

Texas Water Development Board



Review of Compliance with the Public Funds Investment Act

Project #2024.05
December 2023

Executive Summary

We reviewed fiscal year 2022 and 2023 investment activities to determine whether agency processes ensure compliance with the requirements of the Public Funds Investment Act (Texas Government Code, Chapter 2256) and the Texas Water Development Board (TWDB) investment policy. Our review included an evaluation of internal controls.

Overall, we found that the agency complied with the requirements outlined in the Public Funds Investment Act and the TWDB investment policy. Specifically:

- The agency's written investment policy included all required key elements, and the Board reviewed and approved the investment policy and strategies annually.
- Training sessions were attended by each Board member and each investment officer, and a report on training activities was provided to the Board.
- The biennial compliance audit and an independent review of the quarterly reports were performed, and the results of each were reported to the Board.
- Investment activity adhered to the requirements of the Act and the investment policy.
- Fiscal year 2023 quarterly investment reports included all of the required attributes and were also presented to the Board within a reasonable time period after the end of each quarter.
- Each investment officer completed and submitted a non-disclosure statement.

However, our review identified an opportunity to strengthen controls over existing processes to ensure the information included in the quarterly investment reports is accurate.

Background

The Public Funds Investment Act (Act) governs the investment of government funds in Texas. The Act requires certain state agencies, universities, and local governments to arrange for a biennial compliance audit of management controls on investments and adherence to the entity's established investment policies, for those funds the entity is authorized to invest. The TWDB investment policy assigns the responsibility for performing this audit to the Internal Audit Division. Additionally, the results of the audit must be reported to the State Auditor's Office by January 1 of each even-numbered year.

The TWDB investment policy designates the Chief Financial Officer, Development Fund Manager, and the Director of Accounting as the agency's investment officers. Investment officers are responsible for managing and reporting on the agency's investment activities.

As of August 31, 2023, the market value of all investments totaled approximately \$3.9 billion for those funds managed by the TWDB, and included cash, money market funds, commercial paper, repurchase agreements, and a variety of federal, state, and local securities. These investment resources represented the various funds and accounts maintained by the TWDB and the Texas Water Resources Finance Authority in administering financial assistance programs.

Objectives, Scope, and Methodology

Objectives

The objective of the audit was to review the agency's investment activities to determine whether processes ensure compliance with the requirements of the Public Funds Investment Act and the TWDB investment policy. This included:

1. Determining whether policies and procedures complied with the Act, and such policies and procedures were appropriate and reasonable for the agency's investment types and investment goals; and
2. Determining whether internal controls over investments were sufficient to safeguard assets, ensure proper conduct by participants in the investment process, and eliminate conflicts of interest.

Scope and Methodology

The scope of the audit covered fiscal year 2022 and 2023 (September 1, 2021 to August 31, 2023) and was limited to funds managed by the TWDB.

The methodology for the audit consisted of a review of the following documentation:

- Public Funds Investment Act (Texas Government Code, Chapter 2256).
- TWDB investment policies and internal procedures.
- Board memos, meeting minutes, and agendas.
- Funds Management and Investment Agreement between TWDB and the Texas Treasury Safekeeping Trust Company.
- Quarterly investment reports and all related correspondence and documentation.
- Investment training records, reports, materials, and certificates of completion.
- Review of Compliance with the Public Funds Investment Act and Review of Quarterly Investment Reports.
- Public Funds Investment Act (PFIA) and Personal Business Relationship Disclosure Questionnaire.
- Ethics Training Acknowledgement (Conflict of Interest) Forms.

Tests and procedures included the following:

- Conducting interviews with management and staff.
- Determining whether the investment policy included the required elements.
- Determining whether the quarterly investment reports included the specific components required by the Act.
- Testing investment transactions and holdings for adherence to strategies, restrictions, controls and objectives, as defined in the TWDB investment policy.

- Reconciling quarterly investment reports to source supporting documentation, including the investment transaction detail and holdings data, to determine accuracy.
- Selecting a sample of investment transactions and validating that controls ensured assets were properly processed, safeguarded, and reported.

This engagement was conducted in accordance with *Generally Accepted Government Auditing Standards* and the *International Standards for the Professional Practice of Internal Auditing*. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our observations and conclusions based on our audit objectives.

The audit team consisted of:

David Ramos
Michelle Cooper, CGAP, CFE, CICA
Nicole Campbell, CIA, CISA, MPA

Detailed Results

We reviewed fiscal year 2022 and 2023 investment activities to determine whether agency processes ensure compliance with the requirements of the Public Funds Investment Act (Texas Government Code, Chapter 2256) and the TWDB investment policy. Our review included an evaluation of internal controls.

