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Greg Abbott  
Office of the Attorney General of Texas  
P.O. Box 12548  
300 W. 15<sup>th</sup> Street  
Austin, Texas 78711-2548

RD-0364-GA

**Re: Attorney General Opinion Request from Chambers County Pertaining to Its  
County School Land and School Funds**

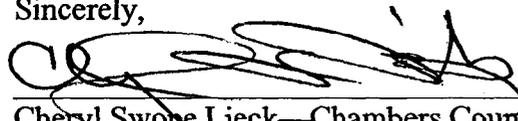
Dear Mr. Abbott:

Pursuant to Sections 402.042 and 402.043 of the Texas Government Code, Chambers County requests an Attorney General Opinion on the following issues:

1. Does Texas law permit Chambers County to hire a qualified bank under the Public Funds Investment Act to invest and manage the permanent and available county school funds?
2. If so, can Chambers County delegate to the qualified bank all decision-making authority to make prudent investments with the county school funds?
3. Does Texas law permit Chambers County to deduct the administrative costs charged by the qualified bank from the county available school fund or from the money raised by the Chambers County School Equalization Tax?

Attached is a brief that analyzes these issues. The brief sets forth the actual facts that pertain to the issues raised above, and the arguments in favor of Chambers County's proposed plan. Please do not hesitate to call me if you have any questions.

Sincerely,

  
Cheryl Swope Lieck—Chambers County Attorney

  
Jerry Sparks—Chambers County Auditor

## **BRIEF**

### **I. FACTUAL BACKGROUND**

In the mid 1800s, the State of Texas gave counties school land for the benefit of the public schools. Chambers County was one of the fortunate counties that received school land. Pursuant to Texas law, Chambers County has held the school land in trust for the benefit of its schools for over 100 years. Interestingly, Chambers County is one of the few counties in Texas that kept the school land over the years.

Chambers County's school land is physically located in Crockett County, Texas. Over the years, Chambers County has generated income from the school land by leasing the land for oil and gas production, grazing and hunting. Revenues from these leases have been collected in an account commonly referred to as the "permanent school fund". The permanent school fund has been invested over the years in United States treasury bills, certificates of deposit, and bonds. Income from these investments has been set aside into a separate account, which is commonly referred to as the "available school fund". The money in the available school fund is distributed to the four school districts in Chambers County once or twice per year based on student populations.

The amount of the permanent school fund has grown exponentially over the years. The permanent school fund is currently about \$6,000,000. Royalty and lease payments continue to rise higher and higher; thus, the permanent school fund account continues to grow. This is excellent news for the Chambers County school districts.

Unfortunately, due to the lack of resources and expertise, Chambers County has struggled to manage and invest the permanent school fund over the years, and is finding it difficult to properly maintain the school land in Crockett County. With the increase in the size of the permanent school fund, the complexities with oil and gas leases and negotiation, the rapid market fluctuation in the interest rates, record keeping, accounting, and other general oversight responsibilities, Chambers County is having a difficult time keeping up with the school land and school funds. As a result, the return on investment for the permanent school fund has not been maximized.

Chambers County would like to maximize the return of investment on the permanent school funds. Chambers County believes that the best way to achieve this goal is to outsource the investment and management decisions over the school funds to a qualified bank. The qualified bank would have more experience, more resources, and certainly would be more equipped to invest the permanent school funds. The qualified bank has the employees, the technology, and the experience to maximize the return of investments, which is in everyone's best interest. On the other hand, Chambers County has neither the expertise nor the resources to maximize the income on the permanent school fund.

Chambers County has discussed this issue with Hibernia Bank. Hibernia Bank is very interested in providing these services to Chambers County, and quite confident that it could maximize the interest income for the permanent school fund. Hibernia Bank would provide sound, professional investment advice and management services over the school funds and school land. In fact, Hibernia Bank has proposed that it manage everything—including lease negotiations and dealing with maintenance issues for the school land.

If Hibernia Bank provided these services, it would be a win-win situation for everyone. The school districts would have their school funds being managed by professional bankers, and their land being managed by real estate management professionals. At the same time, Chambers County would be relieved of the heavy burden of trying to tackle the large responsibility of managing and investing the permanent school fund, and trying to maintain the school land in a distant Crockett County.

