

SUBJECT: Revising determination of ESF sufficient balance and investment of fund

COMMITTEE: Appropriations — committee substitute recommended

VOTE: 22 ayes — Zerwas, Longoria, G. Bonnen, Buckley, Capriglione, S. Davis, Hefner, Howard, Jarvis Johnson, Miller, Minjarez, Muñoz, Rose, Schaefer, Sheffield, Sherman, Smith, Stucky, Toth, J. Turner, VanDeaver, Wilson

0 nays

5 absent — C. Bell, Cortez, M. González, Walle, Wu

SENATE VOTE: On final passage, April 17 — 31-0, on Local and Uncontested Calendar

WITNESSES: For — (*Registered, but did not testify:* Anne O’Ryan, AAA TX; Gary Bushell, Alisance for I-69 Texas, I-14/Gulf Coast Highway; Matthew Geske, Austin Chamber of Commerce; TJ Patterson, City of Fort Worth; Christine Wright, City of San Antonio; Holli Davies, North Texas Commission; Victor Boyer, San Antonio Mobility Coalition, Inc.; Drew Campbell, Transportation Advocates of Texas; Mackenna Wehmeyer, Transportation Advocacy Group Houston)

Against — None

On — Vance Ginn, Texas Public Policy Foundation; (*Registered, but did not testify:* Phillip Ashley, Comptroller of Public Accounts)

BACKGROUND: Revenue for the Economic Stabilization Fund (ESF) comes almost entirely from oil and natural gas production taxes, also known as severance taxes. Before fiscal 2015, the ESF received 75 percent of any severance tax revenue that exceeded the amount collected in fiscal 1987. A constitutional amendment adopted in 2014 requires the comptroller to send one-half of this amount to the State Highway Fund (SHF), with the rest continuing to go to the ESF.

Texas Constitution Art. 3, sec. 49-g(g) sets a cap on the amount of money that the ESF can hold. The fund cannot exceed an amount equal to 10 percent of the total amount deposited into general revenue the previous biennium, minus investment income, interest income, and amounts borrowed from special funds.

Government Code sec. 316.092 requires the lieutenant governor and the House speaker to appoint a select committee of legislators to determine a sufficient balance for the ESF to ensure an appropriate amount of revenue is available in the fund. Sec. 316.092(d) establishes procedures for the Legislature to approve or change the sufficient balance adopted by the committee and presented to the Legislature in a concurrent resolution. If the Legislature does not finally approve a resolution providing for a sufficient balance by the 45th day of the legislative session, the balance adopted by the committee takes effect. These provisions expire December 31, 2024.

Sec. 316.093 establishes the procedures the comptroller uses either to reduce or withhold allocations to the SHF to maintain the sufficient balance in the ESF. These procedures are also used if the select committee has not adopted a sufficient balance for the ESF.

Government Code sec. 404.0241 allows the comptroller to invest a percentage of the ESF that exceeds the fund's sufficient balance in accordance with the investment standard specified in sec. 404.024(j), sometimes called the prudent investor standard. The comptroller is required to adjust the ESF's investment portfolio periodically to ensure that the balance of the ESF is sufficient to meet the fund's cash flow requirements. The comptroller is required to include the fair market value of the ESF's investment portfolio when calculating the cap on the ESF and when determining allocations of revenue to the ESF and SHF.

DIGEST:

CSSB 69 would revise how the state determines the sufficient balance for the Economic Stabilization Fund (ESF) and how the fund can be invested.

Sufficient balance. The bill would eliminate the select committee that

determines the sufficient balance of the ESF. The bill would require the comptroller to determine and adopt the sufficient balance as 7 percent of the certified general revenue related appropriations made for the fiscal biennium in which the determination was made.

Investing the ESF. The bill would revise the investment criteria applied to the ESF. It would require at least one-quarter of the fund's balance to be invested to ensure the liquidity of that amount. The comptroller would have to adjust the investment of the ESF to ensure that at all times at least one-quarter of the fund was invested in such a manner.

