



TEXAS REAL ESTATE COMMISSION INTERNAL AUDIT SERVICES

AUDIT #17-001 PUBLIC FUNDS INVESTMENT ACT COMPLIANCE AUDIT

June 26, 2107

As Prepared by
McConnell & Jones LLP





Table of Contents

Section	Page Number
1.0 <i>Introduction</i>	2
2.0 <i>Compliance Audit Details</i>	3





June 29, 2017

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Dear Madam Chair, Commissioners and Board Members:

Attached is internal audit report #17-001 Public Funds Investment Act Compliance Audit. This audit was performed as part of the approved FY2017 Annual Internal Audit Plan and was required by Texas Government Code Chapter 2256 Public Funds Investment.

We assessed the Texas Real Estate Commission's (TREC) compliance with Texas Government Code Chapter 2256 and determined that the agency is compliant with all requirements except delivering the biennial report of Subchapter A, Chapter 2256. Additionally, management's internal controls for investment processes and reporting are effective and working as designed.

Please contact Darlene Brown at 281.740.0017 if you should have any questions about this audit report.

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Sincerely,

Odysseus Lanier, CPA

Partner

1.0 INTRODUCTION

McConnell & Jones LLP (MJ) serving as the outsourced internal audit function (Internal Audit) for the Texas Real Estate Commission (TREC) performed an internal audit of TREC's compliance with Texas Government Code Chapter 2256 Public Funds Investment, commonly referred to as the Public Funds Investment Act (PFIA).

Government Code Chapter 2256 Section 2256.005 Investment Policies, Investment Strategies; Investment Officer subsection (n) requires that at least once every two years a state agency arranges for a compliance audit of management controls on investments and adherence to the agency's established investment policies to be performed by their internal auditor or a private auditor. The audit resulting audit reports must be reported to the state auditor no later than January 1st of each even numbered year.

TREC does invest public funds and therefore is required to comply with Texas Government Code Chapter 2256 Public Funds Investment. These funds are invested through the Texas Treasury Safekeeping Trust Company (TTSTC or Texas Trust).

We performed this audit in compliance with PFIA timing requirements and as part of the approved FY2017 Annual Internal Audit Plan. This audit was conducted in accordance with generally accepted government auditing standards (GAGAS). Those 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 accomplishes that requirement.

Pertinent information has not been omitted from this report. This report summarizes the audit objective and scope, our assessment based on our audit objectives and the audit approach.

Objectives and Scope

The purpose of this audit is to assess TREC's compliance with the PFIA's specific requirements. In doing so, we also evaluated management controls in place to ensure that the agency's funds are invested according to their investment policy and that the investment reports are accurately compiled and distributed in a timely manner.

Texas Government Code Chapter 2256 Public Funds Investment sections applicable to TREC are:

- Section 2256.005 Investment Policies, Investment Strategies; Investment Officer
- Sec. 2256.007 Investment Training; State Agency Board Members and Officers
- Section 2256.023 Internal Management Reports

The scope period was September 1, 2016 through May 31, 2017.

Conclusion

The Texas Real Estate Commission is in compliance with all applicable requirements of Texas Government Code Chapter 2256 Public Funds Investment except delivering the biennial training report. All required individuals had taken the investment training. Additionally, management's internal controls for investment activities and reporting are effective and working as designed.

2.0 COMPLIANCE AUDIT DETAILS

The Texas Real Estate Commission maintains five separate recovery fund accounts in which reserve funds are placed in short-term investments through the Texas Treasury Safekeeping Trust Company. These funds are:

- 1) Real Estate Recovery Trust Account;
- 2) Real Estate Inspection Recovery Fund;
- 3) Current Operations & Contingencies Reserve;
- 4) Educational Development Reserve; and
- 5) Long-term Facilities Master Plan Reserve.

TREC's investment strategy for these funds is to maintain a laddered approach to the investment portfolio's management. This approach provides for a relatively even distribution of securities maturing each year to facilitate cash flow and investment decisions and also helps to control interest rate exposure.