Of course, Hibernia Bank or some other qualified bank will charge a fee for its services. Chambers County believes the fees should be paid out of the available school fund account, since the schools would be receiving the benefit from Hibernia Bank's professional services. Alternatively, Chambers County believes the expenses should be paid out of the Chambers County School Equalization Tax raised each year for the school districts. It is noted that with Chambers County's present budget, Chambers County cannot afford to pay the administrative fees out of its general fund.

## **II. ARGUMENT AND AUTHORITIES**

The investment and managerial responsibilities of county school funds have traditionally been vested with counties—specifically, the Commissioner's Court of each county. This duty derives from the Texas Constitution and the Texas Education Code. *See* Tex. Const. art. VII §§1-6; Tex. Educ. Code §§17.81-17.83. Accordingly, the Commissioner's Court of Chambers County has the investment and managerial responsibilities of the school funds. The first

question then is whether the Commissioner's Court of Chambers County can delegate these duties to Hibernia Bank or some other qualified bank.

**A. Does Texas law permit Chambers County to hire Hibernia Bank or some other qualified bank under the Public Funds Investment Act to invest and manage the permanent and available county school funds?**

The answer to this question used to be "no". In 1988, a Texas Attorney General found that local governments could not delegate responsibility for investment decisions. *See* Op. Tex. Att'y Gen. No. JM-932 (1988). The opinion stated that a "governmental body or officer in which [the investment of public funds] are vested may not delegate them to other persons in the absence of express authority." (Emphasis added). The opinion concluded that the earlier version of the Public Investment Act, Tex. Rev. Civ. Stat. Art. 842a-2, did not *expressly authorize* the investment of public funds by persons outside local governments, reasoning that these discretionary decisions of investing school funds were left to government absent express statutory language to the contrary. Since the former Public Investment Act did not expressly authorize outsourcing investment decisions, the Texas Attorney General, Jim Mattox opined that such delegation was impermissible.<sup>1</sup>

The Texas Public Investment Act has since been amended. The current Public Investment Act, codified in the Texas Government Code, Tex. Gov't Code § 2256.001 et seq. (hereinafter "PIA"), controls the investment of public funds in Texas. The PIA applies to counties, as well as other local governments. *See* Tex Gov't Code § 2256.002(7) (defining "Local government" to include counties). Importantly, in 1999, under House Bill 3009, the PIA was amended to allow counties "to contract with a registered investment advisory firm to provide for the investment and management of its public funds or other funds under its control." *See* House Comm. Report, Bill Analysis, Tex. H.B. 3009, 76<sup>th</sup> Leg., C.S. (1999). The current language PIA reads as follows:

In the exercise of its power under Subsection (a), the governing body of an *investing entity* may contract with an *investment management firm* registered under the Investment Advisers Act of 1940 (15 U.S.C. Section 80b—1 et seq.) or with the State Securities Board to *provide for the investment and management of its public funds or other funds under its control*. A contract made under authority of this subsection may not be for a term longer than two years. A renewal or

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<sup>1</sup> It is also noted that under general trust principals, trustees, such as Chambers County, cannot ordinarily delegate the authority that has been conferred upon it. *See West v. Haggood*, 174 S.W2d 963 (Tex. 1943).

extension of the contract must be made by the governing body of the investing entity by order, ordinance, or resolution.

*See* Tex. Gov't Code § 2256.003(b) (emphasis added).

An "investing entity" means an entity subject to the PIA under §2256.003. *See* Tex Gov't Code § 2256.002(5). As noted above, "local governments" are subject to the PIA, and the PIA expressly includes counties within the definition of local governments. *See* Tex Gov't Code § 2256.002(7). Moreover, the school funds are clearly public funds or funds under Chambers County's control. Hence, reading this statute literally, counties, such as Chambers County "may contract with an investment management firm...to provide for the investment and management of its public funds or other funds under its control."

The answer therefore, to the first issue, is that Chambers County should be able to contract with Hibernia Bank or some other qualified bank for the investment and management of the school funds.

**B. Can Chambers County delegate to Hibernia Bank or some other qualified bank all decision-making authority to make prudent investments with the county school funds?**

There are no specific guidelines that show how much decision-making authority a county can delegate to Hibernia Bank or some other qualified bank. The PIA does not specifically answer this question. No Texas cases or Attorney General Opinions have addressed the parameters with which a county can delegate investment and management decisions to a bank for the investment of the permanent school funds.