Overall, we found that the agency complied with the requirements outlined in the Act and the investment policy. Specifically:

- The agency's written investment policy included all of the key elements required by Section 2256.005. The policy emphasized safety of the principal, liquidity to meet cash flow needs, marketability, and portfolio diversification. Additionally, the Board reviewed and approved the investment policy and strategies annually.
- Training sessions were attended by each Board member and investment officer, as required by Section 2256.007. The training sessions were related to the individual's responsibilities and were completed within the first six months after taking office or assuming duties, and for each investment officer, a training session was completed during the most recent fiscal biennium. We also noted that a report on training activities was provided to the Board, as required by Section 2256.007(d).
- The biennial compliance audit was performed and the results were reported to the Board, as required by Section 2256.005(n). An independent review of the quarterly reports was also performed, and the results were also reported to the Board, as required by Section 2256.023(d).
- Investment transactions and holdings were evaluated to determine whether they complied with the investment policy, including portfolio objectives and strategies, authorized investments, and restrictions, and as prescribed by Section 2256.009-016. Our review found that the investment activity adhered to the requirements of the Act and the investment policy, and no discrepancies were noted.
- Fiscal year 2023 quarterly investment reports included all attributes required by Section 2256.023(b), including:
 - Detail of the agency's investment position.
 - Signatures of each investment officer.
 - A summary statement for pooled funds.
 - Book values and market values of each separately invested asset at the end of the reporting period by asset and fund type.
 - Maturity dates for each separately invested asset.
 - Fund types for each individual investment that was acquired.
 - A statement regarding compliance of the investment portfolio as it relates to the TWDB investment policy and strategies and the Act.

The reports were also presented to the Board within a reasonable time period after the end of each quarter, in accordance with the agency's internal operating procedures and Section 2256.023(c).

- Each investment officer completed and submitted a disclosure statement, as required by Section 2256.005(i).

However, we identified an opportunity to strengthen controls over existing processes to ensure the information included in the quarterly investment reports is accurate.

1. Fiscal year 2023 quarterly investment reports complied with Section 2256.023 of the Act, and were presented to the Board timely; however, we noted inaccuracies in certain data reported in the Quarterly Investment Report for the Quarter November 30, 2022, and the Quarterly Investment Report for the Quarter Ending August 31, 2023.

We evaluated investment transaction details and holdings for fiscal year 2023 to determine their compliance, and adherence to the strategies and restrictions, listed in the investment policy. Data from the quarterly investment reports was also traced to the corresponding source supporting documentation to ensure the completeness and accuracy of the data presented.

- For the first quarter of fiscal year 2023 (quarterly investment report ending November 30, 2022), our review found that quarterly average yield percentages were inaccurately reported for treasury and TTSTC funds of state pools, the pooled funds total, debt service funds, TWRFA funds, and the portfolio totals. This information was included within the Portfolio Summary by Fund table of the report.

The quarterly average yield percentages were reported lower for pooled funds and portfolio totals, and higher for treasury and TTSTC funds of state pools, debt service, and TWRFA funds, than those calculated and included in the supporting documentation for the report.

- For the fourth quarter of fiscal year 2023 (quarterly investment report ending August 31, 2023), our review found that the following three securities were incorrectly classified by security type:
 - CUSIP 89233HZJ6 was classified as Agencies, but listed as Commercial Paper on the source report for the asset. The market value was \$23,597,406.
 - CUSIP 62479MYW7 was classified as US Treasuries, but listed as Commercial Paper on the source report for the asset. The market value was 29,577,661.
 - CUSIP X9USDDTP3 was classified as US Treasuries, but listed as Short-Term Investment Funds (money market funds) on the source report for the asset. The market value was \$58,121.

The misclassification of these three securities did not impact the total market value of all investments included in the report for the quarter. However, data and charts shown in the report,

of the investment portfolio by security type, including certain categories of security type, were impacted commensurate to the market value of each security.

Although procedures for preparing quarterly investment reports include a peer review step, the peer review did not identify these errors.

Recommendation

Controls should be strengthened to ensure the information included in the quarterly investment reports is accurate.

Management's Response: *Management agrees. We are implementing control totals by class and scheduling an official meeting for a comprehensive review of each report.*

Responsible Party: *Chief Financial Officer*

Implementation Date: *January 1, 2024*

Closing

We would like to express our appreciation to all of the management and personnel for their cooperation and assistance provided to the internal audit staff during this review. For questions or additional information concerning this report, please contact Nicole Campbell at (512) 463-7978.

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