Investment Policy

The PFA requires state agencies that invest public funds to have a written investment policy that is reviewed at least once per year by the governing body. Section 2256.005 Investment Policies, Investment Strategies; Investment Officer lists specific topics that must be included in the agency's investment policy.

Audit procedures applied to determine compliance with these requirements included:

- Reviewed TREC's investment policy and compared it to requirements listed in Section 2256.005.

Figure IP1 compares Section 2256.005 requirements to TREC's investment policy.

Conclusion

TREC is in compliance with Section 2256.005 Investment Policies, Investment Strategies; Investment Officer.

Texas Government Code Sec. 2256.005 Section	PFA Investment Policy Requirements	TREC Investment Policy Meets Requirement
(b)(2)	Primarily emphasize safety of principal and liquidity.	
(b)(3)	Address investment diversification, yield, and maturity and the quality and capability of investment management.	
(b)(4)(A)	Include a list of the types of authorized investments in which the investing entity's funds may be invested.	
(b)(4)(B)	Include the maximum allowable stated maturity of any individual investment owned by the entity.	
(b)(4)(C)	Include for pooled fund groups, the maximum dollar weighted average maturity allowed based on the stated maturity date for the portfolio.	N/A TREC does not invest in pooled fund groups.
(b)(4)(D)	Include methods to monitor the market price of investments acquired with public funds.	

Texas Government Code Sec. 2256.005 Section	PFIA Investment Policy Requirements	TREC Investment Policy Meets Requirement
(b)(4)(E)	Include a requirement for settlement of all transactions, except investment pool funds and mutual funds, on a delivery versus payment basis.	
(b)(4)(F)	Include procedures to monitor rating changes in investments acquired with public funds and the liquidation of such investments consistent with the provisions of Section 2256.021 .	N/A TREC uses TTSTC for investments. TTSTC monitors rating changes.
(d)	As an integral part of an investment policy, the governing body shall adopt a separate written investment strategy for each of the funds or group of funds under its control. Each investment strategy must describe the investment objectives for the particular fund using the following priorities in order of importance: (1) understanding of the suitability of the investment to the financial requirements of the entity (2) preservation and safety of principal (3) liquidity (4) marketability of the investment if the need arises to liquidate the investment before maturity (5) diversification of the investment portfolio and (6) yield.	
(e)	The governing body of an investing entity shall review its investment policy and investment strategies not less than annually	
(e)	The governing body shall adopt a written instrument by rule, order, ordinance, or resolution stating that it has reviewed the investment policy and investment strategies and that the written instrument so adopted shall record any changes made to either the investment policy or investment strategies.	
(f)	Each investing entity shall designate, by rule, order, ordinance, or resolution, as appropriate, one or more officers or employees of the state agency, local government, or investment pool as investment officer to be responsible for the investment of its funds consistent with the investment policy adopted by the entity.	

Investment Officer, State Agency Board Member and Officer Training

The PFIA section 2256.007 lists specific training requirements for the agency

investment officers, board members and officers.

Audit procedures applied to determine compliance with these requirements included:

- Reviewed TREC’s investment training records to determine compliance with section 2256.007 requirements.
- Reviewed quarterly investment reports and reports on Subchapter A, Chapter 2256, provided to TREC’s governing body.

Figure IT1 compares section 2256.007 training requirements to TREC’s records of investment officer training taken.

Conclusion

TREC is in compliance with Section 2256.007, except for providing the biennial report to the Commission and Board regarding Subchapter A, Chapter 2256.

Recommendation

TREC’s investment officer should deliver a biennial training report to their governing body as required in section 2256.007(d).

Managements Response

Although the Commission and Board members have completed the required training and have informal knowledge of the requirements in Subchapter A, Chapter 2256, going forward, management will provide the Commission and Board with formal biennial reports on Subchapter A, Chapter 2256, as required in Section 2256.007.

