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WEST VIRGINIA

SECRETARY OF STATE

KEN HECHLER

ADMINISTRATIVE LAW DIVISION

Form #2

OFFICE OF WEST VIRGINIA
SECRETARY OF STATE

NOTICE OF A COMMENT PERIOD ON A PROPOSED RULE

AGENCY: West Virginia State Board of Investments TITLE NUMBER: 113

RULE TYPE: Legislative; CITE AUTHORITY WV Code §12-6-5 et seq.

AMENDMENT TO AN EXISTING RULE: YES NO

IF YES, SERIES NUMBER OF RULE BEING AMENDED: I

TITLE OF RULE BEING AMENDED: Administration of the Consolidated
Fund by the WV State Board of Investments.

IF NO, SERIES NUMBER OF NEW RULE BEING PROPOSED: _____

TITLE OF RULE BEING PROPOSED: _____

IN LIEU OF A PUBLIC HEARING, A COMMENT PERIOD HAS BEEN ESTABLISHED DURING WHICH ANY INTERESTED PERSON MAY SEND COMMENTS CONCERNING THESE PROPOSED RULES. THIS COMMENT PERIOD WILL END ON 2:00 p.m. AT March 1, 1996. ONLY WRITTEN COMMENTS WILL BE ACCEPTED AND ARE TO BE MAILED TO THE FOLLOWING ADDRESS. —

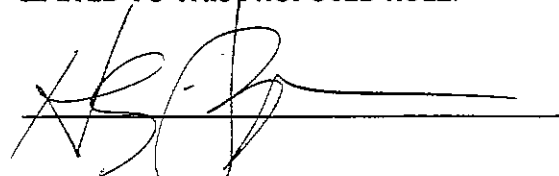
WV State Board of Investments

Attn: Jerry Simpson

State Capitol Building, Room E-122

Charleston, WV 25305

THE ISSUES TO BE HEARD SHALL BE LIMITED TO THIS PROPOSED RULE.



ATTACH A **BRIEF** SUMMARY OF YOUR PROPOSAL

6.60

Board Members:

Honorable W. Gaston Caperton, III
Governor/Chairman

Mr. John T. Poffenbarger
Executive Secretary/Member

Honorable Larrie Bailey
Treasurer/Member

Honorable Glen B. Gainer, III
Auditor/Member

Mr. Carlyle Farnsworth
Member

Ms. Marie Prezioso
Member

Mr. William T. Tracy
Member



State of West Virginia
Board of Investments

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Staff:

H. Craig Slaughter
Executive Director

D. Jerry Simpson
Chief Operating Officer

Matthew E. Jones
Chief Financial Officer

Diana Will
Chief Investment Officer

Mark E. N. Asaad
General Counsel

To: Honorable Ken Heckler
Secretary of State

From: H. Craig Slaughter *HCS*
Executive Director

Date: January 29, 1996

Subject: Notice Of A Comment Period For The Proposed Amendment To The Rule For
The Administration Of The Consolidated Fund.

The Legislature's Performance Evaluation and Research Division in their performance review report of the Board of Investments recommended restructuring the Enhanced Yield Pool to achieve a higher return (see attachment 1 and attachment 2, recommendation 4). The Board of Investments (Board) has also received inquiries from other State agencies about the possibility of increasing the yield on this pool.

Current limits on the pool were adopted due to liquidity concerns that have long since dissipated. The Board at their December 8, 1995 board meeting approved changes to this pool. The maturity length is extended from 3 years to 5 years and the dollar weighted average-maturity was changed from 1 year to 2 years. The only change to the current rule is section 5.2 (d). This change will allow for the implementation of the previously described changes.

If any additional information is needed, please contact Jerry Simpson of my staff at (304) 558-5000.

Large liquid balances that can be invested in longer term assets will generally earn a higher rate of return than repo rates. Generally speaking, the longer the average maturity of the portfolio, the higher the rate of return. Table 6 illustrates this using information from the BOI's quarterly reports.

The BOI has two pools within the Consolidated Operating Fund that are structured as money market funds, the Cash Liquidity Pool and the Government Money Market Pool. The guidelines for investing these pools are the same, investments are limited to purchases of securities with remaining maturities not greater than 397 days and the dollar weighted-average maturity of the securities may not exceed 90 days.

