

# Service Area Plan

## Department of the Treasury

### Banking and Investment Services (72503)

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## Service Area Background Information

### Service Area Description

This service area provides for (1) the management and investment of state funds, (2) the administration and management of the Local Government Investment Pool (LGIP) (3) the administration of the State Non-Arbitrage Program to ensure the investment of bond proceeds are in compliance with federal arbitrage rebate regulations, (4) the development and management of the Commonwealth's statewide banking network and cash concentration system, and (5) the development of banking and cash management services for state agencies and institutions.

Products and services include:

- Portfolio management and investment of the Commonwealth's general account operating funds and special and trust funds
- The LGIP, a AAAM rated "2a7 like" fund available to local governments and other public entities of the Commonwealth for the investment of public funds.
- Development and issuance of a credit card contract administration for the benefit of public agencies and institutions
- Administration of the Community Bankers Bank Agreement that streamlines the placement of time deposits
- Wire transfer and disbursement services for investments, certain vendor payments, and debt service payments
- Administration of the State Non-Arbitrage Program (SNAP)
- Management of external investment managers program for the general account portfolio
- Statewide banking cash management contracts and agreements
- Statewide regional depository cash concentration system
- Interest income forecast and cash flow projections
- Investment program for the Tobacco Indemnification and Community Revitalization Endowment
- Custody of financial assets held by the Commonwealth.

### Service Area Alignment to Mission

This service area directly aligns with the Department of the Treasury's mission of serving the Commonwealth by providing excellent financial management and outstanding customer service.

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#### Service Area Statutory Authority

Chapter 18 of Title 2.2, §2.2-1807 of the Code of Virginia charges the State Treasurer with the custody of all Commonwealth funds and other funds held in a fiduciary capacity; §2.2-1800 through §2.2-1843 mandates how the State Treasurer shall receive, disburse, invest and account for funds; and §2.2-1806 jointly authorizes and empowers the Governor and State Treasurer to invest excess funds. Chapter 45, The Investment of Public Funds Act (§2.2-4500 through §2.2-4517) describes the legal investments for public funds as well as for public sinking funds. Annual operations related to portfolio management and investment services for funds of the Commonwealth are provided for in the Appropriation Act §3-1.01 H.

Chapter 18 of Title 2.2, §2.2-2415 and §2.2-2416 of the Code of Virginia requires investment oversight through the issuance of guidelines by the Treasury Board for the general account, the Securities Lending Program, and the Local Government Investment Pool (LGIP) created by Chapter 46 of Title 2.2. The State Treasurer is expected to issue guidelines for the investment of local funds upon request in Chapter 31 of Title 58, §58.1-3156 of the Code of Virginia. Chapter 46 of Title 3.1, §3.1-1109.1 of the Code of Virginia mandates the administration of the investment program for the Tobacco Indemnification and Community Revitalization Endowment.

Chapter 18 of Title 2.2, §2.2-1803 of the Code of Virginia outlines Treasury's responsibility for maintenance of bank accounts and the regulation of depositing state funds. Treasury's responsibility for deposits in banks and security of deposits is mandated in §2.2-1815.

Chapter 3 of Title 23, §23-21 of the Code of Virginia states that proceeds of Higher Education bonds and revenues shall be paid into State Treasury and Chapter 1 of Title 33.1, §33.1-23.03:5 requires the State Treasurer to administer the investment program for the Transportation Trust Fund.

Statutory authority for Banking and Investment Services is also regulated by Federal statute through the Federal Cash Management Improvement Act which relates to the management of funds provided by the federal government for programs administered by the Commonwealth and the Federal Debt Collection Improvement Act - Section 31001 (X) which requires the acceptance of all federal payments via electronic funds transfer (EFT). Further, the Government Non-Arbitrage Investment Act requires that Treasury makes available to the Commonwealth and its local governments a program to assist with the investment and accounting for bond proceeds in compliance with federal arbitrage rebate regulations. The Commonwealth's State Non-Arbitrage Program (SNAP) is outlined in Chapter 47 of Title 2.2, §2.2-4700 through §2.2-4705 of the Code of Virginia.

See Appendix A, Additional Statutory Authority Information, for additional statutory authority for this service area.

#### Service Area Customer Base

Customer(s)	Served	Potential
Boards and Authorities - Treasury Board	1	1
Business Partners	50	50
Executive Branch Officials, Agencies and Institutions	108	108
Intra-Agency Staff	116	116
Legislative Branch and Money Committees	140	140
Local Government Investment Pool Customers	357	650
Virginia Citizens	7,500,000	7,500,000

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#### **Anticipated Changes In Service Area Customer Base**

- The development of new banking and cash management products made available by Treasury for agencies and institutions could increase the use of these products and impact the customer base. As institutions of higher education gain greater autonomy they have expressed interest in Treasury investment services. Effective July 1, 2008, states will be required to either pledge certain assets to cover Other Post Employment Benefits (OPEBs) or reduce their assets by this amount. Treasury may be involved with other finance agencies in developing options and/or plans for this new GASB requirement.

