

Stat Board of Education

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RQ-0582-JC

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July 26, 2002

Honorable John Cornyn
Texas Attorney General
Price Daniel Building
P.O. Box 12548
Austin, Texas 78711

Re: Enclosed Request for Opinion

Dear General Cornyn:

I have enclosed a request for an attorney general's opinion submitted by several members of the State Board of Education regarding Riders 38 and 90 of the Texas Education Agency appropriation in the current appropriations act. The request was drafted by an ad hoc committee of the State Board of Education consisting of Mr. Rene Nunez, Dr. Alma Allen, Mrs. Geraldine Miller, and Mrs. Judy Strickland and chaired by Mr. David Bradley.

You will also find enclosed correspondence received and sent by the Board concerning the two riders in question, as well as a copy of the Memorandum of Commitment referenced in Rider 90. Please consider this request and provide us an opinion answering the questions posed. Because of the need to properly budget for external fund managers during the next fiscal year, we would very much appreciate an answer at your earliest convenience.

Sincerely,

Grace Shore

Grace Shore, Chair
State Board of Education

cc: Dr. Felipe Alanis, Commissioner of Education
Members, State Board of Education

Enclosures:

Letter from Grace Shore to Lt. Governor Bill Ratliff, Speaker Pete Laney and Carole Keeton Rylander, Comptroller of Public Accounts, dated April 1, 2002 (w/ encl.).

Letter from Sen. Rodney Ellis and Rep. Rob Junell to Lt. Governor Ratliff, Speaker Laney and Comptroller Rylander dated April 11, 2002.

Letter from Comptroller Rylander to Sen. Ellis and Rep. Junell dated April 12, 2002.

Letter from Comptroller Rylander to Grace Shore dated April 15, 2002.

Letter from Lt. Governor Ratliff and Speaker Laney to Grace Shore dated April 18, 2002.

Letter from Mr. David Bradley to Comptroller Rylander dated May 1, 2002.

Letter from Comptroller Rylander to Mr. David Bradley dated May 9, 2002.

Report by Callan Associates dated March 19, 2002, "Investment Manager Fee Shortfall for 2001-2003 Biennium" (referenced in Mr. Bradley's letter to Comptroller Rylander).

Questions for the Texas Attorney General

The State Board of Education (SBOE) has adopted a specific investment asset allocation policy to manage the assets of the Permanent School Fund (PSF). This policy determines both the investment strategies and asset allocations to external investment managers to most ably comply with the requirements of the Texas Constitution and to create adequate revenues to be distributed through the Available School Fund (ASF).

The questions before us arose when Texas Education Agency (TEA) staff recently recommended that the State Board of Education dramatically restructure its asset allocation policy and eliminate certain external investment management allocations.

The TEA's recommendations stem from its contention that funds will not be available to pay the SBOE's external managers, based on the assertion that the additional income goal mentioned in Rider 90 of Title 3 of S.B. 1 must be met before funds can be expended as appropriated in Rider 38.

Issue A:

Rider 38 is a specific appropriations vehicle enabling the State Board of Education to expend Available School Funds (ASF) in excess of the Comptroller's Biennial Revenue Estimate (BRE) to cover internal costs and the payment of external investment managers employed by the State Board of Education. Rider 38 provides:

Permanent School Fund: External Management Fees.

Contingent on the State Board of Education adopting asset allocation and investment policies for the Permanent School Fund that produce income to the Available School Fund for support of appropriations above for Strategies A.2.1, FSP - Equalized Operations and C.1.2, School Finance

System Operations, in excess of the amounts estimated in the Biennial Revenue Estimate prepared by the Comptroller of Public Accounts for the 2002–03 biennium, **additional income** projected by the Board for the Available School Fund from Permanent School Fund investments **is appropriated** to Strategy C.1.2, School Finance System Operations, for expenditure for internal costs and fees for external management of Permanent School Fund assets.

The additional amounts appropriated for external management costs may not exceed .5 percent of market value of funds placed with external managers and may not be transferred to any other strategy within Goal C, Texas Education Agency Operations, or to Goal D, Indirect Administration. The amounts appropriated shall be made available for expenditure on a quarterly basis. Appropriations for external management costs may only be expended if the Board awards contracts for external management services on an open, formal request for proposal process, which gives consideration to both performance and price. (Rider 38, General Appropriations Act, Article III, Emphasis added.)

As opposed to Rider 38, Rider 90 is a general commitment only to attempt to reach an overall goal. The SBOE delivered the subject memorandum to the Comptroller in Fall 2001. Rider 90 provides:

Available School Fund. The State Board of Education shall provide to the Comptroller of Public Accounts a memorandum of commitment indicating that changes in the Permanent School Fund investment strategy will result in an additional \$150,000,000 in the 2002–03 biennium over the Comptroller’s official estimate of Permanent School Fund interest, dividend, and other revenue earnings as reported in the 2002–03 Biennial Revenue Estimate or, if applicable, in the latest succeeding official revenue estimate issued by the Comptroller prior to the date of the agreement. (Rider 90, General Appropriations Act, Article III)

As is obvious from the above language, Rider 90 in no way references Rider 38, nor is there any apparent relationship between the two provisions. Note also that Rider 38 twice addresses contingency, but never mentions nor alludes to Rider 90, by inference or otherwise.