Table 6 illustrates that even within a money market structure investing with longer average maturity can result in higher yields in the long run. The Cash Liquidity Pool had an average maturity of 16 days from March 1993 to April 1995. The average total return during that time for the pool was 4.05%. Over the same period, the Government Money Market Pool had an average maturity of 52 days, and an average total return of 4.15%. The Enhanced Yield Pool is structured to have an average maturity longer than the money market structure. When the enhanced yield rates are compared with the money market pools, the result is similar. Over the period between July 1994 and April 1995, the Enhanced Yield had an average maturity of 151 days compared to 66 days for the Government Money Market and 39 days for the Cash Liquidity Pool. The average total return for the Government Money Market Pool was higher than the Cash Liquidity Pool by 12 basis points and the Enhanced Yield Pool was higher by 23 basis points.

There is a sizable amount of earnings to be gained from achieving 25 basis points more each year on investments. The PERD argues that 25 basis points is the minimum amount of lower earnings. Twenty-five basis points represent \$250,000 in earnings per \$100 million invested. Since the state invests several hundred million dollars in the Cash Liquidity Pool, and repo balances are too high for pension funds, the loss of earnings can easily add up to a few million dollars.

Furthermore, the PERD believes the earnings are lower by more than 25 basis points. Not only is it possible for the BOI to invest with a longer average maturity within the money market structure, the PERD believes that a portion of the excess liquidity could be invested in a structure that has a longer average maturity than the Enhanced Yield Pool.

Conclusion

In conclusion, the PERD contends that the BOI has invested too much of the State's funds in cash-equivalent assets. The rate of return could be higher if the BOI's rules allowed the Consolidated Operating Fund to have an average maturity greater than the current 90 days. Current rules restrict most of the State's funds to money market rates. The amount of lost earnings to the State is likely a few million per year.

Recommendation 1

Attachment 2

The BOI should work with the Legislative Auditor's Budget and Fiscal Affairs Division to develop annual projections of daily cash flow for the General Revenue Fund for the upcoming fiscal year. Thereafter, the BOI will develop these projections on its own. These 12 month projections should then be made available to advisors every month.

Recommendation 2

The BOI should consider giving advisors more specific guidelines that reflect the BOI's objectives for the Consolidated Operating Fund overall. The BOI should provide advisors specific information on what levels of liquidity the BOI desires, how much of a liquidity cushion is needed, and specific ranges of average maturities within the pool's structure, instead of giving only the top maturity limit. The performance measures may need to be adjusted periodically if specific guidelines preclude the possibility of the advisor meeting the performance measures.

Recommendation 3

The BOI should consider rule changes that allow the Consolidated Operating Fund to be invested between the guidelines of a money market structure and a mutual fund structure.

Recommendation 4

The BOI should consider restructuring the Enhanced Yield Pool to achieve a higher enhanced yield. The BOI should also consider increasing the amount within the Enhanced Yield Pool from the current level of \$25 million.

Recommendation 5

The Legislature should consider amending WVC §5-10D-4 to require the actuary for the pension funds to provide the BOI with monthly projections of withdrawals and contributions for the fiscal year for each pension plan. In addition, the amendment should include the requirement that the projections be updated each quarter or more frequently if necessary. The actuary currently projects annual contributions and benefit payments for the pension funds.

Recommendation 6

The Legislature should consider amending WVC §5a-2-11 to require the Department of Administration to provide the BOI with its monthly revenue projections. The Legislature should also consider requiring the Department of Administration to project daily revenue flows for the General Revenue Fund.

WEST VIRGINIA ADMINISTRATIVE REGULATIONS
West Virginia State Board of Investments

Chapter 12-6
Series I

Subject: Rules for the Administration of the Consolidated Fund by the West Virginia State Board of Investments.

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West Virginia State Board of Investments

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Chapter 12-6
Series I

OFFICE OF WEST VIRGINIA
SECRETARY OF STATE

Subject: Rules for the Administration of the Consolidated Fund by the West Virginia State Board of Investments.

Section 1. General

1.1. Scope - These rules implement the provisions of West Virginia Code §12-6-1 et seq. relating to the Consolidated Fund established by §12-6-8(b).