Texas Government Code Sec. 2256.007 Section	INVESTMENT TRAINING; STATE AGENCY BOARD MEMBERS AND OFFICERS.	TREC Investment Officer and Officers Training Meet Requirements
(a)	Each member of the governing board of a state agency and its investment officer shall attend at least one training session relating to the person's responsibilities under this chapter within six months after taking office or assuming duties.	
(b)	The Texas Higher Education Coordinating Board shall provide the training under this section.	N/A
(c)	Training under this section must include education in investment controls, security risks, strategy risks, market risks, diversification of investment portfolio, and compliance with this chapter.	
(d)	An investment officer shall attend a training session not less than once each state fiscal biennium and may receive training from any independent source approved by the governing body of the state agency.	
(d)	The investment officer shall prepare a report on this subchapter and deliver the report to the governing body of the state agency not later than the 180th day after the last day of each regular session of the legislature.	

Figure IT1: Texas Government Code Training Requirements Compared to TREC’s Training Taken TREC’s investment officers, board and council members have taken training required by the Texas Government Code

Management Reports

The PFIA requires state agencies that invest public funds provide investment management reports to its governing body. Section

2256.023 Internal Management Reports lists specific information that must be included in the investment management reports.

TREC prepares investment management reports (staff reports) each month and posts them to their website. The staff reports are provided to their Commissioners and Board members at each quarterly meeting.

Audit procedures applied to determine compliance with Section 2256.023 requirements included:

- Reviewed monthly staff reports for completion and content compliance with Section 2256.023;
- Compared monthly investment reports provided by Texas Treasury Safekeeping Trust Company to the monthly staff reports to determine completeness and accuracy;

- Sampled transactions reported on the monthly staff reports and compared them to supporting documentation (investment authorization and investment conformation) for validity and accuracy; and
- Reviewed internal procedures to determine existence and completeness.

Figure MR1 compares the Section 2256.023 investment management report requirements to TREC’s investment management reports (staff reports).

Conclusion

TREC’s investment management reports (staff reports) are in compliance with Section 2256.023. Additionally, the monthly investment reports were accurate and supported by authorized investment transaction execution documents.

Texas Government Code Sec. 2256.023 Section	Internal Management Reports	TREC Investment Management Reports Meet Requirements
(a)	Not less than quarterly, the investment officer shall prepare and submit to the governing body of the entity a written report of investment transactions for all funds covered by this chapter for the preceding reporting period.	
(b)(1)(2)(3)	The report must: (1) describe in detail the investment position of the entity on the date of the report; (2) be prepared jointly by all investment officers of the entity; (3) be signed by each investment officer of the entity;	
(b)(4)	contain a summary statement of each pooled fund group that states the: (A) beginning market value for the reporting period; (B) ending market value for the period; and (C) fully accrued interest for the reporting period;	
(b)(5)	state the book value and market value of each separately invested asset at the end of the reporting period by the type of asset and fund type invested;	

Texas Government Code Sec. 2256.023 Section	Internal Management Reports	TREC Investment Management Reports Meet Requirements
(b)(6)	state the maturity date of each separately invested asset that has a maturity date;	
(b)(7)	state the account or fund or pooled group fund in the state agency or local government for which each individual investment was acquired;	
(b)(8)	state the compliance of the investment portfolio of the state agency or local government as it relates to: (A) the investment strategy expressed in the agency's or local government's investment policy; and (B) relevant provisions of this chapter.	
(c)	The report shall be presented not less than quarterly to the governing body and the chief executive officer of the entity within a reasonable time after the end of the period.	
(d)	If an entity invests in other than money market mutual funds, investment pools or accounts offered by its depository bank in the form of certificates of deposit, or money market accounts or similar accounts, the reports prepared by the investment officers under this section shall be formally reviewed at least annually by an independent auditor, and the result of the review shall be reported to the governing body by that auditor.	N/A However, Internal Audit reviews compliance with PFIA requirements every two fiscal years

Figure MR1: Texas Government Code Reporting Requirements Compared to TREC's Management Reports
TREC's Investment Reports contain information items required by the Texas Government Code
 Legend: