber Sale Deposits	{54,053}
<b>TOTAL ASSETS</b>	<b>\$27,789,141</b>

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

Remaining land assets of the Normal School Fund total ~~less than 72,000~~ 71,176 acres classified as follows (some acres appear in more than one category, so total acreage is less than the sum of each category):- 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:

<u>Management Classification</u>	<u>Normal School Fund Lands Description</u>	<u>Acres</u>
<u>Timber Base</u>	<u>Upland forest scheduled for sustainable timber harvest activities</u>	<u>29,270</u>
<u>High Conservation Value</u>	<u>Upland forest acres not scheduled for harvesting due to inaccessibility or High Conservation status</u>	<u>2,472</u>
<u>Forest Lowland</u>	<u>Wetland forest acres currently deferred from management activity due to poor timber markets or low volume/value</u>	<u>20,284</u>

<u>Non-Forest</u>	<u>Non-forested acres likely never converted to forest due to excessively wet conditions or other impediments to forest growth</u>	<u>19,324</u>
<u>Normal School Fund Acreage</u>		
<u>Productive Timberland</u>	<u>28,403</u>	
<u>Non-Timbered (primarily wetlands)</u>	<u>20,388</u>	
<u>Land with Management Impediments</u>	<u>21,698</u>	

~~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~~ June 30, 2022, the University Fund had total financial assets of \$234,130. ~~invested as follows:~~

#### University Fund Assets

<u>Fixed Income</u>	<u>Cost Basis*</u>
<u>Public Debt</u> <del>State/State Agency/Municipal Bonds</del>	<u>\$30,192</u>
<u>Private Debt</u> <del>BCPL State Trust Fund Loans</del>	<u>\$147,109</u>
<u>Total Fixed Income</u>	<u>\$177,301</u>
<u>Cash</u>	
<u>State Investment Fund</u>	<u>\$56,829</u>
<b><u>TOTAL ASSETS</u></b>	<b><u>\$234,130</u></b>

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

Land assets of the University Fund consist ~~of 35 acres of a single remaining parcel of 37~~ deeded acres ~~classified as follows:~~ The majority of the parcel is submerged, with the remainder predominantly wetlands.

<u>Management Classification</u>	<u>University Fund Lands Description</u>	<u>Acres</u>
<u>Timber Base</u>	<u>Upland forest scheduled for sustainable timber harvest activities</u>	<u>0</u>
<u>High Conservation Value</u>	<u>Upland forest acres not scheduled for harvesting due to inaccessibility or High Conservation status</u>	<u>3</u>
<u>Forest Lowland</u>	<u>Wetland forest acres currently deferred from management activity due to poor timber markets or low volume/value</u>	<u>0</u>

<u>Non-Forest</u>	<u>Non-forested acres likely never converted to forest due to excessively wet conditions or other impediments to forest growth</u>	<u>32</u>
<u>University Fund Acreage</u>		
<u>Productive Timberland</u>		<u>0</u>
<u>Non-Timbered (primarily wetlands)</u>		<u>37</u>
<u>Land with Management Impediments</u>		<u>37</u>



### 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~~ June 30, 2022, the Agricultural College Fund had total financial assets of ~~\$307,076~~ \$305,282 invested as follows:

#### Agricultural Fund Assets

Fixed Income	Cost Basis*
<del>Public Debt</del> <del>State/State Agency/Municipal Bonds</del>	<del>\$59,047</del>
<del>Private Debt</del> <del>BCPL State Trust Fund Loans</del>	<del>\$224,645</del>
<del>Total Fixed Income</del>	<del>\$283,692</del>
Cash	
<del>State Investment Fund</del>	<del>\$21,589</del>
<b><del>TOTAL ASSETS</del></b>	<b><del>\$305,282</del></b>

\*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~~Controller, 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~~Controller 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.

Upon prior approval from the Board of the general outline of the proposed structure of the sale of Trust Fund Loans, the Investment Committee is authorized to develop and execute an on-going program to sell Trust Fund Loans. This program shall be designed to maintain and improve the strength and resilience of the State Trust Fund Loan Program, increase distributable income earned by the Trust Funds, and improve the ability to manage portfolio assets in accordance with approved Strategic Asset Allocations.

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 completed by a third-party consultant and 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.~~

~~c.~~

### 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.~~

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.