1.2. Authority - West Virginia Code §12-6-5 and §12-6-8.

1.3. Filing Date -

1.4. Effective Date -

1.5. Repeal of Former Rule - This legislative rule repeals and replaces West Virginia 113 CSR1 "Rules For the Administration of the Consolidated Fund by the West Virginia Board of Investments" filed May 17, 1991 and effective May 17, 1991.

1.6. Purpose - The general purpose of these rules is to aid in the implementation of the legislative findings and purpose set forth in the West Virginia Code §12-1-1, wherein the West Virginia State Board of Investments and the Treasurer are authorized to develop and maintain modern systems, consistent with sound financial practices, for the collection, disbursement, management and investment of public moneys. These rules and regulations implement such legislative intent by prescribing procedures for the administration of the Consolidated Fund by the Board and participation in the Consolidated Fund by State agencies (other than pension funds) and local governments.

Section 2. Definitions

For purposes of these rules, unless a different meaning clearly appears from the context:

"Board" means the West Virginia State Board of Investments;

"Code" means the West Virginia Code of 1931, as amended;

"Consolidated Fund" means the investment fund managed by the Board and established pursuant to the West Virginia Code §12-6-8;

"Local Government" means and includes a county, municipality, or any agency, authority, board, commission or instrumentality of a county or municipality, police officers' pensions and relief funds, fire fighters' pension and relief funds, and regional councils created pursuant to the provisions of West Virginia Code §8-25-1 et. seq.;

"Local Government Account" means the special account for the common investment of local government funds within the Consolidated Fund established pursuant to West Virginia Code §12-6-8(b);

"Participant" means all State agencies, local governments and other entities or individuals investing moneys or assets with the Consolidated Fund;

"Securities" has the same meaning set forth in West Virginia Code §12-6-2;

"Select U. S. Government Agency Obligation" means any evidence of indebtedness issued by any of the following: the Government National Mortgage Association (GNMA), and Resolution Trust Corporation Securities (RTC);

"Treasurer" means the Treasurer of the State of West Virginia;

"U. S. Government Agency Obligation" means and includes any obligation of any United State government agency guaranteed as to the payment of both principal and interest, directly or

indirectly, by the United States of America, including but not limited to the following: the Government National Mortgage Association (GNMA); the Federal Farm Credit Bank (FFCB); Federal Land Banks (FLB); the Federal Home Loan Mortgage Corporation (FHLMC); the Federal National Mortgage Association (FNMA); Federal Home Loan Banks (FHLB); Federal Intermediate Credit Banks; Banks For Cooperatives; Tennessee Valley Authority (TVA); United States Postal Service; Farmers Home Administration (FHA); Export-Import Bank; Federal Financing Bank; Student Loan Marketing Association (SLMA); Resolution Trust Corporation Securities (RTC); and Veterans Administration (VA); and

"U. S. Government Obligations" means and includes any direct obligation of, or obligation guaranteed as to payment of both principal and interest by, the United States of America.

Section 3. Participation in the Consolidated Fund

3.1. Participation by State Agencies - The Board of Investments may allow State agencies to participate in the Consolidated Fund upon written request by such State agencies. The Board of Investments is not required to execute a written or electronic request for deposit or withdrawals until the next business day. Requests for deposits or withdrawals shall state the amount which the agency wishes to make available for investment, or the amount which it wishes to withdraw, as the case may be. Such requests shall also contain such other information the Board of Investments considers necessary. The Board of Investments may require advance notice as determined by the Board for withdrawals of one million (\$1,000,000.00) or more.

3.2. Participation by Local Governments

(a) Local governments may commence participation in the Consolidated Fund by completing and returning to the Board of Investments an "account request form". The form of the "account request form" shall be prescribed by the Board of Investments, shall require such information as it considers necessary, and shall be made available to any local government upon request. The Board of Investments shall require each local government to submit copies of resolutions, orders or other proof of authorization or election to participate in the Consolidated Fund. Upon receipt of the account request form and other required information, the Board of Investments shall review and approve the account request form and if approved, the Board of Investments shall assign an account number to the local government within the Local Government Account of the Consolidated Fund. Local governments which require more than one account may request the establishment of additional accounts as needed, subject to the discretion of the Board of Investments.

