HOUSE
RESEARCH
ORGANIZATION bill analysis 4/24/2003

HB 471
Pickett, et al.

SUBJECT: Allowing short-term borrowing to meet TxDOT's cash-flow needs

COMMITTEE: Appropriations — favorable, with amendment

VOTE: 18 ayes — Heflin, B. Brown, F. Brown, Crownover, Deshotel, Ellis, Gutierrez, Hamric, E. Jones, Menendez, Pickett, Pitts, Raymond, Solis, Stick, Truitt, Turner, Wohlgemuth

0 nays

11 absent — Luna, Berman, Branch, J. Davis, Dukes, Eiland, Hope, Hupp, Isett, Kolkhorst, McClendon

WITNESSES: For — Tom Johnson, Associated General Contractors of Texas; Steve Stagner, Texas Council of Engineering Companies

Against — None

On — James Bass and Michael Behrens, Texas Department of Transportation

BACKGROUND: The Texas Transportation Commission (TTC) is appointed by the governor as the policymaking body for the Texas Department of Transportation (TxDOT). Most of TxDOT's budget comes from federal highway reimbursements and legislative appropriations from the state highway fund, much of which comes from sources dedicated by the Texas Constitution.

Under Government Code, ch. 404, subch. H, the comptroller may issue tax and revenue anticipation notes to cover short-term cash flow deficits, with the approval of the Cash Management Committee. The committee members include the governor, lieutenant governor, House speaker, and comptroller.

DIGEST: (*The author plans to offer a floor substitute, which the Digest summarizes in lieu of HB 471, as amended.*)

HB 471 would allow the TTC to undertake short-term borrowing in the form of loans or notes to cover TxDOT operations. Loans could take the form of agreements, notes, contracts, or other forms as determined by the TTC. Loan provisions would be up to the TTC, except that terms could not exceed two years, and loan amounts, including any balances outstanding on other loans, could not exceed the average monthly revenue deposited into the highway fund for the 12 months preceding the month in which the loan was executed. Loans would not create a general obligation of the state but would be payable only as authorized by legislative appropriation.

The two-year repayment term also would apply to any notes issued by the TTC. The bill would specify that highway fund appropriations could be spent to repay loans.

HB 471 also would authorize TxDOT to issue highway tax and revenue anticipation notes (HTRANs) to cover anticipated temporary cash-flow shortfalls in the highway fund during any fiscal year. Subject to approval of the Cash Management Committee, the TTC could issue, sell, and deliver such notes on the state's behalf. The TTC would have to submit to the committee a cash-flow shortfall forecast containing a detailed report of estimated revenue and expenditures. Based on that forecast, the committee could approve note issuance in an amount not to exceed the maximum shortfall amount.

Notes would not be state debts and could be used only for highway fund cash-flow shortfalls. All notes would have to be repaid in full during the fiscal biennium in which they were issued. Note proceeds and credit agreement proceeds would have to be deposited in a special interest-bearing fund in the treasury that the comptroller could invest. TxDOT would have to transfer net proceeds from that fund to the highway fund as needed to pay authorized expenditures.

Notes would be subject to review and approval by the attorney general but not by the Bond Review Board. The comptroller could assist the TTC with note issuance on request. TxDOT's HTRANs fund money could be pledged to secure note payments, performance of obligations under credit agreements relating to notes, issuance costs, and rebates to the federal government.

TxDOT periodically would have to transfer cash from the highway fund to its HTRANs fund to ensure timely payment of notes. Any money remaining in the HTRANs fund after payment of all outstanding notes, federal rebates, and issuance costs would have to be transferred to the highway fund. If funds were insufficient to pay these costs, the Legislature could appropriate money from the highway fund to cover them.

HB 471 would appropriate to TxDOT for fiscal 2004-05 all money deposited in the HTRANs fund during that biennium, as well as amounts from the highway fund necessary to cover any insufficiencies in the HTRANs fund to pay principal, premium or interest, or issuance costs of notes.

The bill would take effect September 1, 2003, except that the short-term loan provisions would take effect when the proposed constitutional amendment (HJR 28 by Pickett, et al.) authorizing TxDOT borrowing took effect (at canvassing). The section would not take effect if voters did not approve the constitutional amendment.

SUPPORTERS SAY:

HB 471, as amended, would help TxDOT deal with short-term cash flow problems. Transportation funding continues to lag behind demand. The vicissitudes of federal highway funding reimbursements and the seasonal nature of road building contribute to cash-flow problems at TxDOT. Outstanding contracts totaling up to $7 billion and unpredictable weather make it difficult to forecast cash flow.

Sometimes, overabundant funds can cause shortfalls. In October 2001, for example, TxDOT paid out more than $300 million due to an unusually high volume of road work and right-of-way acquisition. On one day that month, the highway fund balance dipped to $4 million. This situation delayed payments to some contractors and vendors, hurting small companies particularly, and led to a temporary suspension of many new projects. State agencies must be able to meet their obligations, and Texas motorists and business interests cannot afford unnecessary road work stoppages.

HB 471 is predicated largely on adoption and voter approval of HJR 28, a proposed constitutional amendment authorizing short-term borrowing by TxDOT. The bill would implement the comptroller’s recommendation to allow TxDOT to issue revenue-based notes or take out loans from public or private sources to meet short-term needs created by its unique cash-flow dynamics.

Giving TxDOT the flexibility to obtain loans from private capital markets would inject competition into the process. With interest rates at historic lows, this could save the state significant interest costs. Regardless, the Legislature could appropriate repayment from dedicated revenue in the highway fund. The borrowing limit, two-year time limit, and the restriction precluding new borrowing until some repayment had been made would provide proper safeguards for taxpayers' money.

