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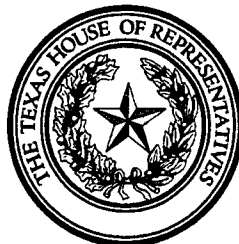
HOUSE RESEARCH ORGANIZATION

special legislative report

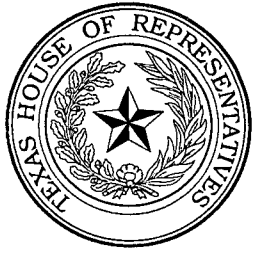
1991

CONSTITUTIONAL AMENDMENTS: PART TWO

September 19, 1991



Number 172



HOUSE RESEARCH ORGANIZATION

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Tom Whatley, Director

September 19, 1991

Number 172

1991 CONSTITUTIONAL AMENDMENTS: PART TWO

Thirteen proposed amendments to the Texas Constitution will be submitted for voter approval at an election to be held on Tuesday, November 5, 1991. The proposed amendments are analyzed in this special legislative report.

Two other proposed constitutional amendments were considered at an election held on August 10, 1991; the results of that election may be found on page vi of this report. The proposed amendments considered on August 10 were analyzed in House Research Organization Special Legislative Report Number 171, *1991 Constitutional Amendments: Part One*, July 8, 1991.

A handwritten signature in cursive script that reads "Anita Hill".

Anita Hill
Chairman

A handwritten signature in cursive script that reads "Henry Cuellar".

Henry Cuellar
Vice Chairman

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CONSTITUTIONAL AMENDMENT PROCESS

Since its adoption in 1876, the Texas Constitution has been amended 328 times. Thirteen proposed constitutional amendments have been adopted by the Legislature and submitted to the voters at the general election on Tuesday, November 5.

Joint Resolutions

All amendments to the Texas Constitution must be proposed by the Texas Legislature in the form of joint resolutions, which must be submitted for voter approval. For example, SJR 8 on this year's ballot refers to Senate Joint Resolution 8. Under Art. 17, sec. 1 of the Constitution, a joint resolution proposing a constitutional amendment must be adopted by a two-thirds vote of the membership of each of the two houses of the Legislature (100 votes in the House of Representatives; 21 votes in the Senate). The governor cannot veto a joint resolution.

A 1972 amendment to Art. 17, sec. 1 allows proposed constitutional amendments to be adopted by the Legislature during special sessions. For example, four of the proposed constitutional amendments submitted by the 72nd Legislature for the November 5 ballot were adopted during this summer's special sessions.

Contents of joint resolutions

Joint resolutions include the text of the proposed constitutional amendment and specify the date on which it will be submitted to the voters. A joint resolution may include more than one proposed amendment. If more than one amendment is submitted to the voters at the same election, the secretary of state conducts a random drawing and assigns a ballot number to each proposed amendment.

The Legislature may submit the same proposed amendment an unlimited number of times. For example, Proposition 13, authorizing \$300 million in general obligation bonds for college student loans, on the November 5, is essentially identical to a proposal on this year's August 10 ballot, Proposition 2, which was narrowly rejected by the voters.

Wording of ballot propositions

The joint resolution specifies the wording of the proposition that is to appear on the ballot. The Legislature has broad discretion concerning how the ballot proposition is to be worded. In rejecting challenges to proposed amendments on the basis that the ballot language was vague, incomplete or misleading, the courts generally have ruled that ballot language is sufficient if it identifies the proposed amendment for the voters. The courts have assumed that voters are already familiar with the proposed amendments when they reach their polling place and do not rely solely on ballot language to make their decision.

Date of election

The Legislature may call a special election for voter consideration of proposed amendments on any date (as long as election authorities have sufficient time to provide notice to the voters and print the ballots). For example, two proposed amendments, concerning property tax exemptions in county education districts and general obligation bonds for college student loans, were submitted to the voters this year at an election held on Saturday, August 10 (for results of that election, see page v). The usual practice in recent years has been to submit most proposed amendments to the voters at the November general election in odd-numbered years.

