HOUSE RESEARCH ORGANIZATION bill analysis 5/25/2021

SB 1232 (2nd reading)
Taylor
(Bonnen)

SUBJECT: Creating Texas Permanent School Fund Corporation to manage PSF

COMMITTEE: Appropriations — favorable, without amendment

VOTE: 19 ayes — Bonnen, Ashby, C. Bell, Capriglione, Gates, Holland, Howard, A. Johnson, Jarvis Johnson, Julie Johnson, Minjarez, Morrison, Schaefer, E. Thompson, Toth, VanDeaver, Walle, Wilson, Wu

0 nays

8 absent — M. González, Dean, Dominguez, Raney, Rose, Sherman, Stucky, Zwiener

SENATE VOTE: On final passage, May 6 — 30-0

WITNESSES: For — John Hryhorchuk, Texas 2036; (*Registered, but did not testify*: Leticia Van de Putte, San Antonio Chamber of Commerce; Gilbert Zavala, The Greater Austin Chamber of Commerce)

Against — (*Registered, but did not testify*: Dena Donaldson, Texas American Federation of Teachers; Laura Atlas Kravitz, Texas State Teachers Association; Dorothy Ann Compton)

On — Jeff Gordon, General Land Office; Keven Ellis and Tom Maynard, State Board of Education; Todd Williams, School Land Board; Mike Meyer and Holland Timmins, Texas Education Agency; (*Registered, but did not testify*: Chuck Campbell, State Board of Education/Permanent School Fund)

BACKGROUND: The Texas Constitution of 1876 established the Permanent School Fund (PSF) and transferred half of the public lands owned by the state to the PSF as an endowment to provide a perpetual source of funding for public education. The State Board of Education (SBOE) manages financial assets for the PSF and the School Land Board (SLB), an independent entity of the General Land Office, oversees the management, sale, and leasing of more than 13 million acres of PSF land.

The 86th Legislature in 2019 enacted HB 4388 by Murphy, which created the PSF Liquid Account in the state treasury to be used by the SLB and SBOE. The law authorizes the SBOE to invest the funds in liquid assets.

DIGEST:

SB 1232 would create the Texas Permanent School Fund Corporation to manage the Permanent School Fund (PSF) and the Charter District Bond Guarantee Reserve Fund. It would require the transfer of certain revenue from the School Land Board to the corporation, and repeal requirements for a PSF Liquid Account.

PSF Corporation. SB 1232 would authorize the State Board of Education (SBOE) to incorporate the Texas Permanent School Fund Corporation and delegate to the corporation the board's authority to manage and invest the PSF and the Charter District Bond Guarantee Reserve Fund. The SBOE would have to adopt the initial articles of incorporation for the corporation.

The corporation would be a special-purpose governmental corporation and instrumentality of the state with necessary and implied powers to accomplish its purpose. The corporation could engage in any activity necessary to manage PSF investments, including entering into any contract, to the extent the activity complied with applicable fiduciary duties. It also could delegate investment authority to one or more private professional investment managers.

Membership. The board of directors would be composed of the following nine members:

- five members of the SBOE, appointed by the board;
- the commissioner of the General Land Office (GLO);
- one member appointed by the GLO commissioner who had substantial background and expertise in investments and asset management; and
- two members appointed by the governor, with the advice and consent of the Senate, from a list of three individuals nominated by

the SBOE and three individuals nominated by the School Land Board, each of whom would have to have substantial background and expertise in investments and asset management and could not be members of either board.

The SBOE by rule would establish the terms of the members it appointed. Members appointed by the GLO commissioner and the governor would serve staggered six-year terms, with the term of one member expiring on January 1 of each odd-numbered year.

The board would have to elect officers in accordance with the corporation's bylaws, and would have to meet at least three times per year. The board would have to develop written investment objectives for the PSF and employ a well-recognized performance measurement service to evaluate and analyze investment results.

Chief executive officer. The board would have to determine a hiring process to employ a chief executive officer, who would carry out duties as specified in the bill. The CEO could appoint an internal auditor, who would have to be approved by the board.

Immunity, insurance. The corporation, its officers and employees, and the board would be entitled to sovereign immunity to the same extent as any other state agency. The corporation could purchase or acquire liability insurance to protect board members and employees.

