ARIZONA STATE BOARD OF INVESTMENT

2016 FIVE-YEAR REVIEW REPORT

TITLE 2. ADMINISTRATION

CHAPTER 13. STATE BOARD OF INVESTMENT

ARTICLE 1. GENERAL PROVISIONS

Arizona State Board of Investment
2016 Five-Year Review Report
I. Introduction

Under A.R.S. § 41-1056, every agency shall review its rules at least once every five years to determine whether any rule should be amended or repealed. Each agency shall prepare a report summarizing its findings, its supporting reasons, and any proposed course of action; and obtain approval of the report from the Governor's Regulatory Review Council (GRRC). The schedule for reviews is determined by GRRC. The report for the Arizona Board of Investment rules listed under A.A.C. Title 2, Chapter 13, Article 1 is due January 29, 2016.

The Board of Investment is responsible for reviewing the investment of state monies, serving as trustees of the Permanent Land Trust Funds, and approval of the State Treasurer's Office Investment Policy. The Board of Investment provides independent oversight to the approximately $13.2 billion of assets under management held by the Office of the State Treasurer. The Board in conjunction with the State Treasurer's office also selects the State's Servicing Bank provider.

A.R.S. 35-311 established the Board of Investment membership as the State Treasurer (with the Treasurer as Chairman), the Director of the Department of Administration, the State Banking Superintendent, and two other individuals appointed by the Treasurer.

II. Five-Year Rules Review Report Applying to all Three Rules

1. **Statutory Authority.**

   General: A.R.S. § 35-315 (B). In a public meeting held on May 16, 1996, the Board of Investment (then called the Board of Deposit) approved the rule.

2. **Objectives:**

   The rules establishes a logistical framework/mechanism within which the provisions of A.R.S. 35-315(B) may be carried out allowing the State Treasurer's Office to adopt procedures for the receipt and deposit of general fund interest earnings as well as for the invoice from and payment to the state's servicing bank. The rules authorize deposit of general fund interest earnings into a general fund account known as the "Servicing Bank Charges Account" to pay servicing charges to the State's servicing bank. After the claims have been paid from the Servicing Bank Charges Account, any remaining interest earnings are transferred back into the general fund.

   The servicing bank provides the State Treasurer's office with a monthly account analysis statement for services rendered in the preceding month. The statement includes the number of transactions performed, amount and time duration of deposits and all other information required under the servicing bank contract.

3. **Effectiveness.**

   The rules are effective in meeting their respective objectives.

4. **Consistency.**

   The rules are consistent with the Board of Investment statutes: A.R.S. Title 35, Chapter 2, and Article 2. There are no other inconsistencies with statutes, or other rules. These are the only rules governing the Board.

5. **Enforcement.**

   The rules are enforced as written.

6. **Relation to Federal Law**

   Federal law is not applicable to this rule. The rule is based on state law.

7. **Clarity, Conciseness and Understandability.**

   The rules are clear, concise, and understandable.

8. **Written Criticisms.**

   The Board has not received any written criticisms of the rules in the past five years.

9. **Economic, Small Business, and Consumer Impact Comparison.**

   The economic impact to the state has been positive since the earnings that the State Treasurer's office can make on investments is higher than the credit the servicing bank provides for compensating balances. Currently, operating balances are earning between 55 to 77 basis points compared to the 45 basis points earned through compensating balances. Under the previous 5-year review, compensating balances were receiving 50 basis points versus the 75-100 basis points earned by the Treasurer's investments. The increased earnings made by the Treasurer's office investments to pay for the servicing bank contract as opposed to leaving compensating balances at the bank has been the case throughout the 20 years this rule has been in place. The Arizona economy also benefits from this arrangement as it frees up capital of the servicing bank to be used in the private sector. State law requires banks to pledge collateral of 102% for all public entity deposits that are not covered by federal insurance. The Treasurer's office would have to deposit substantial amounts of operating funds in the servicing bank account in order to achieve sufficient credit for off-setting the costs of the bank contract. This would require the bank to deploy more of its capital to the public sector as opposed to the private sector and also charge the state more for the contract due to the increased cost of setting aside this collateral. Any risk of the Treasurer's office of investing operating balances in obligations of the United States Government or U.S. agencies as well as highly rated debt issued by U.S. firms is mitigated by the increased returns the office generates for taxpayers and the expansion of the private sector in the state.

10. Analysis Submitted Comparing Rule's Impact.

No analysis was submitted.

11. Completion of Previous Five-Year Review.

This is the fourth five-year review of these rules. The previous review was conducted by GRRC in 2011. Previous 5-year review changes were made through a letter to the Secretary of State.

12. Least Burden and Costs to Persons Regulated Necessary to Achieve the Underlying Regulatory Objective.

The definitions do not impose a burden or cost on the public.

13. Issuance of a regulatory permit, license, or agency authorization.

No permit, license or authorization is required under the rule.

14. Proposed Action.

The Board plans to leave the rule as written. Prior 5-year review action updated rules to reflect statutory name change for the Board as well as correcting errors in statutory citations in the rules.