On May 28, 2002, TEA legal counsel explained to the SBOE that Section 6.05 of the Appropriations Act indicates that legislative intent is determined by the chairmen of the legislative committees:

Well, the opinions definitely and especially from the legislators do demonstrate legislative intent. And, furthermore, in the Appropriations Act we have a Section 6.05 which indicates to agencies that if you cannot figure out what the legislative intent was, you need to go to the chairs of the legislative committees who were in charge of that particular provision and ask them for their legislative intent. (Joan Allen, TEA legal counsel, May 28, 2002)

However, upon examining the actual language of Section 6.05, we find it instead provides that discussions had during the committee proceedings govern legislative intent:

Interpretation of Legislative Intent. Funds appropriated by this Act shall be expended as nearly as practicable, for the purposes for which appropriated. In the event an agency cannot determine legislative purpose from the patterns of appropriations, the agency shall seek to determine that purpose from the proceedings of the legislative committees responsible for proposing appropriations for this state. (General Appropriations Act, Article IX, Sec. 6.05)

Nowhere in the recordings of the House, Senate or Conference Committee proceedings is any reference made to Rider 90 superseding Rider 38, nor is there any discussion of any relationship between the two riders. Clearly, at the time the two riders were discussed and adopted, the legislative committees did not intend to subjugate Rider 38 to Rider 90.

Additionally, because Rider 38 is a specific appropriation, while Rider 90 is a general commitment to attempt to reach an amount, even if the two items were contained within one appropriation rider, which they are not, the very general nature of Rider 90 cannot and does not supersede nor override the specific provisions of Rider 38.

It is estimated that the available revenues from Permanent School Fund (PSF) investments will exceed the Biennial Revenue Estimate (BRE). It is also estimated that adequate excess revenues will be available to pay the PSF external management fees.

Because PSF revenues exceed the BRE, and because the Board awarded the contracts for external management services in accordance with Rider 38, it is our understanding that the provisions of Rider 38 take effect: "*additional income . . . is appropriated*" to payment of the external management fees.

Based upon the foregoing, WE ASK:

Question Number 1:

Does Rider 90 require that the PSF produce an additional \$150,000,000; or does Rider 90 require that the SBOE provide a memorandum of commitment to the Comptroller of Public Accounts?

Question Number 2:

Is the expenditure of funds appropriated in Rider 38 contingent on the PSF producing the \$150,000,000 identified in Rider 90?

Issue B:

In providing administrative services to the SBOE, the TEA certifies and forwards invoices to the Comptroller for payment. TEA staff has stated unequivocally that the funds appropriated in Rider 38 are unavailable for expenditure as authorized by the SBOE.

Directing the expenditure of funds under Rider 38, of course, is necessarily predicated on the Board's authority and responsibility to manage the assets of the Permanent School Fund mandated in Article VII, Section 5(d) of the Texas Constitution:

(d) Notwithstanding any other provision of this constitution, in managing the assets of the permanent school fund, the State Board of Education may acquire, exchange, sell, supervise, manage, or retain, **through procedures and subject to restrictions it establishes and in amounts it considers appropriate,** any kind of investment, including investments in the Texas growth fund created by Article XVI, Section 70, of this constitution, that persons of ordinary prudence, discretion, and intelligence, exercising the judgment and care under the circumstances then prevailing, acquire or retain for their own account in the management of their affairs, not in regard to speculation but in regard to the permanent disposition of their funds, considering the probable income as well as the probable safety of their capital. [Emphasis added.]

Chapter 43 of the Texas Education Code is even more specific in its delineation of SBOE authority. Texas Education Code, Section 43.0006(a) provides:

(a) The State Board of Education may delegate investment authority and contract for the investment of the permanent school fund to the same extent as the governing board of an institution of higher education with respect to an institutional fund under Chapter 163, Property Code.

Chapter 163.006(2) and (3) of the Property Code provide that the State Board of Education may:

(2) **contract with** independent investment advisors, investment counsel, investment managers, banks, or trust companies to act for the board in investment of institutional funds; and

(3) **authorize payment** of compensation for investment advisory or management services.

Were the TEA, contrary to the directions of the SBOE, to withhold or limit in any manner the payment of fees and/or expenses to the SBOE's external investment

managers, investment advisory committee members, investment advisors, investment counsel, banks, trust companies, and/or any service provider whose services the SBOE contracts or employs in accordance with its constitutionally mandated fiduciary responsibilities, not only would the TEA interfere with the contractual relationships entered into by the SBOE; but the TEA would, in effect, force the SBOE to breach its contracts and thereby open the State up to suits of breach of contract.

Additionally, such withholding or limiting of fee payments would restructure asset allocation and/or investment strategies contrary to those previously set by the SBOE. To limit and/or withhold expenditure of fee payments or expenses would thus prohibit the Board from exercising its authority and usurp from the SBOE its constitutional responsibility to manage the assets of the PSF.

Clearly, (a) the Constitution and Chapter 43 of the Texas Education Code give the State Board of Education specific management authority and responsibility for the assets of the Permanent School Fund; and (b) Chapter 163 of the Property Code authorizes the SBOE to enter into contracts and to authorize payment of funds for that task.

Based upon the foregoing, WE ASK:

Question Number 3:

Can the TEA refuse to follow the directions of the SBOE, toward fulfilling the Board's Constitutional and legal obligations, to facilitate the expenditure of funds appropriated therefor?