

# **THE TENNESSEE BACCALAUREATE EDUCATION SYSTEM TRUST FUND PROGRAM**

## **EDUCATIONAL INVESTMENT PLAN (“TNStars® College Savings 529 Program”) INVESTMENT POLICY REVISED AND RESTATED**

**NOTICE:** This document does not outline the investment risks, fees, expenses, terms, conditions, restrictions and other important information for TNStars’ Participants. Participants should obtain such information from the TNStars College Savings 529 Program Disclosure Brochure and through the prospectus and additional information provided by the underlying mutual fund company associated with any investment option to which a Participant is considering allocating contributions. The Disclosure Brochure and information on how to obtain prospectus information is available on the TNStars’ website, [www.tnstars.com](http://www.tnstars.com), or by contacting:

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## I. Definitions

The following definitions are used hereafter with respect to this Investment Policy:

**BEST Program** –Tennessee Baccalaureate Education System Trust Fund Program comprised of two types of qualified tuition plans: Educational Services Plan and the Educational Investment Plan.

**Board** – the Board of Trustees of the Baccalaureate Education System Trust Fund Program, also known as the “BEST Board” or “BEST Board of Trustees,” which is empowered under the Statute to carry out the purposes and objectives of the Tennessee Baccalaureate Education System Trust Fund Program.

**Consultant(s)** – An entity or individual, duly selected and contractually bound, with substantial experience in providing investment advice on and/or consulting services in the evaluation and selection of investment options. Such Consultant(s) will be appropriately registered, or exempt from registration, under the applicable state and federal securities laws, rules and regulations.

**Department of Treasury Staff** – Each Department of Treasury employee involved in the administration or management of the Tennessee Baccalaureate Education System Trust Fund Program. Department of Treasury Staff includes, but is not limited to, the State Treasurer, Chief Investment Officer and Program Director.

**Educational Investment Plan** – A plan that permits an account owner (Participant) to establish an educational investment trust account, to which one (1) or more contributors may make contributions, that is intended to be applied to a beneficiary's qualified higher education expenses. A Participant, will own units of interest issued under the TNStars College Savings 529 Program and not direct shares of the underlying mutual funds or interest in the interest bearing account related to, as applicable, the investment option(s) the Participant selects. Such units of interest are municipal fund securities, as defined by the Municipal Securities Rulemaking Board (“MSRB”).

**Participant** – an owner of an Educational Investment Plan account.

**TNStars** – TNStars College Savings 529 Program, a qualified tuition program offered by the State of Tennessee through the Educational Investment Plan. *See also Educational Investment Plan.*

**T.C.A.** – Tennessee Code Annotated.

**Underperforming Investment Option** –An investment option that is rated “underperforming” based on a performance analysis conducted by Consultant(s) and/or Department of Treasury Staff.

**Watch List** – A list maintained by the Department of Treasury Staff in order to efficiently track any Underperforming Investment Option.

## **II. Overview and Authority**

### **A. Introduction**

The Tennessee Baccalaureate Education System Trust Act (“Act”) was established by Chapter No. 388 of the Public Acts of 1995, approved June 12, 1995, for the purpose, in part, of encouraging the pursuit of, and financial planning for, higher education.. The Act created the Tennessee Baccalaureate Education System Trust Fund Program (“BEST Program”). As the BEST Program evolved, the Educational Investment Plan was created to assist families in saving and investing for the qualified higher education expenses of attending an eligible educational institution and thereby to encourage timely financial planning for and students’ participation in higher education.

While the Board is authorized under T.C.A. 49-7-808 to develop one or more plans under the Educational Investment Plan, the plan currently available is the TNStars College Savings 529 Program (“TNStars”).

### **B. Investment Authority**

The investments by the Educational Investment Plan shall be governed by the investment policies and guidelines (“Investment Policy”) adopted by the Board and by the requirements of T.C.A. § 49-7-814. Implementation of the Educational Investment Plan’s Investment Policy established by the Board is hereby delegated to the State Treasurer who shall put such policy into effect. In addition, the day-to-day operations and responsibilities of the BEST Program, including the Educational Investment Plan, are hereby delegated to the State Treasurer.

In implementing this Investment Policy and carrying out the day-to-day operations and responsibilities of the BEST Program, the State Treasurer has the authority to delegate certain responsibilities to the Chief Investment Officer, Program Director and Department of Treasury Staff.