(b) All notifications of deposit of funds by local governments into the Local Government Account, shall be made in a manner prescribed by the Board of Investments. The Board of Investments shall execute such request in a timely manner not to exceed 3 business days. All notifications of deposits shall be confirmed in writing by the local government and sent by mail on the same day the notification is made. The Board of Investments shall prescribe the forms which local governments shall use for the confirmation of such deposits by mail. All notifications of withdrawals of funds by the local governments from the Local Government Account shall be made by written or electronic request. The

Board of Investments shall prescribe the forms to be used for withdrawals. The Board of Investments shall prescribe the time period for the deposit or withdrawal of funds. The Board of Investments may require advance notice as determined by the Board for withdrawals of one million (\$1,000,000.00) or more.

(c) All deposits by local governments into the Local Government Account shall be made by means approved by the Board. All wired funds transferred by local governments shall be collected balances available for wire transfer and immediate credit at the Federal Reserve Bank. All checks accepted by the Board, shall be credited to the Local Government Account within two business days, following receipt by the Board of Investments. All funds transferred to the Board through ACH shall be credited to the Local Government Account on the day received by the Board.

(d) All withdrawals by local governments from the Local Government Account shall be made by check, Automated Clearing House, wire transfer, or any other method approved by the Board. The Board of Investments may require advance notice as determined by the Board for withdrawals of one million dollars (\$1,000,000.00) or more. Withdrawals of less than one hundred dollars (\$100.00) shall be made by check or through the Automated Clearing House.

Section 4. Accounting

4.1. Nature of Ownership - Each Participant shall own an undivided interest in the portfolio of the Consolidated Fund based on the Participant's prorata contribution of assets at any time. Ownership shall be expressed in terms of units. Each Participant, by completing and

returning an "Account Request Form" to the Board of Investments, has consented to the methods of sharing gains and losses and all other accounting methods required or adopted by the Board.

4.2. Accounting System - The Board of Investments shall implement an accounting system based on generally-accepted accounting principles.

4.3. Distribution of Earnings; Monthly Statement - The Board shall make a distribution from the pools undistributed earnings either by credit or debit to the principal account of the Participant or by means determined by the Board. The method of such distribution shall be at the Board's discretion. The Board of Investments shall furnish to each Participant a monthly statement of distributed earnings, deposits, withdrawals and changes in market value, if applicable, for each account. Participants will be periodically provided statements reflecting an accurate statement of the yield for the preceding period for the investment pool in which the Participant is investing.

Section 5. Investment of Consolidated Fund

5.1. General Investment Policies, Objectives and

Restrictions - All investment pools in the Consolidated Fund shall be individually subject to the policies, objectives and restrictions set forth herein.

(a) Purpose - The Board's purpose is to invest and protect the assets of the Consolidated Fund for the benefit of the citizens of the State of West Virginia.

(b) Standard of Care - All investments are to be made with the exercise of that degree of judgment and care, under circumstances then prevailing, which people of experience, prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

(c) Permissible Investments - The Consolidated Fund shall comply with West Virginia Code §12-6-9 and these rules and regulations, with regard to permissible investments.

(d) Social Responsibility - To the extent that investments are consistent with all other standards established by the Board, selection of investments should consider the best interests of the people of the State of West Virginia.

(e) Custody - The Board shall designate and maintain custodial arrangements in its sole discretion. However, no investment advisor shall maintain custody of the securities of the Consolidated Fund.

(f) Investment Advisors - The Board may select and maintain investment advisors who shall act in accordance with the terms and conditions specified by the Board and the applicable requirements of State and Federal Law.

(g) Investment Objectives - All pools within the Consolidated Fund, except the single-purpose pools described in Subsection 5.02(e), are subject to the investment objectives listed below in descending order of priority:

(1) Preservation of Capital - To preserve the capital investment in the Consolidated Fund.

(2) Liquidity - To maintain sufficient liquidity to provide for all anticipated withdrawals or transfers and to invest in securities with sufficient marketability to provide for unexpected withdrawals.

(3) Diversification - To diversify the investment of the assets of the Consolidated Fund so as to minimize the risk of losses.

(4) Turnover - To minimize transaction costs.

(5) Stability - To maintain a high level of security in the Consolidated Fund by minimizing risk and volatility insofar as possible.

(6) Rate of Return - To achieve a rate of return consistent with the rate of return objectives set by the Board.

(h) Investment Restrictions

(1) The Consolidated Fund shall abide by the investment restrictions of West Virginia Code §12-6-10 and as further set forth by the Board.