~~6.~~

### 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 value of real-estate holdings where possible by clearing title issues, gaining legal access, and developing roads.
  - generate long-term capital gains income through timber harvesting that follows third party audited Forest Stewardship Council (FSC) sustainable timber management standards.
  - improve management and administrative efficiencies through the rearrangement of land assets into larger contiguous blocks. This is accomplished through the sale or exchange of small/non-productive remote parcels, followed by the purchase or exchange for larger/more productive parcels adjacent to existing blocks.
- ~~a. • Research, develop, and initiate new methods of generating revenue from the land base with strategies including carbon sequestration projects, commercial maple syrup tapping contracts and long-term leasing for solar energy generation. 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 by statute 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 allowed 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. The 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 and other 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~~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~~requires 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 is 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.

Asset diversification since the implementation of the Prudent Investor Standard has meaningfully reduced distribution risk. However, m~~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. ~~The A prudent~~ minimum amount ~~of to be maintained within the~~ Common School Fund and Normal School Fund smoothing accounts shall be maintained at is hereby established at~~50% .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 or before October 1 ~~of~~ each ~~fiscal~~ year, the BCPL ~~Senior Accountant/Financial Manager~~Controller 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"..."<sup>4</sup>

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 in the~~ fund principal ~~balance 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 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 ~~149-150+~~ 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.<sup>3</sup> 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 less than 80,000~~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. In addition, the historic value of land assets has increased at a rate that is higher than inflation, and annual revenue generated from lands has exceeded management and holding costs. At some point in the future, BCPL may want to reconsider the current asset allocation to timberland, but it is remains in the best interest of Trust Fund beneficiaries to take reasonable steps in-to 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~~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”.

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



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 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 ~~1516,075-206~~ acres and purchased about ~~1416,660-370~~ acres of replacement School Trust Lands. During the same period, BCPL has also exchanged a significant amount of land (~~1,403-609~~ acres in and ~~2,065-305~~ 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-parcels~~ 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

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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~~ less than 8,000 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 1<sup>st</sup> 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. ~~Until the last decade, First published by the U.S. Bureau of Labor Statistics in 1967,~~ this index ~~has had~~ grown at an average annual rate ~~of 6.0% and has remained~~ significantly ~~higher above~~ than the overall inflation rate ~~since inception~~:

Average Annual Rate of Inflation

<u>As of June 30,</u>	CPI Educational Books and Supplies	CPI <sup>1</sup>	Common School Fund Avg Annual Fund Growth
<del>1967</del> <u>1972-2019</u> <del>2022</del>	<del>6.05</del> <u>.7%</u>	<del>4.04</del> <u>.0%</u>	<del>7.24</del> <u>%</u>
<del>2000</del> <u>1992-2019</u> <del>2022</del>	<del>5.04</del> <u>.5%</u>	<del>2.15</del> <u>%</u>	<del>5.25</del> <u>.6%</u>
<del>2010</del> <u>2012-2019</u> <del>2022</del>	<del>3.62</del> <u>.5%</u>	<del>1.72</del> <u>.6%</u>	<del>3.73</del> <u>.9%</u>
<u>2017-2022</u>	<u>1.0%</u>	<u>3.9%</u>	<u>4.2%</u>

<sup>1</sup> Consumer Price Index for All Urban Consumers: All Items in U.S. City Average (CPIAUCSL)

~~In contrast to the standard measure of CPI, the annual rate of CPI – Educational Books and Supplies is clearly declining over time. This trend may be due to the introduction of digital technology into the classroom and/or other factors. In any case, annual distributions for public school library media and resources are increasingly used for products and services distinct from traditional books and supplies. Over time, this trend has made this specialized index less suitable for evaluating growth in the Common School Fund.~~

~~Projections of inflation are also complicated by the unknown long-term impacts of the Covid-19 pandemic on supply/demand imbalances and on global supply chains. Because of these factors, prudence dictates that a conservative long-term inflation assumption of 4% be established within this policy. 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, t~~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, t~~This ~~fact trend~~ is not likely to continue if fund growth is limited to the historic sources of fines, forfeitures and escheats. ~~First, t~~There are political and economic pressures on amounts contributed to the Common School Fund from these historic sources. ~~Second~~In addition, 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~~Therefore, to maintain principal growth at or above the rate of