Conflicts of interest. The board would have to adopt an ethics policy that provided standards of conduct related to the management and investment of the PSF, including requirements for disclosure and other provisions specified in the bill. The board would have to define the types of relationships that could create a possible conflict of interest.

Open meetings. The board would be subject to state open meetings laws. It could conduct a closed meeting to deliberate or confer with one or more employees, consultants, or its legal counsel or with third parties relating to investment transactions, restricted securities, and procurement under certain conditions as specified in the bill.

Applicability of certain laws. The corporation would be exempted from:

- state laws classifying employee positions and regulating travel expenses, to the extent the board determined that an exemption would be necessary to perform the board's fiduciary duties;
- all state laws regulating or limiting purchasing by state agencies;
- the franchise tax; and
- any filing costs or other fees imposed by the state on a corporation.

School Land Board. The bill would require the School Land Board (SLB) to transfer all revenue derived from mineral or royalty interest, less any amounts specified by appropriation to be retained by the SLB, to the corporation for investment in the PSF. The bill would abolish the PSF Liquid Account.

Investment standards. The bill would remove existing regulations regarding the manner in which the SBOE may invest the PSF and subject the investment only to the prudent investor standard established in the Texas Constitution.

SB 1232 would require the Texas PSF Corporation to submit an annual audit report of corporation operations to the Legislative Budget Board (LBB) and an annual investment report on the allocation of assets and investment performance to the SBOE and GLO.

Distributions to ASF. Under SB 1232, the Texas PSF Corporation could make distributions from the PSF to the Available School Fund (ASF) in an amount not to exceed the constitutional limitation. In establishing an annual minimum distribution rate to the ASF, the corporation could consider the constitutional requirements, factors related to current and future public school students, and any other relevant factors.

Not later than November 1 of each even-numbered year, the corporation would have to submit to the Legislature, comptroller, SBOE, and LBB a report that detailed certain information about the transfer.

Bond guarantee program. The corporation, SBOE, and Texas Education Agency would have to coordinate to determine the corporation's role in the operation and management of the PSF in connection with the bond guarantee program for charter districts to ensure the proper and efficient operation of the program.

SB 1232 would establish timelines for transfers of powers, duties, functions, programs, and activities of the SBOE and SLB relating to the management and investment of the PSF to the corporation.

The bill would take effect September 1, 2021.

SUPPORTERS SAY:

SB 1232 would boost funding for public education by improving the management of the $48 billion Permanent School Fund (PSF). The bill would provide unified management of the fund's assets by creating the Texas Permanent School Fund Corporation. While the fund is considered the largest of its kind in the United States, its return on investments has lagged behind similar endowments. The new corporation is designed to operate in a manner similar to the way UTIMCO manages the Permanent University Fund, which grew at 118 percent over 20 years compared to 76 percent for the PSF.

Part of the reason for the lower performance of the PSF is the split management of the fund between two entities. The State Board of Education (SBOE) manages about two-thirds of the fund and the School Land Board, an independent entity of the General Land Office (GLO), manages the other third. The SLB under current law has a more restricted pool of investment options. Splitting the investment process has caused the state to miss out on investment returns due to different collateral requirements and investment options.

The bill would maintain the constitutional requirements for the SBOE and GLO while combining PSF funds in the new government corporation. The bill would streamline PSF investment management into one jointly managed investment pool that would reduce state costs, protect against asset allocation risks, and allow for greater investment growth. By repealing a statutory requirement that certain assets be held in a liquid account, the bill would free up as much as $4 billion for longer-term investment. The bill is expected to result in more than $100 million added to the PSF each year.

While some say that appointed officials should not have a role in overseeing the PSF, the majority of the new corporation's governing board would be elected SBOE members, and the governor's appointees would have to come from a list of individuals recommended by the SBOE and School Land Board.

CRITICS SAY:

SB 1232 would unnecessarily change the historic control of the PSF from the SBOE to a new government corporation even as the endowed fund has performed well and grown to $48 billion. The purpose of the constitutionally dedicated PSF is not to grow exponentially but to provide a steady guarantee that future generations of Texans will have education funding. The bill would remove management of fund assets from the elected SBOE to a new entity that would be governed by a board that would include some gubernatorial appointees, creating the potential for private interests to gain involvement in managing this important public asset.

NOTES:

Because of uncertainty regarding future returns on investment and fund distributions, the Legislative Budget Board states that the fiscal implications of the bill cannot be determined.