Publication

Art. 17, sec. 1 of the Constitution requires that a brief explanatory statement of the nature of each proposed constitutional amendment, along with the wording of the ballot proposition for the proposed amendment, be published twice in each newspaper in the state that prints official notices. The first notice must be published 50 to 60 days before the election. The second notice must be published on the same day of the subsequent week. Also, the secretary of state is to send a complete copy of each amendment to each county clerk, who must post it in the courthouse at least 30 days prior to the election.

The secretary of state prepares the explanatory statement, which must be approved by the attorney general. The Secretary of State's Office also arranges for the required newspaper publication, often by contracting with the Texas Press Association. The average estimated cost of publishing a proposed amendment twice in newspapers across the state is \$60,000.

Implementing Legislation

Some constitutional amendments are self-enacting and require no additional legislation to implement their provisions. Other amendments grant general authority to the Legislature to enact legislation in a particular area or within certain guidelines. These amendments require implementing legislation to fill in the details of how the amendment will operate. The Legislature frequently adopts implementing legislation in advance, with the effective date of the legislation contingent on voter approval of a particular amendment. If the amendment is rejected by the voters, then the implementing bill, or at least the part of the bill dependent on the constitutional change, does not take effect.

Effective Date

Unless a later date is specified, joint resolutions proposing constitutional amendments take effect when the statewide majority vote approving the amendment is canvassed (i.e. when the votes are officially counted). Statewide election results are tabulated by the secretary of state and must be canvassed by the governor 15 to 30 days following the election.

RESULTS OF THE AUGUST 10, 1991 CONSTITUTIONAL AMENDMENTS ELECTION

Two proposed constitutional amendments were adopted by the Legislature during its 1991 regular session and submitted to the voters at a statewide election held on Saturday, August 10, 1991. The voters approved Proposition 1, allowing voters to determine property taxation policy in county education districts, but rejected Proposition 2, an additional \$300 million in general obligation bonds for the college student loan program. (For additional information on the proposed amendments on the August 10 ballot, see House Research Organization Special Legislative Report No. 171, *1991 Constitutional Amendments, Part One*, July 8, 1990.)

According to the Secretary of State's Office, the final statewide results of the August 10 election were:

**Proposition 1 — Allowing voter approval of county education district
property tax exemptions and taxation of personal property**

For:	515,013 (58.4 percent)
Against:	367,564 (41.6 percent)

**Proposition 2 — Authorizing \$300 million in general obligation bonds for
college student loans**

For:	433,116 (49.6 percent)
Against:	440,763 (50.4 percent)

SUBJECT: Allowing cities of 5,000 or fewer residents to amend their charters

BACKGROUND: Art. 11, sec. 5 of the Texas Constitution permits cities with populations of more than 5,000 to become home-rule cities and adopt a city charter, which can be amended by majority vote of the city's voters once every two years. Home-rule cities may adopt charter provisions and city ordinances that do not conflict with state law. Cities with a population of 5,000 or less are governed by general laws enacted by the Legislature.

DIGEST: Proposition 1 would allow home-rule cities in which the population has fallen to 5,000 or less to amend their city charters by majority vote of the qualified voters.

The ballot proposal reads: "The constitutional amendment allowing home-rule cities with a population of 5,000 or less to amend their charters by popular vote."

SUPPORTERS SAY: Under the existing constitutional provision, a city that once had sufficient population to adopt a charter may not amend that charter if the municipal population declines to 5,000 or less. Proposition 1 would give home-rule cities whose population has declined to 5,000 or less clear authority to amend their city charters and keep those that already have made charter changes from being in technical violation of the Texas Constitution.

Some city charters include requirements that the charter be amended from time to time. For example Port Aransas' city charter must be amended every four years. Yet thirty-seven home-rule cities currently have populations of 5,000 or less and are stuck in a "Catch 22" situation in which they cannot amend their charters despite legislative mandates or individual charter provisions requiring charter changes.