Chambers County believes that Hibernia Bank or some other qualified bank should have complete authority over the investment and management of the school funds and school land. Banks are certainly more capable of maximizing interest income on the permanent school funds; banks are more experienced; their employees have more training; banks have more human resources; they are more equipped; they have the financial resources and contacts; and, they are certainly more technologically advanced and better suited to deal with today's sophisticated marketplace. The bottom line is that a bank would have a better chance of success in maximizing interest income for the permanent school fund if it had complete control over the permanent school funds, at least with respect to the management and investment functions. For these reasons, Chambers County argues that it should be able to delegate complete investment and management decision-making authority to Hibernia Bank or some other qualified bank.

If Chambers County had to authorize each investment, the benefits of outsourcing these responsibilities would be lost. Chambers County's limited resources would be spread thin to achieve any oversight responsibility. If Hibernia Bank or some other qualified bank is only permitted to merely "advise" Chambers County, this advice will likely become so watered down as it trickles through all the proper channels in the county that as a result, the advice will be ineffective and unproductive. In other words, the good advice may become so diluted, or worse, not followed, that the utility of outsourcing becomes nonexistent. For these reasons, Chambers County contends that Hibernia Bank or another qualified bank should have complete authority to invest and manage the school funds and school land under a contract that complies with the PIA.

**C. Does Texas law permit Chambers County to deduct the administrative costs charged by Hibernia Bank or some other qualified bank from the county available school fund or from the money raised by the Chambers County School Equalization Tax?**

Unfortunately, the PIA does not expressly answer this question either. Rather, the PIA seems to permit outsourcing for investment and management services related to the school funds, but is silent on the issue of payment for the services. Implicitly at least, it seems that the payment for these services should come from the available school fund or the Chambers County School Equalization Tax, since the management and investment services related to the school funds and school land would directly benefit the school districts in Chambers County. It would be unfair to charge Chambers County's general fund for a benefit that goes directly to the school districts, especially in a time when counties are struggling with their budgets and their limited resources.

With its present budget in place, Chambers County cannot pay out of its general fund any administrative costs charged by Hibernia Bank or some other qualified bank. Presently, the only feasible way to implement this proposed plan would be to charge the available school fund account or take some of the revenues from the Chambers County School Equalization Tax to pay for these administrative costs. Otherwise, Chambers County would not be able to afford the proposed plan. If the plan fails, Chambers County would not reach its goal in maximizing the interest income on the permanent school funds, and the school districts and Chambers County would all have to suffer the consequences of having Chambers County continue to invest the permanent school funds. In short, the school children of Chambers County would continue to have their money and land invested and managed by county employees, as opposed to bankers and real estate professionals. And as a result, they would have little, if any, hope of realizing maximum return of investment for their permanent school fund.

Certainly, with the recent amendments to the PIA, it is clear that the public policy of the State of Texas is evolving. Slowly but surely the public policy has changed from one where the counties provided all the investment services on the school funds internally, to a situation now where counties are encouraged to outsource these services to professionals in banking and real estate. The reason for this policy change is clear—in order to maximize return of investment for the school districts, banks and real estate professionals are better suited to handle the management and investment responsibilities over the school funds. Hence, Section 2256.003(b) of the Texas Government Code was enacted.

The only way for Chambers County to take advantage of the benefits created under Section 2256.003(b) is to pay for the professional services out of the school money. If this is ruled impermissible, all the advantages created under the new PIA are completely lost. Further, the archaic unproductive system in place will remain in place if the proposed plan cannot be financed with school funds. As a result, Chambers County, the school districts, and most importantly, the school children will have to suffer the consequences.

### **III. CONCLUSION**

In sum, Chambers County believes that it can hire Hibernia Bank or some other qualified bank to invest and manage the school funds and school lands. Further, Chambers County believes that it can delegate complete decision-making authority to Hibernia Bank or some other qualified bank to make prudent investment and management decisions over the permanent school funds and school land. Finally, Chambers County believes it can deduct or charge whatever administrative costs are incurred in connection with the management and investment services provided to Chambers County in the proposed plan. These conclusions are consistent with the recent amendments to the PIA, consistent with the public policy of the State of Texas, and certainly in the best interest of Chambers County, the school districts and school children.