University of California

Governmental Accounting Standards Board (GASB) Statement No. 79, *Certain External Investment Pools and Pool Participants*

Issues Resolution Memo No. 79-1

Evaluation of GASB Statement No. 79 as it Relates to UC Reporting Entities

Issued: December 2015

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BACKGROUND

GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*, was adopted by the University beginning July 1, 2015. GASB Statement No. 79 was proposed and approved due to the SEC publishing significant amendments in July 2014 to its 2010 Rule 2a7 that became starting in April 2016. Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, provides that qualifying external investment pools (those that are 2a7-like) can measure all of their investments at amortized cost. Because of the July 2014 changes to the SEC 2010 Rule 2a7, stakeholders requested that the Board reconsider existing guidance that refers to SEC Rule 2a7. Rule 2a7 contains the SEC's regulations that apply to money market funds. GASB Statement No.79 creates new criteria and guidelines for electing to measure external investment pools at amortized cost. If the non-compliance with those criteria is significant, then external investments should apply provisions in GASB Statement No. 31, as amended, and be measured at fair value. GASB Statement No. 79 amends Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, paragraphs 11 and 16; Statement No. 40, *Deposit and Investment Risk Disclosures*, paragraph 15; Statement No. 59, *Financial Instruments Omnibus*, paragraph 5; and Statement No. 72, *Fair Value Measurement and Application*, paragraph 69.

DEFINE ISSUES

The University must determine whether GASB Statement No. 79 changes any existing financial reporting and disclosure requirements for any of the University's financial reporting entities.

AUTHORITATIVE GUIDANCE AND APPROACH

An external investment pool is defined in Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, as "an arrangement that commingles (pools) the moneys of more than one legally separate entity and invests, on the participants' behalf, in an investment portfolio; one or more of the participants is not part of the sponsor's reporting entity" (paragraph 22).

According to paragraph 4 of GASB Statement No. 79, an external investment pool may elect to measure for financial reporting purposes all of its investments at amortized cost if it meets all of the following criteria:

a) Transacts with its participants at a stable net asset value per share (for example, all contributions and redemptions are transacted at $1.00 net asset value per share)

b) Meets the portfolio maturity requirements in paragraphs 8-16

These include:
- Securities or investments acquired with a remaining maturity of 397 calendar days or less
- Portfolio maintains a weighted average maturity of 60 days or less
- Portfolio maintains a weighted average life of 120 days or less

c) Meets the portfolio quality requirements in paragraphs 17-26

These include requirements such that investments acquired presents minimal credit risk:

- a security should be acquired only if it has been rated by a nationally recognized statistical rating organization (NRSRO) that is denominated in U.S. dollars and has a credit rating within the highest category of short-term credit ratings (or its long-term equivalent category)
- a security that has not been rated by any NRSRO may be acquired only if the security is denominated in U.S. dollars and is determined (based upon the qualifying external investment
- pool's analysis) to be of comparable credit quality to securities that have been rated within the highest category of short-term credit ratings (or its long-term equivalent category

d) Meets the portfolio diversification requirements in paragraphs 27-31

These include requirements such that the investments acquire by the external investment pool do not exceed more than 5 percent of its total assets in investments of any one issuer.

e) Meets the portfolio liquidity requirements in paragraphs 32-38

These include requirements holding liquid assets sufficient to meet reasonably foreseeable redemptions.

f) Meets the shadow pricing requirements in paragraphs 39 and 40.

The external investment pool must calculate its shadow price on a monthly basis. The shadow price is the net asset value per share of a qualifying investment pool, calculated using total investments measured at fair value at the calculation date. The monthly calculation of the shadow price should occur no earlier than five business days prior to and no later than the end of the month. At each calculation date, that shadow price should not deviate more than one half of 1 percent from the net asset value per share calculated using total investments measured at amortized cost.