OPPONENTS SAY: The arbitrary population limit on the size of home-rule cities should not be in the Constitution at all. Any community, no matter how small, should have the option of governing itself. If, however, some population cutoff for home-rule cities is justified, then the Legislature should have the flexibility

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to set the limit and provide for exceptions as needed. The population limit for home-rule cities in the 1876 Constitution was 10,000; it was lowered to 5,000 in 1909 to allow smaller towns and cities to make laws unique to their community. Rather than be tinkered with again, the limit should be eliminated from the Constitution.

NOTES:

According to the Texas Municipal League, these 37 home-rule cities now have populations of 5,000 or less, based on the 1990 census: Anson, Ballinger, Bowie, Center, Cisco, Colorado City, Daingerfield, DeLeon, Eastland, Electra, Elgin, George West, Giddings, Glenn Heights, Gorman, Granbury, Jersey Village, LaFeria, La Grange, Lake Worth, Lakeway, Luling, Marble Falls, McGregor, Muleshoe, Nassau Bay, Olney, Port Aransas, Port Isabel, Quanah, Ranger, Rockport, Rusk, Stamford, Terrell Hills, Tulia and West Orange.

SUBJECT: State aid for toll road projects and highway fund repayment from tolls

BACKGROUND: Art. 3, sec. 50 of the Texas Constitution prohibits the Legislature from lending or giving the state's credit to any person, association, municipal corporation or other corporation. Sec. 52-b, added in 1954, specifically prohibits the Legislature from granting public money or lending state credit to, or assuming indebtedness for, any person, firm, government agency or public corporation that is authorized to build, maintain or operate turnpikes.

During the same legislative session in which the constitutional amendment was adopted, the Texas Turnpike Authority (TTA) was established, initially to finance the building of the Dallas-Fort Worth Turnpike. The TTA, with headquarters located in Dallas, is responsible for building, financing and operating toll roads and bridges in the state. Since no state revenue can be used to finance or operate toll roads, all roads and bridges operated by TTA are entirely supported by toll fees, and the authority receives no appropriation from the Legislature.

Currently, the authority operates three tollway projects: the Dallas North Tollway, the Mountain Creek Lake bridge in Dallas and a bridge over the Houston Ship Channel. The authority formerly operated the Dallas-Fort Worth Turnpike, but once the bonds for that project were redeemed in 1977, it was transferred to the state highway department to operate as a freeway.

The Constitution, in Art. 3, sec. 52(b) and (c), authorizes certain local governments to issue bonds for local toll roads under certain circumstances. Under this provision, two local toll roads have been built by Harris County: the Sam Houston Tollway and the Hardy Street Tollway.

HB 9 by Cain, enacted by the Legislature during its first called session this year, became law on September 1 and created a new Texas Department of Transportation by combining the Department of Highways and Public Transportation, the Department of Aviation, the Texas Motor Vehicle Commission and, eventually, the Texas Turnpike Authority. HB 9 specifies that it is the intent of the Legislature that the TTA will be consolidated within the Texas Department of Transportation on September 1, 1997, if Proposition 2 is approved by the voters. The Sunset Advisory Commission

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would review the feasibility of consolidation and report to the Legislature in January 1993, 1995 and 1997. The sunset reports would include information about the cost of total or partial consolidation, the impact of consolidation on the availability of federal funding for turnpikes and the need for future turnpikes.

DIGEST:

Proposition 2 would amend Art. 3, sec. 52-b of the Constitution to permit the Texas Department of Transportation to contribute money, from any source available, to the Texas Turnpike Authority for its turnpike, toll road and toll bridge projects, as long as any money paid out of the State Highway Fund was repaid from tolls or other turnpike revenue.

The ballot proposal reads: "The constitutional amendment mandating the repayment to the Department of Transportation of monies expended to assist the Texas Turnpike Authority in the construction, maintenance, and operation of turnpikes, toll roads and toll bridges."

**SUPPORTERS
SAY:**

Proposition 2 would modify an outdated constitutional restriction and help finance needed road construction projects by allowing the Texas Department of Transportation and the TTA to pool their resources. While it would allow state help for toll road projects, the proposed amendment would ensure that any money contributed from the State Highway Fund would have to be repaid through toll revenues.

