

**LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS**

Bill Number: CS/SB 231a

51st Legislature, 1st Session, 2013

Tracking Number: .192467.2

Short Title: School District & Charter School Investments

Sponsor(s): Senator Timothy M. Keller and Representative Jimmy C. Hall

Analyst: Ian Kleats

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SENATE FINANCE COMMITTEE SUBSTITUTE FOR SENATE BILL 231

AS AMENDED

The Senate Floor amendment would allow school districts of any size (rather than districts having a student enrollment of more than 3,000 students as stated in the introduced bill), to invest sinking funds, unexpended bond proceeds, and unencumbered cash balances in:

- **certain fixed-income securities or pooled fixed-income securities; and**
- **shares of pooled investment funds managed by the state investment officer.**

Among its other provisions, the Senate Floor amendment:

- **removes a requirement that credit unions, in which governmental units place interest-bearing deposits, must be insured by an agency of the United States; and**
- **amends current law and cleans up proposed language from the introduced bill to be consistent with the original provisions of the introduced bill.**

Original Bill Summary:

Among its provisions, CS/SB 231 amends current law to:

- **remove requirements in the *Public School Finance Act* that detail how school districts or state-chartered charter schools deposit public money by changing “shall” to “may” (see **Technical Issues** for further discussion);**
- **allow, but not require, school districts and state-chartered charters to deposit public funds in accordance with another section of law;**
- **allow school district designees to invest sinking funds, unexpended bond proceeds, and unencumbered cash balances into certain federally backed securities, while defining school board designees to include both local school districts and state-chartered charter schools; and**
- **allow designees of school districts having student enrollment of more than 3,000 to invest sinking funds, unexpended bond proceeds, and unencumbered cash balances into certain fixed-income securities, pooled fixed-income securities, and shares of pooled investment funds managed by the state investment officer;**

The bill would also:

- remove certain statutory requirements for the distribution of deposits between all depositories within the geographical boundaries of a governmental unit; and
- confer the responsibility of prescribing an apportionment formula to the director of the Financial Institutions Division of the Regulation and Licensing Department.

The bill does not specify an effective date of the bill's provisions, and therefore, will be 90 days following adjournment, which is June 14, 2013.

Fiscal Impact:

CS/SB 231 does not contain an appropriation or a revenue impact.

Fiscal Issues:

Arbitrage

CS/SB 231 would allow school districts and state-chartered charter schools to invest unexpended bond proceeds into certain securities. Some of the allowable securities, as expanded by the bill, could have interest rates higher than the bonds issued on behalf of the school district. This opens up the possibility that school districts could engage in arbitrage with public funds.

Current law requires that, if a cash deposit by a school district into an interest-bearing account is part or all of the proceeds of a bond issuance, the interest rate on the deposits not materially exceed the rate of the bonds if the bonds would lose their tax-exempt status under provisions of Section 103 of the federal *Internal Revenue Code* (IRC).

The bill provides no such rate of return restrictions for the investment of unused bond proceeds into securities that could prevent arbitrage.

Tax Exempt Status of Bonds

Allowing school districts to invest unexpended bond proceeds could result in certain issues for the tax-exempt status of those bonds. For instance, if school district bonds come to be considered arbitrage bonds as defined by the federal IRC, which they currently are not, the bonds could lose their tax-exempt status.

The IRC details several methods through which proceeds of a bond issuance can be invested in higher yielding investments without jeopardizing their tax-exempt status. However, those methods require that certain, narrowly prescribed criteria are met, and it is unclear whether school districts and state-chartered charter schools could satisfy those requirements.

Technical Issues:

CS/SB 231 would remove requirements in the *Public School Finance Act* that detail how school districts or state-chartered charter schools must deposit public money. In place of the current requirement, the bill would permit, but not require, school districts or state-chartered charter schools to deposit in accordance with another section of law. However, should a school district or state-chartered charter school elect not to use the optional deposit provisions, it is unclear what other provision of law, if any, would apply.

Substantive Issues:

Provisions in the *Public School Finance Act* already allow for the temporary investment of demand deposits not immediately needed for the operation of a school district or state-chartered charter school. Those investments may take the form of securities issued by the state or the US government or its departments and agencies, and that those securities are backed by the full faith and credit of the respective governments.

Consequently, Section 2 of the bill may duplicate some existing provisions in current law, with the notable exception of expanding the allowable securities in which the school district or state-chartered charter school may invest; these additional securities include issuances from the Federal Home Loan Mortgage Corporation (“Freddie Mac”), the Federal Farm Credit Bank, and the Federal Home Loan Banks. The rate of return on those securities is typically higher than US Treasuries or municipal bonds in which the districts may currently invest.

Background:

The Public Education Department (PED) notes in its bill analysis that previous amendments were made to the *Public School Capital Improvements Act* and the *Public School Buildings Act* requiring school districts to include the capital improvements funding needs of state-chartered charter schools and locally chartered charter schools, residing within the school district, on the resolutions submitted to the qualified voters. Now that this funding stream exists, SB 231 would allow a state-chartered charter school to have the ability to invest these funds. PED highlights that these types of funds are often invested because they are non-reverting funds.

Committee Assignments:

SEC/SFC/HEC/HTRC

Related Bills:

None as of March 7, 2013.