~~inflation, it will be necessary to rely on for long-term capital gains from the for-fund investment portfolio s to contribute to that that growth rate. with the addition of long-term capital gains.~~

A prudent assumption may be that ~~long-term capital gains financial assets currently~~ need to contribute 1-2% of annual growth ~~to the Common School Fund for principal to increase at the rate of inflation. T and~~ this requirement ~~will is~~ 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~~ allocations 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 over \$130-110 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
<b>Fixed Income</b>	<b>55%</b>	
Public Debt		
State/State Agency/Municipal Bonds	5%	0% to <del>30</del> 20%
U.S. Treasury/Agency Bonds	0%	0% to <del>30</del> 20%
U.S. Treasury Inflation Protected Securities	0%	0% to 10%
Corporate Bonds	<del>10</del> 5%	0% to <del>30</del> 20%
Private Debt		
BCPL State Trust Fund Loans	<del>30</del> 25%	<del>20</del> 10% to <del>50</del> 30%
Other Private Debt	<del>10</del> 15%	<del>10</del> 0% to <del>20</del> 30%
<b>Equities and Alternatives</b>	<b>45%<del>50</del>%</b>	
Public Equities		
<u>Preferred Equities</u>	<u>5.0%</u>	<u>0% to 10%</u>
Domestic Equities	7.5%	5% to <del>30</del> 20%
Global Equities	7.5%	5% to 20%
Alternatives		
Private Real Estate	20%	<del>5</del> 10% to <del>25</del> 30%
<u>Real Assets/Infrastructure</u>	<u>5</u> 4%	0% to 10%
Private Equity/Venture Capital	<del>5</del> 4%	0% to 10%
<b>Total Equities and Alternatives</b>	<b>48%</b>	
<b>Cash</b>	<b>02%</b>	0% to 10%

### 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.

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## Benchmarks

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

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

# 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 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 less than 72,000~~ 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 1<sup>st</sup> 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 4.95% since first created in 1993, ~~well above the overall inflation rate (CPI) during this period:~~

Average Annual Rate of Inflation

<u>As of June 30,</u>	CPI - Education	CPI <sup>1</sup>	Normal School Fund Avg Annual Fund Growth <sup>#2</sup>
<del>1993-2019</del> <u>2022</u>	<del>4.94.5%</del> <u>4.95%</u>	<del>4.02.5%</del> <u>2.16%</u>	<del>11.9.7%</del> <u>1.92.3%</u>
<del>2000-2012</del> <u>2012-2019</u> <u>2022</u>	<del>4.72.7%</del> <u>3.32.2%</u>	<del>2.16%</del> <u>13.79%</u>	<del>1.92.3%</del> <u>12.0.8%</u>
<del>2010-2017</del> <u>2017-2019</u> <u>2022</u>	<del>3.32.2%</del>	<del>13.79%</del>	<del>12.0.8%</del>

<sup>1</sup> Consumer Price Index for All Urban Consumers: All Items in U.S. City Average (CPIAUCSL)

<sup>#2</sup> Fund balance for ~~2010-2012, 2017,~~ and ~~2019-2022~~ is net of monies reserved for land bank purchases.

~~In contrast to the standard measure of CPI, the annual rate of CPI – Education is clearly declining over time. This trend may be due to the introduction of digital technology into the classroom and/or other factors. Projections of inflation are also complicated by the unknown long-term impacts of the Covid-19 pandemic on supply/demand imbalances and on global supply chains. Because of these factors, prudence dictates that a conservative long-term inflation assumption of 4% be established within this policy.~~

~~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 above, n~~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.

Prior to FY2020, Normal School Fund financial assets needed to produce the income required to fund agency expenses in the management of land and timber assets. This obligation effectively constrained the allocation of financial assets to fixed income securities.

However, the ~~FY2020 FY2020~~ switch to ~~GPR funding of agency expenses from (State of Wisconsin general purpose Purpose tax Tax revenues 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 ~~has allowed the~~ the reallocation of ~~assets assets to~~ supplement long-term capital gains.

