REPORT HIGHLIGHTS

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Colorado Department of the Treasury's Investment Management

Performance Audit, October 2019

AUDIT CONCERN

The investment management practices of the Colorado Department of the Treasury (Treasury) were consistent with statutory requirements and generally achieved the Treasury Investment Program's statutory objectives of legality, safety, liquidity, and yield. However, the Treasury's portfolio holdings did not always comply with its Investment Policy Statements, and opportunities exist to improve the manner in which the Treasury reports its investment performance.

KEY FINDINGS

- The Treasury established two performance benchmarks against which it could evaluate and report on its performance, a yield benchmark and a total return benchmark, but it regularly only reported its book yield because its investment strategy is focused on maximizing yield and cash flow. This showed the Treasury outperforming its yield benchmark at nearly every point between Calendar Years 2011 through 2018, but an analysis of total returns reveals a more nuanced perspective in which the Treasury outperformed and underperformed its benchmarks in different years. Measuring total returns accounts for both the yield generated and the change in value experienced due to market conditions, and is therefore an important indicator of the overall value, risk, and return characteristics of a portfolio.
- Some investment holdings were outside the parameters allowed in the Investment Policy Statements.
  - The Treasury allocated assets within the T-Pool in a manner consistent with the Investment Policy Statements, but allocations of the Public School Permanent Fund and the Unclaimed Property Tourism Fund portfolios to Treasury/Agency assets and to corporate bonds and notes were often not compliant, as were allocations from these portfolios to the T-Pool.
  - Some T-Pool investment holdings exceeded maturity limits, including assets with maturities exceeding one year in its T-Pool Cash sub-portfolio and five years in its T-Pool Bond sub-portfolio.
- The Treasury did not always maintain documentation supporting older total return benchmark information or portfolio credit ratings, including information generated by its prior custodian, impeding verification and replication of reported results.

BACKGROUND

The Treasury is part of the executive branch of state government. The State Treasurer, an elected position, is the chief executive of the Treasury and is authorized by statute to maintain custody of and invest state monies. The Treasury manages three primary portfolios:

- Treasury Pool (T-Pool): pools monies held in more than 800 government funds; as of December 31, 2018, it held nearly $8 billion in assets.
- Public School Permanent Fund: holds assets from the sale or use of lands that have been granted by the federal government for educational purposes; as of December 31, 2018, it held approximately $775 million in assets.
- Unclaimed Property Tourism Promotion Trust Fund: holds the proceeds from the sale of securities held as unclaimed property for more than a year; as of December 31, 2018, it held approximately $208 million in assets.

RECOMMENDATIONS

- Enhance measurement and reporting of portfolio performance by including in quarterly reporting both the book yield and total returns of its portfolios versus established benchmarks, and ensuring total return benchmarks are consistent with the Treasury's Investment Policy Statements.
- Specify in the Investment Policy Statements how compliance with key restrictions related to asset allocations, maturity, and credit quality will be measured, and develop a formal procedure requiring investment officers to obtain the pre-approval from the State Treasurer for deviations from Investment Policy Statement provisions.
- Ensure adequate documentation is maintained by Treasury and/or its custodian for all benchmarks used to allow results to be verified and replicated.

The Treasury agreed with these recommendations.