### **C. Fiduciary Standard**

All assets of the Educational Investment Plan shall be invested and managed solely in the interest of the Educational Investment Plan’s Participants and in a manner consistent with the duty of loyalty found in T.C.A. §35-14-107, the prudent investor rule pursuant to T.C.A. §35-14-103 and the standard of care pursuant to T.C.A. §35-14-104. Furthermore, the delegation of investment and management functions shall be carried out in accordance with T.C.A. §35-14-111.

### **D. Scope**

The Investment Policy is binding on all persons and entities with authority over the Educational Investment Plan’s assets, including, but not limited to, the Board, Department of Treasury Staff and any other person who or entity that may have a fiduciary relationship with the Educational Investment Plan.

### **III. Objective**

The purpose of this Investment Policy is to support the Educational Investment Plan's primary purpose by:

- Outlining the distinct roles and responsibilities of the Board, Department of Treasury Staff and Consultant(s);
- Establishing investment criteria which the Board determines to be prudent and in the best interest of the Participants, for the selection, ongoing evaluation, and, if necessary, termination, of investment options;
- Communicating the Investment Policy, as approved by the Board, to the Department of Treasury Staff, Consultant(s) and any other person who or entity that may have a fiduciary relationship with the Educational Investment Plan; and
- Functioning as a supervisory tool, guiding the ongoing oversight of the investment options available under the Educational Investment Plan.

### **IV. Roles and Responsibilities**

In addition to the responsibilities described below and throughout the Investment Policy, the Consultant(s), as well as any other person who or entity that may have a fiduciary relationship with, or act as a service provider to, the Educational Investment Plan, may have additional duties and responsibilities outlined within federal and state laws, rules and regulations; executed contracts or agreements; or as dictated by standard business or industry practices.

#### **A. Board of Trustees**

- 1) Adopt an Investment Policy that establishes the investment criteria, which the Board determines to be prudent;
- 2) Delegate investment and management functions that a prudent trustee of comparable skills would properly delegate under the circumstances;
- 3) Evaluate the investment performance of the investment options, through reports supplied by the State Treasurer, Department of Treasury Staff, Consultant(s), and/or other service providers; and
- 4) Periodically review the actions taken by delegates in order to monitor performance and compliance with the terms of the delegation.

#### **B. State Treasurer**

- 1) Implement the Investment Policy, as approved by the Board;
- 2) Delegate investment and management functions that a prudent trustee of comparable skills would properly delegate under the circumstances;
- 1) Approve a prudent menu of investment options through the evaluation of the investments and recommendations made by the Chief Investment Officer and Department of Treasury Staff;
- 3) Review and, as applicable, authorize the use of Consultant(s), service providers and the employment of Department of Treasury Staff;
- 4) Evaluate and, as applicable, approve the processes employed and procedures established by Department of Treasury Staff;
- 5) With the advice and counsel, as applicable, of legal counsel, negotiate and execute all contracts, agreements, forms and memoranda of understanding

deemed necessary or desirable for the efficient administration of the Educational Investment Plan's assets;

- 6) Monitor the investment performance of the investment options; and
- 7) Take actions that are deemed essential to protect the assets and Participants of the Educational Investment Plan with any emergency actions being promptly reported to the Board.

### **C. Chief Investment Officer**

- 1) Assume executive responsibility and authority, as delegated by the State Treasurer, and undertake the necessary authority to effectively manage and supervise, as applicable;
- 2) Delegate investment functions to Department of Treasury Staff that a prudent trustee of comparable skills would properly delegate under the circumstances;
- 2) Create a prudent menu of investment options through the evaluation of the investments and recommendations made by Department of Treasury Staff, Consultant(s) and/or service provider(s);
- 3) Report to and consult with the State Treasurer and/or his designee on investment activities;
- 4) Collaborate, as applicable, with the Department of Treasury Staff, Consultant(s), and service providers on development and implementation of appropriate strategies, policies, and procedures;
- 5) Prepare and submit reports, as required, to document activities; and
- 6) Notify the State Treasurer of situations that merit the Board's attention.