(2) Not more than 20% of the portfolio of the Consolidated Fund may be invested in any single industry sector. (The utility sector shall be subdivided for the purpose of this restriction

between telephone, electric, gas distribution, and similar utility industry segments.)

(3) The Consolidated Fund shall maintain a reasonable balance between the various classes of fixed income securities, without over concentration.

(4) The Consolidated Fund shall abide by the quality restrictions of West Virginia Code §12-6-9.

(5) Investment in financial futures contracts, options and other similar investments is prohibited.

(6) Minimum Amount of Investment - The minimum amount for investment in the Consolidated Fund is One Hundred Dollars (\$100.00). There is no minimum time for which deposits will be retained.

5.2. Investment Pools - The Consolidated Fund is composed of various investment pools. It is the intent of the Board that there be separate portfolio guidelines for the administration of each investment pool in addition to the policies, objectives and restrictions set forth in Subsection 5.01. The Board of Investments shall administer each investment pool in the Consolidated Fund in accordance with the rules and regulations and such guidelines as may be further prescribed by the Board.

(a) Cash Liquidity Pool - This investment pool is composed of the operating funds of the State, funds held in trust by State agencies, and funds invested by local governments. This pool is limited to securities with remaining maturities of not greater than three hundred ninety-seven (397) days and the dollar weighted-average-maturity of the securities in the portfolio may not exceed ninety (90) days. Also, the pool must meet all requirements outlined in Tables I and II of this Rule.

(b) Government Money Market Pool - This investment pool is composed of Participants whose funds may only be invested in U. S. Government Obligations, select U. S. Government Agency Obligations or repurchase agreements. This pool is limited to securities with remaining maturities of three hundred ninety-seven (397) days or less and the dollar weighted average maturity of the securities in the portfolio may not exceed ninety (90) days. Also, the pool must meet all requirements outlined in Table A of this Rule.

(c) Municipal Bond Restricted Pool - This investment pool is for the Municipal Bond Commission whose funds shall only be invested in U. S. Government Obligations, select U. S. Government Agency Obligations or repurchase agreements. This pool is limited to

--securities with remaining maturities of 5.0 years or less and the dollar weighted average maturity of the securities may not exceed 2.0 years. The pool must meet all requirements outlined in Table A of this Rule.

(d) Enhanced Yield Pool - This investment pool is composed of the operating funds of the State which the Board's staff have determined are not immediately needed to fund the State's liquidity requirements. This pool is limited to securities with remaining maturities of ~~not greater than (3.0) years and the (5.0) five years or less.~~ (5.0) five years or less. The dollar weighted-average-maturity of the securities in the portfolio may not exceed ~~(1.0)(2.0) one~~ two years. The pool must meet all requirements outlined in Tables I and II of this Rule.

(e) Single Purpose Pools - These investment pools are designed to meet the needs of individual State agencies. The Board of Investments shall invest only in the type of securities identified by the State agency controlling the pool, as recommended by the State agency and as necessary to meet the needs of each individual pool as to type of security and length of maturity, provided that such investments consist solely of those permitted by these rules.

(f) Other Investment Pools - The Board is further authorized to establish additional investment pools as the need may arise, provided that within eighteen months after their establishment these rules and regulations are amended to reflect their existence and appropriate investment guidelines are established for each pool. This provision does not apply to any new single purpose pool established pursuant to Subsection 5.02(c) of this rule.

TABLE I
GUIDELINES FOR DIVERSIFICATION
ACCORDING TO KIND OF INVESTMENT INSTRUMENT

<u>Instrument</u>	<u>Code Reference</u>	<u>Minimum</u>	<u>Maximum</u>
1. U. S. Government Obligation	§12-6-9(a)	0%	100%
2. U. S. Agency Obligation	§12-6-9(b)	0%	100%
3. Corporate bonds, notes debentures, commercial paper, and other evi- dence of indebtedness	§12-6-9(g) §12-6-10(1)	0%	75%
4. Commercial paper and other corporate ob- ligations maturing in less than one year	§12-6-9(g) §12-6-10(2)	0%	20%
5. Obligations of any single private corporation	§12-6-10(3)	0%	3%
6. Fully collateralized WV certificates of deposit maturing in less than one year	§12-6-9(h)	0%	30%
7. Repurchase agreements	§12-6-5(9)	0%	100%
8. Reverse repurchase agreement	§12-6-5(10)	0%	15%

