



# Texas Education Agency

IO # 14604  
MBJ

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July 1, 1992

The Honorable Dan Morales  
Attorney General of Texas  
Supreme Court Building  
P. O. Box 12548  
Austin, Texas 78711-2548

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Opinion Committee

Dear General Morales:

Your opinion is respectfully requested with regard to the following question concerning the constitutional validity of Section 15.14 of the Texas Education Code.

Is it constitutional to lend securities owned by the permanent school fund in the manner and for the purpose set forth in Section 15.14 of the Texas Education Code?

In Opinion No. MW-429, Attorney General Mark White opined that the provision of Section 15.14 of the Texas Education Code that authorizes the loan of securities "is unconstitutional in that it contravenes the provisions of Article VII, Sections 4 and 5 of the Texas Constitution." Op. Tex. Att'y Gen. No. MW-429, at p. 5-6 (Jan. 21, 1982). Since that time, Article VII, Section 5, of the Texas Constitution has been amended to include a provision that appears to authorize securities lending and that specifically provides that it overrides any contrary constitutional provisions. A memorandum brief on this issue is enclosed for your consideration.

The State Board of Education is contemplating entering into an agreement with a bank that provides for the lending of permanent school fund securities, which is expected to produce approximately three million dollars per year for the available school fund. Your early consideration of this request therefore would be appreciated.

Sincerely,

A handwritten signature in cursive script, appearing to read "Lionel R. Meno".

Lionel R. Meno  
Commissioner of Education

Enclosure

In 1982, Texas Attorney General Mark White opined that the provision of Section 15.14 that authorizes the loan of securities "is unconstitutional in that it contravenes the provisions of Article VII, sections 4 and 5 of the Texas Constitution." Op. Tex. Att'y Gen. No. MW-429, at p. 5-6 (Jan. 21, 1982). At time of Opinion No. MW-429, Article VII, Section 4, of the Texas Constitution required that investments of the permanent school fund be made by the Comptroller, subject to the direction of the Board of Education, and provided that "the state shall be responsible for all investments." The Attorney General in Opinion No. MW-429 held that: "In our opinion, the short term loan of permanent school fund securities in exchange for cash collateral which is invested, constitutes an investment of permanent school funds. Thus, this investment function can be performed only by the comptroller." Op. Tex. Att'y Gen. No. MW-429, at p. 3 (Jan. 21, 1982). With respect to the requirement that the State be responsible for all investments, the Attorney General stated that: "In our opinion, the legislature may not constitutionally authorize the delegation of the investment function to a commercial bank." Id.

As noted above, the Attorney General in Opinion No. MW-429 held that Section 15.14 of the Texas Education Code contravenes the provisions of Article VII, Section 4 and Section 5 of the Texas Constitution. Opinion No. MW-429, however, does not specifically state how Section 15.14

contravenes Article VII, Section 5, of the Texas Constitution. Article VII, Section 5, establishes the permanent school fund and the available school fund and it provides that the principal of bonds and other funds and the principal from the sale of land of the school fund shall be the permanent school fund and that the interest derived therefrom and certain taxes levied thereon shall be the available school fund.<sup>1</sup>

Following Opinion No. MW-429, Article VII, Sections 4 and 5, of the Texas Constitution were amended. Article VII, Section 4, of the Texas Constitution was amended in 1985 to provide that the permanent school funds shall be invested by the treasurer (as opposed to the Comptroller), as may be directed by the Board of Education. The provision requiring that "the state shall be responsible for all investments" was not amended.

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1. The Attorney General in Opinion No. MW-429 stated that, as part of the securities lending program, the "bank would invest cash collateral and part of the interest on this investment would go to the permanent school fund." Op. Tex. Atty. Gen. No. MW-429, at p. 2 (Jan. 21, 1982). It may be inferred (although the Opinion does not so state) that this transfer of part of the interest to the permanent school fund is the violation of Article VII, Section 5, referred to by the Attorney General. In a brief in support of its request for reconsideration of Opinion No. MW-429, the Commissioner of Education noted that this was a misstatement of the facts and that a portion of the interest earned on the bank's investment of the collateral (which belongs to the broker and is pledged by the broker as collateral, but is not part of the permanent school fund) would go to the available school fund as "rent" for the securities pursuant to Section 15.14(b)(7), and would not go to the permanent school fund. Under these circumstances, it is unclear why the Attorney General in Opinion No. MW-429 determined that securities lending violated the provisions of Article VII, Section 5, of the Texas Constitution.

In 1987, a new subsection--Subsection (d)--was included in Article VII, Section 5. Subsection (d) provides:

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 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 probable income as well as the probable safety of their capital.

Tex. Const. art. VII, §5(d). Subsection (d) makes it clear that the Board of Education, in managing the assets of the permanent school fund, may supervise and manage any kind of investment meeting the prudent person standard set forth in that subsection and that it may do so through such procedures and subject to such restrictions as it establishes. The Attorney General held in Opinion No. MW-429 that the loan of securities under Section 15.14 of the Education Code constitutes an "investment" of permanent school funds. See Tex. Att'y Gen. No. MW-429, at p. 3 (Jan. 21, 1982). Read together, Subsection (d) of Article VII, Section 5, and Opinion No. MW-429 thus authorize the Board of Education to supervise and manage the loan of securities (as long as such investment meets the prudent person standard set forth in that subsection) through such procedures as it establishes. Under this authorization, the Board could enter into a contract with a bank to loan securities under the supervision

and management of the Board. Furthermore, Subsection (d) specifically provides that it overrides any contrary constitutional provision, and thus Subsection (d) would override the provisions of Article VII, Section 4, that require that the treasurer invest the permanent school fund and that the State be responsible for all investments, to the extent that such provisions could be construed to prohibit the Board of Education from entering into a contract with a bank that provides for securities lending.

#### CONCLUSIONS

The lending of securities owned by the permanent school fund in the manner and for the purpose set forth in Section 15.14 of the Texas Education Code appears to be authorized by Article VII, Section 5(d), of the Texas Constitution. Article VII, Section 5(d) overrides the provisions of Article VII, Section 4, to the extent that the latter provisions could be construed to prohibit the Board of Education from entering into a contract with a bank that provides for securities lending.