~~To provide for future fund growth above the long-term rate of inflation, a prudent goal would be for financial assets to provide an additional 2.0% annual growth from long-term capital gains 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 A prudent assumption would round that requirement up to 2.5%, 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 Maintaining this level of supplemental growth of 2.5% from financial assets requires a significant allocation to equity securities and real estate that have produced significant capital gains over the long-term. However, the fund must also continue producing the stable income stream necessary to fund designated UW scholarship and academic programs. Therefore, the allocation not dedicated to produce long-term capital gains must shift to higher-yielding private debt funds. 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 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 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.

### **Fund Size**

The smaller size of the Normal School Fund combined with the large minimum investment size required by many private funds constrains the number of these funds available for investment. In turn, limiting the number of funds makes diversification *within* the chosen funds an important consideration in management of the portfolio.

### **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
<del>Fixed Income</del>	<del>30%</del>	
Public Debt		
State/State Agency/Municipal Bonds	0%	0% to 20%
U.S. Treasury/Agency Bonds	0%	0% to 20%
U.S. Treasury Inflation Protected Securities	0%	0% to <del>10</del> 20%
Corporate Bonds	0%	0% to <del>10</del> 20%
Private Debt		
BCPL State Trust Fund Loans	<del>30</del> 0%	20% to <del>40</del> 20%
Other Private Debt	<del>0</del> 35%	10% to <del>10</del> 50%
<del>Equities and Alternatives</del> <b>TOTAL FIXED INCOME</b>	<del>70</del> 35%	
Public Equities		
Preferred Equities	5%	0% to 10%
Domestic Equities	<del>15</del> 10%	<del>10</del> 5% to <del>30</del> 20%
Global Equities	<del>15</del> 10%	<del>10</del> 5% to <del>30</del> 20%
Alternatives		
Private Real Estate	40%	10% to 60%
<del>Real Assets</del> /Infrastructure	0%	0% to 10%
Private Equity/Venture Capital	0%	0% to 10%
<b>TOTAL EQUITIES AND ALTERNATIVES</b>	<b>65%</b>	
<del>Cash</del> <b>CASH</b>	<b>0%</b>	

### 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.

Normal School Fund:

Asset Class	Benchmark
Fixed Income	S&P Taxable Municipal Bond <u>Index</u>
<u>Preferred Equities</u>	<u>S&amp;P Preferred Stock Index</u>
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

# 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

**BOARD MEETING  
OCTOBER 4, 2022**

**AGENDA ITEM #6  
CARBON CREDIT PROPOSAL FROM ANEW CARBON DEVELOPMENT LLC**

**RECITALS**

- A. The Board of Commissioners of Public Lands staff requested forest carbon project assessment proposals from entities that assist landowners in selling carbon credits.
- B. BCPL received a proposal from Anew Carbon Development, LLC (“ANEW”) for participation in the voluntary market under the American Carbon Registry (ACR) Improved Forest Management (IFM) program. While BCPL sought proposals from multiple sources, this was the only proposal received.
- C. ANEW has a significant amount of experience in this area and has assisted other public land managers such as Bayfield County in participating in carbon markets. ANEW’s proposal would provide BCPL with the opportunity to sell carbon sequestration credits over a forty-year period from approximately 50,000 acres of school trust lands selected by BCPL.
- D. The proposal would not require BCPL to expend money for the carbon sequestration assessment. The sale of carbon credits is projected to generate more than twelve million dollars (\$12 million) in net revenue for the BCPL trust funds over the first ten years of the project from the sale of carbon sequestration credits.
- E. BCPL staff have reviewed the proposal from ANEW and have determined that ANEW is qualified to provide the services to BCPL that would be necessary for BCPL to participate in the above-described carbon credit program. BCPL staff members recommend that BCPL accept the proposal from ANEW and begin work on developing a contract with ANEW for the sale of carbon credits.

**NOW, THEREFORE BE IT RESOLVED**, that the Board of Commissioners of Public Lands authorizes BCPL staff to accept the proposal from ANEW.

**BE IT FURTHER RESOLVED**, that BCPL staff is authorized and directed to work on developing a contract with ANEW for BCPL to participate in the voluntary carbon credit market described above. Such contract shall be in accordance with state law and on such terms and conditions as the Executive Secretary determines to be reasonable and necessary. The Executive Secretary is authorized and directed to execute any documents reasonably necessary to complete such transactions. BCPL staff members shall provide the Board with timely reports on the progression of such project.