The highway tax and revenue anticipation notes (HTRANs) proposed for TxDOT would function like those issued by the comptroller to meet other state agencies' periodic cash-flow shortfalls. If voters approved the constitutional amendment proposed by HJR 28, however, HB 471 would give TxDOT much-needed additional flexibility. Any notes issued by TxDOT could be repaid across biennia. If the resolution failed or if voters rejected the amendment, notes would have to be repaid during the biennium in which they were issued. Doing otherwise would create an unconstitutional debt, because the notes would not be repaid from current revenue. Even such a limited borrowing authority, however, would improve TxDOT's cash flow.

Although the bill would place no restrictions on lenders, it would emphasize borrowing against the highway fund, not from hard-pressed general revenue. Treasury loans probably could not be made because the amended bill no longer would give the comptroller contractual authority to do so. Nevertheless, the bill would not increase the state debt load because the state's full faith and credit would not be pledged, and repayment would have to be appropriated specifically.

This new borrowing authority would function much like a line of credit. It would be based on revenue that TxDOT needed at a particular time and might not have on hand but would have in the near future. Short-term borrowing would not generate new revenue or fund additional projects. Unlike bonds, it is a cash management tool, not a funding mechanism. Although the borrowing limit would fluctuate from month to month — the Legislative Budget Board put the initial estimate at $476 million — it would be a reasonable maximum given the magnitude of TxDOT's operations.

This cushion would enable TxDOT to manage its cash position more aggressively and focus less on managing to the lowest daily balance. This would reduce concerns about spending beyond day-to-day available cash balances.

Short-term borrowing also should improve project readiness and speed of delivery. Although it is difficult to quantify, a tangible value is inherent in starting projects earlier and completing them sooner. Cost savings include lower prices due to the reduced impact of inflation, with the added benefit of interest earned on those savings. The result would be a net financial gain to TxDOT, according to the comptroller, and an economic boon to the state from lower opportunity costs due to quicker turnaround.

TxDOT realizes that it needs to improve its cash forecasting methods. It also has taken steps to reduce interest paid on late payments, noting that its total costs to date are less than 1 percent of the amount TxDOT spent on highway contracting, according to a recent news article.

OPPONENTS SAY:

With the state in a dire fiscal situation, this is the wrong time to be increasing debt, even if it is backed by dedicated revenue. Short-term borrowing would require appropriations the state cannot afford to be spending on interest, however low the rates. Borrowing would increase TxDOT's costs in terms of forgone interest earned on cash balances and in interest charges for new borrowing. Whether TxDOT actually could speed up projects and realize any savings is uncertain at best.

No other state agency in Texas engages in short-term borrowing to pay for its daily operations. While the Comptroller's Office issues tax and revenue anticipation notes, it does so not to cover its own expenses, but so it can pay other agencies' bills and fulfill state obligations on time.

TxDOT is a $6 billion-per-biennium agency with a constitutionally dedicated revenue source, yet it cannot manage its budget effectively. According to the state auditor's March 2003 report, TxDOT needs to improve the accuracy of its cash management methodology to maximize available funds. The highway fund audit discovered that, between September 1999 and September 2002, TxDOT's three-month forecast of lowest daily balances was off by an average of 258 percent. A recent news report citing the comptroller identified TxDOT as having paid more interest on late payments to vendors than any other state agency — more than $900,000 since April 2000, when a state law requiring interest on late payments took effect. This kind of performance should not be rewarded with short-term borrowing authority or credit.

OTHER OPPONENTS SAY:

Rather than "hedge its bets" on amending the Constitution, the Legislature should choose which borrowing mechanism is most appropriate and see how well TxDOT handles it during the next biennium.

The floating maximum borrowing limit would be too unpredictable, even with the inclusion of outstanding loan balances. It could go much higher, particularly if Congress increases Texas' share of federal highway funds in the upcoming spending reauthorization. A lower ceiling would be more prudent during times of economic uncertainty.

NOTES:

As filed, HB 471 would have authorized the TTC to borrow money from the state treasury or any other source to carry out TxDOT's functions. A contract for a loan could have contained any provisions that TxDOT considered appropriate, but the loan term could not have exceeded five years. The comptroller could have contracted with TxDOT for a loan, other than from the highway fund. The committee amended the filed version by changing the limit on the loan term from five years to two years.

The author's floor amendment would delete a reference to the state treasury as a lender, along with the provision authorizing the comptroller to contract with TxDOT on treasury loans of undedicated funds. The amendment would define loans as agreements, notes, contracts, or other forms determined by TTC, and would grant the TTC borrowing authority as opposed to allowing it to authorize TxDOT to borrow money. It would authorize spending from the highway fund for loan repayment.

The floor amendment would add a new subchapter to Transportation Code, chapter 201, authorizing highway tax and revenue anticipation notes (HTRANs) and would apply the two-year loan term to them. The amendment would set forth the purposes and procedures for and by which HTRANs would be authorized, issued, spent, and repaid, including interest earned and transfers to and from the highway fund as needed. The amendment would appropriate HTRANs proceeds to TxDOT for fiscal 2004-05 and any highway fund money needed to cover HTRANs costs.

HJR 28 by Pickett, et al., which would amend the Constitution to allow authorization of short-term borrowing by TxDOT, is on today's Constitutional Amendments Calendar.

The companion bill, SB 831 by Lucio, has been referred to the Senate Infrastructure Development and Security Committee.