### **D. Program Director**

- 7) Assume executive responsibility and authority, as delegated by the State Treasurer, and undertake the necessary authority to effectively manage and supervise the day-to-day operations of the BEST Program, as applicable;
- 8) Delegate functions to Department of Treasury Staff that a prudent trustee of comparable skills would properly delegate under the circumstances;
- 9) Report to and consult with the State Treasurer and/or his designee on administrative, organizational and management activities;
- 10) Collaborate, as applicable, with the Department of Treasury Staff, Consultant(s), and service providers on development and implementation of appropriate strategies, policies, and procedures;
- 11) Prepare and submit reports, as required, to document activities; and
- 12) Notify the State Treasurer of situations that merit the Board's attention.

### **E. Department of Treasury Staff**

- 3) Utilize special skills and expertise in an effort to accomplish the delegated or assigned task;
- 4) Evaluate the investment performance of the investment options, through reports supplied by the Consultant(s) and/or other service providers;
- 5) Assist the State Treasurer, or his designee, Chief Investment Officer and Program Director with respect to any matters related to the Educational Investment Plan;
- 6) Prepare and submit reports, as required, to document activities; and
- 7) Notify the State Treasurer of situations that merit his attention.

## **F. Consultant(s)**

- 1) Act in a fiduciary capacity in selecting investment options that are suitable for the Educational Investment Plan;
- 2) Source and evaluate prospective investment options on an as-needed or as-requested basis;
- 3) Prepare and submit relevant, reliable and timely investment and performance reports and objective advice as required or as needed by the Board, State Treasurer, Chief Investment Officer or Department of Treasury Staff; and
- 4) Support the Board, State Treasurer, Chief Investment Officer, Program Director or Department of Treasury Staff with respect to any matters related to the Educational Investment Plan.

## **V. Governing Principles**

### **A. Primary Investment Philosophy**

In the Educational Investment Plan, each Participant may have a different risk tolerance, investment horizon, college savings goals and overall investment objectives. As such, Educational Investment Plan Participants are responsible for their own investment decisions. To accommodate varying investment objectives, risk tolerances and time horizons, the Board seeks to provide Participants with a prudent menu of investment options that is diversified across a range of asset classes, risk levels and investment strategies and reasonable in cost when compared with other investment options with similar objectives.

### **B. Authorized Asset Classes and Investment Strategies**

Subject to the approval of the State Treasurer and all the terms, conditions, limitations and restrictions imposed, as applicable by this Investment Policy, the Board authorizes investment options, including but not limited to, the following major asset classes and investment strategies:

- Equity (Large-, Mid-, or Small-Cap)
  - Growth
  - Blend
  - Value
  - Specialty (e.g. sector, international, etc.)
- Fixed Income
  - Investment Grade (Short-, Intermediate-, or Long-Term)
  - Inflation-Protected
  - Specialty (e.g. high-yield, international, etc.)
- Balanced/Asset Allocation (asset allocation remains static)
- Age-Based/Lifecycle (assets reallocated, over time, based on a specific date; commonly referred to as glide path)
- Stable Value/ Fixed Account (or similar option that provides a guaranteed minimum rate of return or interest)

The Board acknowledges that the use of all of the above-referenced major asset classes and investment strategies may not be required in order to develop a prudent menu of investment options.

### **C. Authorized Investment Vehicles**

Subject to the approval of the State Treasurer and, as applicable, all the terms, conditions, limitations and restrictions imposed by this Investment Policy, the Board authorizes the following investment vehicles: mutual funds, exchange traded funds and fixed accounts.

### **D. Benchmarks**

Each investment option will be evaluated against its designated benchmark, index or respective peer group, as outlined in Appendix A. The appropriateness of each investment option's designated benchmark, index or respective peer group should be periodically evaluated by the Department of Treasury Staff and may be amended, subject to the approval of the State Treasurer.

### **E. Revenue Sharing, Distribution and Service Fees**

To offset the costs of administration, the Educational Investment Plan may receive payments known as offsets or administrative fee reimbursements from certain mutual fund companies. Any offsets received shall be used to a) reduce the overall expenses of the Educational Investment Plan or b) directly reimbursed or applied to the applicable Participant's account.

## **VI. Consultant(s) and Service Providers**

If determined to be in the best interest of the Educational Investment Plan, the State Treasurer is authorized to contract with financial consultants, actuaries, auditors, investment managers and other consultants and professionals as necessary to carry out the responsibilities of the Educational Investment Plan. The Board delegates to the State Treasurer the responsibility to determine the procurement method for such services or providers, including the general and technical qualifications. The State Treasurer shall also determine the duties and responsibilities of the providers with such duties and responsibilities enumerated in a contractual agreement.

