

SUBJECT: Revising the Texas Tomorrow Fund program

COMMITTEE: Pensions and Investments — favorable, without amendment

VOTE: 8 ayes — Telford, Woolley, Goolsby, Rangel, Sadler, Serna, Tillery, Williams
0 nays
1 absent— Berlanga

WITNESSES: None

BACKGROUND : The 74th Legislature in 1995 established the Texas Tomorrow Fund to allow individuals or groups to prepay higher education tuition and fees at prices that are locked in at the time payments begin.

The Prepaid Higher Education Tuition Board is authorized to make investments according to the provisions of the 1995 Public Funds Investment Act. The act establishes a “prudent person” standard for investing in certain specified securities including federal securities, federally-backed securities, securities backed or fully guaranteed by state or local governments, certificates of deposit, fully collateralized repurchase agreements and bankers acceptances with a maturity of 270 days or less and certain mutual funds. The Public Funds Investment Act requires governmental entities to have a written investment policy, prohibits investment in certain types of “derivative” securities, establishes reporting requirements and requires investment pools to establish advisory boards and maintain a bond rating of at least AAA.

The 1995 act allows private entities to purchase tuition scholarships for economically needy students to be awarded by the tuition board. The board also established a non-profit direct-support organization (DSO) to receive gifts, grants and loans and to purchase scholarships.

DIGEST: HB 9 would allow state or local governments to purchase prepaid tuition scholarships to be awarded by the tuition board's direct-support organization (DSO) to students based on economic or academic criteria established by the

DSO. A prepaid tuition contract could be purchased without identifying a specific beneficiary. The state comptroller would be the executive director of the DSO.

The bill would eliminate the requirement that the Texas Tomorrow Fund be invested according to the Public Funds Investment Act. Investments would have to be made based on the “prudent person” standard, not for speculation but for permanent disposition of funds, considering probable income as well as probable safety of capital.

HB 9 also would make a number of other changes including:

- allowing tuition to be paid for students over the age of 18, as long as they are still enrolled in high school;
- specifying that program provisions track the Internal Revenue Code, including imposing penalties for refunds and imposing certain reporting and confidentiality requirements;
- adding to the list of creditors' claims from which money in the Texas Tomorrow Fund is exempted;
- providing that any refund of prepaid amounts go to the purchaser rather than the beneficiary; and
- allowing the transfer of prepaid tuition among any beneficiaries specified by the purchaser, removing the requirement that the beneficiaries be siblings, step-siblings, or half-siblings.

HB 9 would take immediate effect if finally approved by a two-thirds record vote of the membership in each house.

**SUPPORTERS
SAY:**

HB 9 would make several needed changes to enhance the Texas Tomorrow Fund program to help finance higher education for the students of Texas. Allowing the state and local governments to contribute to the Texas Tomorrow Fund would demonstrate the commitment state government and the citizens of Texas have to providing affordable higher education for students from all income levels. The public funds could draw down

significant private matching dollars, encouraging increased private contributions to the fund and providing tuition scholarships for a greater number of students.

A similar program enacted by the State of Florida has been very successful. In 1990, Florida appropriated \$1.2 million, with the full amount matched by private contributions. By 1995, a legislative appropriation of \$1 million drew \$3 million in private donations.

The Texas Tomorrow Fund mainly benefits middle class Texans who can afford to prepay tuition. Authorizing the DSO to award scholarships on behalf of the state would allow the benefits of the program to be shared with children from low-income families. Giving children an early guarantee of college tuition can be a highly motivating factor, increasing students' chances of succeeding in high school and college.

Although the Texas Tomorrow Fund has been successfully launched, some provisions of the program need clarification so that the fund can provide the best service for participants in the program and the best results for the citizens of Texas. Various changes proposed by HB 9 would increase program flexibility for purchasers and allow the greatest number of students to participate. For example, allowing students over the age of 18 to participate in the fund so long as they are still enrolled in high school would enable older students to have the same advantages as their younger counterparts.

HB 9 would also make various changes to ensure that payments under the prepaid tuition plan are not treated as taxable income nor that purchasers use the plan as a tax shelter. For example, returning any refunded money to purchasers instead of beneficiaries would prevent the tax-exempt fund from being used as a tax shelter. Various other changes would track language in Section 529 of the Internal Revenue Code to maintain the program's tax exempt status.

The Texas Tomorrow Fund would best be managed through long-term "prudent person" investment policies using sound, well-established principles. The Prepaid Higher Education Tuition Board that oversees the fund should be granted the same latitude for investing as for other funds,

such as the Employee Retirement and Teacher Retirement Systems and the Permanent University Fund, with similarly long-term investment cycles. The Public Funds Investment Act criteria are more appropriate for short-term investments.

OPPONENTS
SAY:

The state and local governments should not directly contribute to the Texas Tomorrow Fund. Despite rising costs, Texas has one of the country's most affordable higher education systems. In a time of financial uncertainty, it is unwise to begin subsidizing higher education for individual students by funding scholarships. Such activity is best left to the private sector.

HB 9 outlines the parameters of the Texas tomorrow scholarship program only in the vaguest terms. It would allow the DSO to establish the economic and academic terms on which scholarships were awarded, but would provide no guidelines or standards for awards except the existing requirement that the recipients not be delinquents.

The Texas Tomorrow Fund should not be invested using the broad “prudent person” investment authority. The money in the fund should be invested with utmost caution in sound, safe investment securities provided for in the Public Funds Investment Act.

NOTES:

HJR 8, HB 8, and HB 634, also relating to the Texas Tomorrow Fund, are on today's calendar for second readings.

The Senate companion bill, SB 782 by Barrientos et al., has been referred to the Finance Committee.