

Chairman Levdansky, Chairman Nickol and members of the House Finance Committee, I want to thank you for giving me this opportunity to discuss House Bill 2259.

I am here today requesting your support for House Bill 2259, which extends part of the investment authority for Treasury's funds. The extension will allow Treasury to continue to broadly invest in securities including equities and mutual funds until December 31, 2010, and provides the appropriate authority to obtain reasonable returns with reasonable risk assessment.

The investment authority being extended has benefited the entire Commonwealth by generating nearly \$790 million since 2001. This figure is derived by taking the difference between the return with equities versus the return that would have been obtained without the addition of equities to Treasury's fixed income investments.

I would also like to take this opportunity to present a general overview of Treasury's investment activities and answer any questions you may have about Treasury's programs and services.

Before I begin, I would like to compliment the entire Treasury staff for their dedication and hard work. I have worked diligently to foster a constructive, energetic, collaborative and professional environment within the Department for our experienced, talented, and devoted people. I would especially like to commend them for navigating the difficult financial markets we have been experiencing this past year.

My term as Treasurer has been a gratifying and invigorating professional experience thus far. I have very much enjoyed working closely with the Legislature to expand and promote Treasury's many programs and services. Much of our success is due to the strong support of the General Assembly. I am confident that your support of House Bill 2259 will allow Treasury to continue its good work.

As many of you know, I launched the *e-Treasury Pennsylvania* initiative in September. The goal of this program is to create a framework for enhanced efficiency, high professional standards, transparency, and, above all else, good governance.

As the expression "*e-Treasury*" implies, the emerging Department will be progressive in both outlook and performance.

e-Treasury envisions a Treasury that:

- Safeguards the financial assets of all Pennsylvanians
- Employs modern business practices
- Constantly updates information technology
- Optimizes savings and revenues
- Exercises highest business standards

We are currently in the last round of reviews on the *e-Treasury Pennsylvania* report. The document, which will be constantly updated, will detail the issues that Treasury should address and offer recommendations on how to implement them.

I look forward to sharing the final report with the members of the General Assembly and the residents of Pennsylvania, along with my plan for implementing the recommended changes.

One of the areas on which *e-Treasury Pennsylvania* focused is financial asset management. This focus is driven by my commitment to utilize my many years of experience in public and private finance to serve as a prudent and vanguard investor for the Commonwealth's funds and to provide effective stewardship of those funds and investments.

All public investments whether undertaken by a treasurer or a pension fund are made pursuant to the "prudent person" rule or a derivation thereof. For example, the Pennsylvania pension funds operate under the "prudent investor" rule.

The concept was formally established by a Massachusetts jurist providing guidance to trustees in the early part of the 19th century. He directed investments in a manner by which "men of prudence, discretion and intelligence manage their own affairs, not in regard to speculation but in regard to the permanent disposition of their funds, considering the probable income, as well as the probable safety to the capital to be invested." The rule has gained widespread application and evolved to reflect changing investment philosophies. Today, the rule is reflected in the current Fiscal Code, which is particularly relevant to Treasury's investment portfolio where investments are considered both individually and within the context of the overall portfolio.

The Treasurer serves as custodian of nearly \$122 billion and actively invests approximately \$19.1 billion. Treasury oversees investment pools on behalf of various investors. These pools include those dealing with funds from the Commonwealth, individuals, local governments and nonprofit organizations.

Under Treasury's Investment Policy, "the investment strategy for each investment pool reflects a unique application of the prudent person test, drafted specifically to balance the investment criteria in an appropriate manner for these particular investors" (Treasury Investment Policy, page 1). Further, that policy provides that Treasury seek "quality investments that will maximize the likelihood that each pool will consistently satisfy its respective program requirements. Quality investments are those that are suitably conservative while still projected to outperform the relevant market benchmarks, net of all fees and expenses, over the appropriate time horizon. Finally, Treasury will actively pursue investments offering a reasonable risk-adjusted rate of return, appropriate to each pool and equal or superior to comparable alternative investments available to the pool, that also provides a positive stimulus to strategic segments of Pennsylvania's economic base, communities and citizens" (Treasury Investment Policy, pages 6-7).

As of March 31, 2008, Treasury had approximately \$17.4 billion in investments under management contained in 140 funds. Treasury's two largest pools, labeled Pool 98 and Pool 99, invest the Commonwealth's operating moneys.

Pool 98 (the Common Investment Pool), which contained \$7.8 billion as of March 31, 2008, is a variable share price investment vehicle that seeks to generate additional investment return over time by investing in fixed income and equity securities. Pool 99 (the Liquid Asset Pool), which contained \$2.5 billion as of March 31, 2008, is a stable share price investment vehicle that invests exclusively in fixed income securities, primarily of short duration.

Pool 98 is the repository of the bulk of the assets and transactions. As the checking account for the Commonwealth, it must contain the liquid assets required to meet the daily payment demands. In 2007, Treasury was responsible for 23 million payments totaling over \$64 billion.

Pool 98 also contains the security investments authorized by Section 301.1 (i) of the Fiscal Code, which is currently scheduled to expire at the end of the year. As I stated earlier, this additional investment authority has generated returns of nearly \$790 million more since 2001 than if we had invested solely in an assortment of fixed investments without equities added to our allocation mix. These investments, like all Treasury's investments, are governed by the prudent person rule. For the most part, these investments are made through investment managers, with the assistance of an investment advisor.

The remainder of Pool 98's investments contain assets that represent most of Treasury's Strategic Investment Opportunity category. These investments returned a yield of approximately 5.45% for the calendar year 2007. The authority for such investments predates the section under discussion and includes many investments that have been held for a significant number of years, including Israeli Bonds and notes from PHEAA. Two of the more recent investments include the Keystone Home Energy Loan Program - KeystoneHELP - and the Credit Union Better Choice program.

I would like to thank the House for its unanimous support for the continuation and expansion of KeystoneHELP in House Bill 1 (Special Session). The amendment, which provides \$5 million to Treasury, will leverage more funds to be used for moderate interest loans for energy efficient improvements and other energy-related loans. This initiative was recently expanded with the initiation of a Pennsylvania Housing Finance Agency (PHFA) program that now allows larger loans for KeystoneHELP's energy efficient projects. We look forward to working with you to make this proposal law.

Finally, I would like to talk about the Credit Union Better Choice program, which Treasury developed in conjunction with the Pennsylvania Credit Union Association. Credit Union Better Choice is believed to be the only program in the nation to provide a statewide alternative to payday lending, protecting consumers from the exorbitant fees that oftentimes trap them in a debt cycle. Credit Union Better Choice provides

consumers with low-cost, short-term loans and an investment in their futures through the program's financial literacy and savings components.

As you all know, it has been my goal as Treasurer to provide effective stewardship of the Commonwealth's funds and investments through calm economic times as well as the rough seas we are currently experiencing. As such, I am committed to keeping an eye out not only for future risks, but also for emerging opportunities for positive returns for the Commonwealth. Positive returns can be enhanced, however. I strongly believe that we can do well for our Funds and at the same time do good for Pennsylvania stakeholders. The KeystoneHELP and Credit Union Better Choice programs are perfect examples of this philosophy.

Thank you again for the opportunity to discuss Treasury's operations and programs. My staff and I are here to answer any questions that you may have.

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