## **VII. Selection Criteria for Investment Options**

The Board recognizes that various factors are taken into consideration when evaluating investment performance and the menu of investment options. The Board relies on the State Treasurer, Department of Treasury Staff and, if applicable, the Consultant(s) to use reasonable judgment in proactively and objectively evaluating each investment option.

### **A. Mutual Funds and Exchange Traded Funds**

Mutual funds and exchange traded funds must be publicly listed and may be either actively or passively managed. At the time of selection, a mutual fund or exchange traded fund must have:

- At least three (3) years of investment and operational history;
- Align with its respective benchmark, net of fees, over at least two of the most recent 1-, 3-, or 5-year periods; and
- An expense ratio competitive with other investment options with similar objectives.



## **B. Fixed Account**

A fixed account will generally guarantee a minimum rate of return or interest. Fixed accounts available through either a bank depository account must provide participant-level FDIC protection.

# **VIII. Monitoring and Reporting**

## **A. Quarterly**

After the end of each calendar quarter, or as deemed necessary by the Board, State Treasurer or Department of Treasury Staff, Department of Treasury Staff and/or selected service provider will provide a comprehensive performance report for each investment option.

Additionally, Department of Treasury Staff and/or selected service provider or Consultant(s) will complete a performance analysis for all of the investment options offered under the Educational Investment Plan. Such performance analysis will include, but is not limited to statistical measures of performance, risk, style consistency, and other criteria used to evaluate the relative success and stability of each investment option.

The performance reports and performance analysis will be reviewed and evaluated by the Department of Treasury Staff. During such evaluation, any investment option that has

- performed materially below benchmark and below universe median performance for both the 3-, and 5-year periods,
- for passive index mutual funds or commingled funds, materially failed to track the stated index,
- significant changes in ownership, management, investment objective or investment style,
- substantial portfolio turnover,
- material violations of federal or state law, policies or procedures, or
- excessive reoccurring administrative or operational issues

will be selected for further review by the Department of Treasury Staff and/or Consultant(s). *See Underperforming Investment Options for further information.*

## **B. Periodically**

The Board, State Treasurer, or Department of Treasury Staff may conduct, or request to be conducted, at any time a review or evaluation of an investment option.

## **C. Annually**

At least annually, the Department of Treasury Staff and/or selected service provider shall review the Investment Policy and overall investment performance (measured in 1-, 3-, and 5- cycles) of the investment options offered in the Educational Investment Plan and provide any recommendations to the State Treasurer.

## **IX. Underperforming Investment Options**

If an investment option has been selected for further review, Department of Treasury Staff and/or Consultant(s) will gather additional information related to the underperformance and/or event(s) triggering the review. Additionally, the applicable investment company or bank may be informed and/or invited to meet with Department of Treasury Staff and explain the underperformance or events and any remedial efforts.

If, based on such review, the State Treasurer and Department of Treasury Staff determine that the underperformance or event is material then the investment option will be placed on the Watch List. The investment option will remain on the Watch List and re-evaluated during the next quarter's performance analysis.

An investment option will be added to, removed from or remain on the Watch List based on each quarter's performance analysis. However, an investment option that is on the Watch list for four or more ( $\geq 4$ ) consecutive quarters or seven or more ( $\geq 7$ ) total (non-sequential) quarters in a trailing twelve (12) quarter period may be, at the State Treasurer's discretion,:

- closed to new contributions;
- phased out of the menu of available investment options; and/or
- terminated and its assets transferred to a new or existing investment option.

The Board and State Treasurer reserve the right to change, eliminate, or restrict any investment option and such actions do not require Participant consent. When feasible and appropriate, reasonable notice will be provided to Participants regarding any material changes to the menu of available investment options.

## **X. Program Management Fee**

The State Treasurer is hereby authorized to charge and collect reasonable administrative fees and charges in connect with the creation and maintenance of the educational investment trust accounts. This program management fee may include the costs, fees and expenses necessary or proper to incur in order to operate and administer the Educational Investment Plan.