#### **Service Area Partners**

##### **Cash concentration system administrator**

Facilitates the movement of deposits from regional banks into the state's concentration bank

#### **Service Area Partners**

##### **Credit card administrator**

Perform credit card services for any state agency or institution

#### **Service Area Partners**

##### **External investment management companies**

Responsible for the management of about 25% of the General Account's assets and the Tobacco Indemnification Endowment Fund and the SNAP Program

#### **Service Area Partners**

##### **Investment consultant**

Responsible for monitoring the performance of the investment management firms and taking the lead on all investment manager searches, the development of investment policies and guidelines and reporting investment results to the Commonwealth Treasury Board

#### **Service Area Partners**

##### **Investment dealers**

Compete in the purchase and sale of securities

#### **Service Area Partners**

##### **Major banking partners**

Provide collection and disbursement services and Virginia's community banks providing local deposit services

#### **Service Area Partners**

##### **Master custody bank**

Responsible for all safekeeping of investments, pricing, accounting, and investment compliance, as well as acting as transfer agent for the Local Government Investment Pool and providing the fund accounting function for the Pool

#### **Service Area Partners**

##### **Standard and Poor's investment rating firm**

Provides surveillance and monitoring of the Local Government Investment Pool to ensure that the fund is managed in compliance with a AAAM rating.

#### **Service Area Partners**

##### **Third Party Securities Lending Agent**

Provides securities lending services for both the General Account and Lottery.

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#### Service Area Products and Services

- Investment management services for the general account, the Local Government Investment Pool, the Tobacco Indemnification and Community Revitalization Fund, and various trust funds
- Monthly statements and quarterly newsletter to all Local Government Investment Pool participants
- Monthly report to Treasury Board, which includes a review of investment returns, investment income, comparison of investment income to both actual and relative to established benchmarks, review of general monthly economic and portfolio(s) activities, and comparison of investment income to forecasted amount
- Monthly investment results to Executive Branch Secretaries and Agencies and Legislative Branch Money Committees
- General Account interest income forecast to Department of Taxation for their incorporation into the state-wide forecast
- Annual input and discussion of investment results to the Operations Division for inclusion in Commonwealth's Comprehensive Annual Financial Report
- Literary Fund forecast to Department of Education, Secretaries of Finance and Education, and Legislative Branch Money Committees
- Custody and safekeeping services for all financial assets held by the Commonwealth
- Wire transfer services for investments, certain vendor payments and debt service payments
- Cash management and banking consulting services to state agencies, public entities, and local governments
- Securities lending program

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#### Factors Impacting Service Area Products and Services

- As a result of a generally strong economy, General Account balances over the years have increased dramatically. This increases the workload and also the complexity in the management of the General Account's assets.
- The State's restrictive method of compensating and rewarding superior performing employees will present an ever increasing problem as the U.S. economy continues to strengthen. This will affect all service areas of Treasury, including and especially this service area. The younger workforce is more willing to make career changes, putting us at a serious disadvantage in adding and retaining the best work force possible.
- A continued increase in separately managed portfolios increases the workload and oversight of these portfolios.
- The Local Government Investment Pool AAAm rating increases reporting, compliance and credit review requirements.
- Third-party securities lending requires additional monitoring and mediation as there are now three parties rather than two involved and compensation for securities lending is no longer part of the Master Custody contract.
- New investment programs with unique requirements such as the TICR endowment add additional requirements on staff.

#### Anticipated Changes To Service Area Products and Services

- While GASB 40 will have a serious impact in the special and trust area, this service area will be negatively affected as well. More requirements include a more comprehensive narrative and more detailed statistical data that will have to be provided by this service area.
- A new master custody contract that will become effective April 1, 2006, may require treasury staff to assume certain tasks such as data entry for wire transfers and trades that have been previously performed by the master custodian.
- Growing portfolio(s), coupled with new and more complex investment options and investment programs, will require more time and a highly motivated and knowledgeable staff.

#### Service Area Human Resources Summary

##### Service Area Human Resources Overview

Human resources for this service area include 10 full-time classified positions. Position titles and reporting structure can be found in Appendix B, Service Area Structure.