TABLE II
GUIDELINES FOR DIVERSIFICATION
ACCORDING TO QUALITY OF CORPORATE DEBT INSTRUMENTS
AUTHORIZED BY TABLE I

<u>Instrument</u>	<u>Minimum</u>	<u>Maximum</u>
1. Corporate bonds and notes rated "AAA" or equivalent	0%	100%
2. Corporate bonds and notes rated "AA" or equivalent	0%	50%
3. Corporate bonds and notes rated "A" or equivalent	0%	30%
4. Commercial paper rated in highest grade ("P-1" or equivalent)	0%	20%

Any Corporate debt instrument that is downgraded following purchase may be liquidated at the Board of Investments discretion if such downgrading puts the debt instruments out of compliance with Table II.

TABLE A
GUIDELINES FOR DIVERSIFICATION
ACCORDING TO KIND OF INVESTMENT INSTRUMENT

<u>Instrument</u>	<u>Code Reference</u>	<u>Minimum</u>	<u>Maximum</u>
1. U. S. Government Obligation	§12-6-9(a)	15%	100%
2. Select U. S. Government Agency Obligation	§12-6-9(b)	0%	100%
3. Repurchase agreements	§12-6-5(9)	0%	75%
4. Reverse repurchase agreements	§12-6-5(10)	0%	15%

Section 6. Miscellaneous

6.1. Payment of Expenses from Earnings - The Board of Investments shall deduct expenses incurred in the administration of the Consolidated Fund from the gross earnings of the fund prior to distribution of the earnings. Such fees shall be established by the Board on a pro rata basis.

6.2. Reserve for Losses - The Board is authorized to establish, by appropriate accounting method, a reserve for loan losses. No interest shall be included in earnings calculations on any loans that are delinquent by sixty days or more, or for which the Board's staff determine collection to be doubtful.

6.3. Board Reports - The Board of Investments staff shall provide Board members monthly financial statements prepared in accordance with Generally Accepted Accounting Principles and financial schedules reflecting all purchases, sales and trades for each investment pool.

6.4. Authorized Financial Institutions and Brokers - The Board of Investments may not do business with any financial institution or brokerage firm that has not been approved by the Board. At the first Board meeting of each fiscal year, the Board's staff shall provide for the Board's review and approval a complete list of all financial institutions and brokerage firms for which the Board's staff request to transact business.

WEST VIRGINIA ADMINISTRATIVE REGULATIONS
West Virginia State Board of Investments

Chapter 12-6
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APPENDIX B

FISCAL NOTE FOR PROPOSED RULES

Rule Title: Administration of the Consolidated Fund by the WV State Board of Investments
 Type of Rule: X Legislative Interpretive Procedural
 Agency: WV State Board of Investments
 Address: State Capitol Building - Room E-122
Charleston, WV 25305

1. Effect of Proposed Rule

	ANNUAL FISCAL YEAR				
	INCREASE	DECREASE	CURRENT	NEXT	THEREAFTER
<u>ESTIMATED TOTAL COST</u>	\$	\$	\$	\$	\$
PERSONAL SERVICES					
CURRENT EXPENSE					
REPAIRS & ALTERNATIONS					
EQUIPMENT					
OTHER					

2. Explanation of above estimates:

These proposed rules are an amendment to the original rules effective July 1, 1994. It is not anticipated that these amended rules will require the expenditure of any additional funds.

3. Objectives of these rules:

These amended rules affect only the Enhanced Yield Pool. The maturity length is extended from 3 years to 5 years and the dollar weighted average-maturity was changed from 1 year to 2 years.

Rule Title: Administration of the Consolidated Fund by the WV State Board of Investments

4. Explanation of Overall Economic Impact of Proposed Rule.

A. Economic Impact on State Government.

These proposed rules will allow those State agencies participating in this pool to earn a higher rate of return on their investments.

B. Economic Impact on Political Subdivisions; Specific Industries; Specific groups of Citizens.

Currently no political subdivisions are investing in this pool.

C. Economic Impact on Citizens/Public at Large.

See 4A

Date:

1/6/96

Signature of Agency Head or Authorized Representative