The comptroller could invest the rest of the fund using the prudent investor standard, which would authorize the comptroller to use any kind of investment that a prudent investor exercising reasonable care, skill, and caution would use in light of the purposes, terms, distribution requirements, and other circumstances then prevailing for the fund, taking into consideration the investment of all the assets of the fund. The comptroller would be able to pool assets of the economic stabilization fund with other state assets for investing.

The bill would remove a current requirement that the provisions on investing the ESF expire when provisions about the select committee and the sufficient balance also expire.

The bill would take effect September 1, 2019. Provisions about adjusting flows of general revenue to the ESF and SHF under what would be the new sufficient balance would apply beginning with fiscal 2022.

**SUPPORTERS
SAY:**

CSSB 69 would revise how the Economic Stabilization Fund (ESF) is administered to maximize its investments while keeping the fund safe and available to the Legislature. The bill would establish a responsible way to steward taxpayer dollars to meet both unforeseen needs and prudent investing. The bill would not affect transfers to the State Highway Fund, which would continue once the ESF's sufficient balance was met.

Sufficient balance. The bill would revise the way the sufficient balance

of the ESF was determined so that it was set in a more objective manner, rather than being decided by a committee. CSSB 69 would set the sufficient balance at 7 percent of the certified revenue estimate, which would ensure that enough was set aside to deal with unexpected economic downturns or natural disasters while simplifying and depoliticizing the calculation. The bill would not make it harder than it is currently to spend funds, including those below the sufficient balance, which could continue to be spent as under current law.

The bill would set the sufficient balance requirement at 7 percent of the certified general revenue estimate based on information from credit rating agencies about how the level of state reserves results in the highest credit rankings. For fiscal 2018-19, without counting the supplemental budget, this would result in a sufficient balance of \$7.5 billion.

Investing the ESF. The investment structure that would be set up by the bill would make sure that the bulk of the ESF was invested in a safe class of assets that would yield a better return on the state's investments than occurs under current law. Currently, the comptroller can invest only a portion of the fund that is above the sufficient balance under the prudent investor standard, which leaves much of the fund bringing in lower yields. CSSB 69 would extend the successful strategy of using the prudent-investor standard, which is well defined and would allow investments to keep pace with inflation and maintain purchasing power. Funds invested this way would continue to be available to the Legislature and could be accessed quickly if needed. The bill would ensure that 25 percent of the fund would be kept immediately available, essentially in cash or cash equivalents. Taken together, all of the ESF would be available to the Legislature if needed for a disaster or other reasons.

OPPONENTS
SAY:

CSSB 69 could limit the appropriate use and administration of the ESF by changing how the fund's sufficient balance would be set.

Sufficient balance. By removing legislative input in determining the sufficient balance and instead setting it as a percentage of the budget, the bill could make it difficult for the Legislature to use ESF funds that go

below that threshold. The sufficient balance can be seen as a floor on what can be spent from the ESF, and the bill would set what might be seen as an inflexible floor. The Legislature would not be able to adjust the sufficient balance, even if it felt such an adjustment was necessary.

Investing the ESF. The state should keep the funds it needs in emergency reserves and return what it does not need to taxpayers to be used in the private sector. The state would see more returns in the long run with this strategy than it would from creating a new investment standard for the ESF. The ESF was established to address unforeseen shortfalls in revenue, not as a way to raise revenue.

OTHER
OPPONENTS
SAY:

If the state is going to retain ESF funds and invest them, it also should reduce the overall cap on the fund so that the fund does not grow too large and encourage government spending. One way to accomplish this would be to remove federal funds from the calculation of the ESF cap.

The state should establish a disbursement fund to ensure earnings on the ESF were used to meet the state's needs.

NOTES:

According to the Legislative Budget Board, the bill would have a positive impact to the ESF of \$247.4 million through fiscal 2020-21.