##### Service Area Full-Time Equivalent (FTE) Position Summary

Effective Date:	1/1/2006
Total Authorized Position level .....	10
Vacant Positions .....	1
Non-Classified (Filled).....	0
Full-Time Classified (Filled) .....	9
Part-Time Classified (Filled) .....	0
Faculty (Filled) .....	0
Wage .....	0
Contract Employees .....	0
Total Human Resource Level .....	9

##### Factors Impacting Service Area Human Resources

Human Resource factors impacting this service area include hiring and retaining the best professional staff, given a strong U.S. economy and the State's restrictive policy of rewarding superior performance.

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#### Anticipated Changes in Service Area Human Resources

Anticipated changes in human resources for this service area include the potential retirement of at least 20% of current senior personnel within the next five years.

#### Service Area Financial Summary

The budget for this service area is \$4,487,472 for FY 2007 and \$4,491,573 for FY 2008. Of this amount, \$291,809 in FY 2007 and \$295,910 in FY 2008 is derived from non-general fund sources. It is anticipated that the S & P fee will be funded with the LGIP fee income rather than with a General Fund appropriation. However, this service area will need an additional staff assistant to assist with the general administration functions of the department and help staff with the administration of and reporting requirements of new programs added during the past year. These include SNAP, TICR endowment and third-party securities lending. Also, this position will be back-up to the LGIP client service position (nongeneral fund expenditure of \$55,431 for FY 2007 and \$59,532 for FY 2008). In addition, the State Non-Arbitrage Program has been transferred from the Accounting and Trust service area to this service area and the change to the base budget (\$50,000) is also reflected below for this transfer.

	<u>Fiscal Year 2007</u>		<u>Fiscal Year 2008</u>	
	<b>General Fund</b>	<b>Nongeneral Fund</b>	<b>General Fund</b>	<b>Nongeneral Fund</b>
<b>Base Budget</b>	\$4,146,809	\$186,378	\$4,146,809	\$186,378
<b>Changes To Base</b>	\$48,854	\$105,431	\$48,854	\$109,532
<b>SERVICE AREA TOTAL</b>	<b>\$4,195,663</b>	<b>\$291,809</b>	<b>\$4,195,663</b>	<b>\$295,910</b>

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## Service Area Objectives, Measures, and Strategies

### Objective 72503.01

***Achieve investment earnings yield on the Commonwealth's General Fund Primary Liquidity Portfolio that exceed the benchmark one-year Constant Maturity Treasury yield by 15 basis points over a five-year period.***

Our objective for this goal is to enhance investment earnings for the general fund's Primary Liquidity Portfolio to exceed market benchmarks. Exceeding market rates is a measure of success in the management and investment of funds.

#### **This Objective Supports the Following Agency Goals:**

- Deliver high-quality cash management services, driven by cost effective solutions, creativity and fiduciary prudence.

( This objective supports the agency goal to "Deliver high-quality cash management services, driven by cost effective solutions, creativity and fiduciary prudence". In addition, it aligns with state objectives to be a national leader in the preservation and enhancement of our economy, to engage and inform citizens to ensure we serve their interests and to be recognized as the best managed state in the nation.)

#### **This Objective Has The Following Measure(s):**

- **Measure 72503.01.01**

***General Fund investment earnings yield for primary liquidity portfolio.***

**Measure Type:** Outcome      **Measure Frequency:** Quarterly

**Measure Baseline:** Investment earnings for the Primary Liquidity Portfolio for fiscal year 2005 exceeded the benchmarked one-year Constant Maturity Treasury yield by 66 basis points above the 15 basis points target set in the performance measure.

**Measure Target:** Over a five-year period, the Primary Liquidity Portfolio investment earnings yield will exceed the one-year Constant Maturity Treasury yield by 15 basis points.

#### **Measure Source and Calculation:**

The data sources are the General fund investment earnings report for the Primary Liquidity Portfolio and the one-year Constant Maturity yield. The one-year Constant Maturity treasury yield is calculated by the Federal Reserve Bank and is published monthly in the Federal Reserve statistical Release H.15 (Selected Interest Rates). The calculation is the Primary Liquidity Portfolio investment yield minus the one-year Constant Maturity Treasury yield minus 15 basis points target computed on a monthly basis and averaged for the quarter.

#### **Objective 72503.01 Has the Following Strategies:**

- Increase use of credit quality spread products in the management of our portfolio(s), given market conditions that are not within the control of the portfolio manager(s).
- Review allocation of investments instruments based on current market conditions.
- Review on a regular basis the forecast of receipts and disbursements to better determine maturity structure of the general account portfolio.
- Meet with external investment managers to discuss market conditions, the economic environment, and investment guidelines.