## **XI. Other Considerations**

The Board, State Treasurer, Department of Treasury Staff, Consultant(s) and service providers are required to comply with all applicable federal and state laws, rules and regulations. The Investment Policy may reference or restate applicable laws, rules and regulations, or portions thereof, for convenience; however, in the event of any conflict between the law and this Investment Policy, the law prevails. Each fiduciary to the Educational Investment Plan is ultimately responsible for compliance with applicable laws, rules and regulations.

The Board hereby authorizes the State Treasurer to take, for and on behalf of the Educational Investment Plan, all actions necessary to comply with applicable federal and state securities laws, rules and regulations. In implementing such, the State Treasurer may delegate certain responsibilities to the Department of Treasury staff or service providers.

In cases of uncertainty, the State Treasurer is authorized to provide interpretive guidance and approve, from time to time, variances from the requirements contained within the Investment Policy, including immediate termination of an investment option or options, in furtherance of compliance or as deemed in the best interest of the Educational Investment Plan's Participants, consistent with both fiduciary standards and the scope of the Investment Policy. Such interpretive guidance or variance shall be reported in writing to the Board at its next meeting.

## **XII. Approval and Adoption**

The Board of Trustees of the Tennessee Baccalaureate Education System Trust Fund Program, hereby approved and adopted this revised and restated Investment Policy of the Educational Investment Plan at its meeting on the 31<sup>st</sup> day of March, 2016.



DAVID H. LILLARD, JR., CHAIRMAN  
BOARD OF TRUSTEES

Tennessee Baccalaureate Education System Trust Fund Program

## Appendix A – Investment Options and Designated Benchmarks as of March 24, 2016

<b>Investment Option</b>
TN PRIMECAP Odyssey Aggressive Growth Fund <b>Benchmark - S&amp;P Mid-Cap 400 Index</b>
TN Vanguard Mid-Cap Growth Fund (Investor Shares) <b>Benchmark - S&amp;P Mid-Cap 400 Index</b>
TN DFA Large Cap International Portfolio (Institutional Class) <b>Benchmark - MSCI World ex USA Index</b>
TN Vanguard 500 Index Fund (Admiral Shares) <b>Benchmark - S&amp;P Large-Cap 500 Index</b>
TN DFA US Small Cap Fund <b>Benchmark - Russell 2000</b>
TN DFA US Large Cap Value Fund <b>Benchmark S&amp;P Large-Cap 500 Index</b>
TN Vanguard Wellington Fund (Admiral Shares) <b>Benchmark - 65% S&amp;P 500 35% Barclays US Credit A or Better</b>
TN Vanguard LifeStrategy Conservative Growth Fund <b>Benchmark - 60% Barclays US Aggregate Index, 28% MSCI US Broad Market Index, 12% MSCI ACWI ex USA Index</b>
TN Vanguard LifeStrategy Income Fund <b>Benchmark - 80% Barclays US Aggregate Index, 14% MSCI US Broad Market Index, 6% MSCI ACWI ex USA Index</b>
TN Vanguard Intermediate-Term Investment-Grade Fund (Admiral Shares) <b>Benchmark - Barclays US 5-10 Year Credit Index</b>
TN Vanguard Intermediate-Term Treasury Fund (Admiral Shares) <b>Benchmark - Barclays US 5-10 Year Treasury Index</b>
TN Vanguard Total Bond Market Index Fund (Admiral Shares) <b>Benchmark - Barclays US Aggregate Index</b>
TN DFA Inflation-Protected Securities Portfolio (Institutional Class) <b>Benchmark - Barclays US TIPS Index</b>
TN First Tennessee Interest Bearing Account
<b>Age Band</b>
0-4 (DFA US Large Cap Value Fund) <b>Benchmark - S&amp;P Large-Cap 500 Index</b>
5-10 (Vanguard Wellington Fund (Admiral Shares)) <b>Benchmark - 65% S&amp;P 500 35% Barclays US Credit A or Better</b>
11-14 (Vanguard LifeStrategy Conservative Growth Fund) <b>Benchmark - 60% Barclays US Aggregate Index, 28% MSCI US Broad Market Index, 12% MSCI ACWI ex USA Index</b>
15-17 (Vanguard LifeStrategy Income Fund) <b>Benchmark - 80% Barclays US Aggregate Index, 14% MSCI US Broad Market Index, 6% MSCI ACWI ex USA Index</b>
18+ (Vanguard Total Bond Market Index Fund (Admiral Shares)) <b>Benchmark - Barclays US Aggregate Index</b>