IMPLEMENTATION

Investments held by the University are principally carried in three investment pools, the Short Term Investment Pool (STIP), the Total Return Investment Pool (TRIP) and the General Endowment Pool (GEP). Cash for operations and bond proceeds for construction expenditures are invested in STIP. The University uses STIP to meet operational liquidity needs. TRIP provides the opportunity to maximize the return on long-term capital by taking advantage of the economies of scale of investing in a large pool across a broad range of asset classes. The GEP is a balanced portfolio and the primary investment vehicle for individual endowments and funds functioning as endowments. STIP, TRIP, and GEP are managed by the Office of the Chief Investment Officer.

Additionally, the University has fiduciary responsibility for the University of California Retiree Health Benefit Trust (UCRHBT), and the University of California Retirement System (UCRS). UCRS includes two defined benefit plans, the University of California Retirement Plan (UCRP) and the University of California Public Employees' Retirement System (PERS) Voluntary Early Retirement Incentive Plan (PERS–VERIP), and four defined contribution plans in the University of California Retirement Savings Program (UCRSP). UCRP provides lifetime retirement income, disability protection, death benefits, and post-retirement and pre-retirement survivor benefits to eligible employees of the University, and some legally separate entries.

UCRHBT, PERS, and UCRSP include investments made only by entities within the Universities reporting unit, and are therefore not external investment pools. STIP, GEP, TRIP, and UCRS pool are external investment pools as they include investments on behalf of organizations that are a part of the University, and external organizations that are associated with the University, but not financially accountable to the University. Those organizations include:

- The 10 Campuses, which are not considered separate legal entities or component units, but part of the University.
- The medical centers, which are not considered separate legal entities or component units, but part of the University.
- The 10 campus foundations, which are legally separate from the University, and reported by the University as discretely presented component units.
- Children's Hospital & Research Center Oakland (CHRCO), a private not-for-profit corporation, where the University is the sole corporate and voting member. CHRCO will be

reported by the University as a blended component unit starting in fiscal year ending June 30, 2016.

- Hastings College of the Law, which is affiliated with the University, but not a component unit or included in the financial reporting entity.

Analysis of STIP, GEP, TRIP, and UCRP against the criteria in GASB Statement No. 79:
The standard is not applicable. Even though we keep STIP at a constant value of $1 per share, we don’t record any investments at amortized cost. Actual income earned, including any realized gains or losses on the sale of STIP investments, is allocated to the holders based upon the number of shares held. The University, as the manager of the pool, absorbs all unrealized gains and losses associated with the fluctuation in the fair value of investments in the portfolio and guarantees $1 per share to all holders. The discretely presented components units may purchase or redeem shares in GEP, TRIP or other investment pools at the unitized value the time of purchase or redemption. All of our investments are recorded at fair value, so the standard isn’t applicable.

Analysis of EIP against the criteria in GASB Statement No. 79:
It is also noted that CHRCO invests in the UCSF Foundation's Endowed Investment Pool (EIP), an external investment pool managed by the UCSF Foundation.

Requirement per GASB Statement No. 79, paragraph 4	**EIP – Investments by CHRCO**
a) Transacts with its participants at a stable net asset value per share	Does not meet; Transacts at the unitized value of the portfolio
b) Meets the portfolio maturity requirements in paragraphs 8-16	Does not meet; Maturity dates greater than 397 calendar days. Investments in the EIP with the UCSF Foundation are committed to a one year lock-up period
c) Meets the portfolio quality requirements in paragraphs 17-26	Does not meet; Not all investments are of the highest rating by NRSRO.
d) Meets the portfolio diversification requirements in paragraphs 27-31	No further assessment completed as criteria a), b), and c) are not met, and all criteria must be met in order to elect to measure investments at amortized cost.
e) Meets the portfolio liquidity requirements in paragraphs 32-38	
f) Meets the shadow pricing requirements in paragraphs 39 and 40	

CONCLUSION:

Implementation of GASB Statement No. 79 has no effect on the financial statements for the year ended June 30, 2016 as none of the University’s external investment pools meet the requirements for electing to measure their investments at amortized cost. All of the University’s external investment pools will continue to be measured at fair value. As the foundations may have other investments outside of the investment pools analyzed above, if the foundations are measuring any investment at amortized cost, the foundations should evaluate whether to continue.