Working together, the highway division of the Texas Department of Transportation and the TTA could build projects beneficial to Texas motorists that otherwise might not be built. If a project could not immediately generate the toll revenues needed to pay back its bonds, the department could make up the difference with state money that would later be repaid with toll revenues. Ultimately these turnpikes will become part of the state highway system.

Texas metropolitan areas have local transportation needs that could be met more quickly if projects were undertaken as turnpikes rather than as freeways, especially if they have received a relatively low statewide priority ranking from the highway division. The state has far greater demand for construction and maintenance of state highways than its current revenues can fund, and federal funding cutbacks have placed an even greater strain

on highway resources. Building needed projects sooner could save money in the long run because, even though the current inflation rate is relatively low, construction costs still are rising.

It often is difficult for the TTA to find toll projects that would generate enough initial revenue to finance themselves without some seed money to get the project started. Yet with so many demands on state highway dollars, these locally important projects might not be built for many years, if at all, unless they are set up as toll projects.

Ratings of Texas Turnpike Authority bonds might improve if, for future projects, some state help were allowed. Better bond ratings would save money that otherwise would go to pay higher interest rates. However, bond holders would have no claim on state funds.

The TTA is unlikely to default on revenue bonds backed by tolls; bond buyers in the market already have judged these bonds to be sound. But even in the unlikely event that it did default, the bonds would *not* be a debt of the state. These bonds are a contract between the TTA and the bondholder, and not only is no other revenue source pledged to repay them, the bonds (and the Constitution) specifically provide that state funds may not be used to repay them.

As noted by the Texas Performance Review, which recommended making this change, Proposition 2 would give the state greater flexibility to take advantage of any federal funds that might become available for toll projects in the future. Proposed amendments to the Federal Surface Transportation Reauthorization Act would allow federal funds to be used for toll roads, including a federal match of up to 35 percent for toll facilities. However, the current constitutional limitation prohibits the Legislature from appropriating *any* public money, including federal funds received by the state, for construction and operation of toll roads. Building roads with the mixture of funds made possible by this amendment would free up money for projects in other areas of the state where toll roads are not feasible.

Turnpike projects constructed with the help of federal funds would have to comply with the requirements of the National Environmental Policy Act, and this would result in better protection of the environment. Projects

using state highway funds would have to comply with state environmental requirements. Both state and federal requirements are more stringent than the guidelines that the TTA currently follows.

HB 9, the transportation reorganization statute enacted this year, provides that it is the intent of the Legislature that the Texas Turnpike Authority be merged into the Department of Transportation in 1997, after study by the Sunset Commission, but only if Proposition 2 is approved. (Without Proposition 2, the ban on state support of toll roads would rule out merging TTA into a department funded by state appropriations.) The transportation commission now has some role in determining the feasibility of toll projects, but the proposed consolidation would help streamline future state transportation planning, helping to ensure that the Department of Transportation could consider toll roads in its statewide road planning. It also would allow greater coordination within the new department in building highway access roads to toll projects.

While the Houston Ship Channel Bridge project received some initial criticism, its financial problems came about because the highway department had delayed building connecting roads to the bridge, resulting in lower-than-expected initial traffic flow and toll revenues. Approval of Proposition 2 would ensure that toll projects would be properly integrated into the state's transportation network and that the highway department and the turnpike authority would better coordinate their plans.

Two local toll roads have been built in Harris County, 100 percent financed by local general-obligation and revenue bonds backed by the taxing authority of the county: The Sam Houston Tollway and the Hardy Tollway. So far this financing arrangement between the county and the local toll road authority has worked well. The success of this local cooperation augers well for joint TTA and state highway division projects that would be made possible by Proposition 2.

The highway department has not received general revenue for highways since 1987 and does not expect to receive any in the future unless the funds are earmarked for specific purposes. It is highly unlikely that the Legislature would use ever general revenue to help build toll roads and

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even more unlikely that general revenue used for that purpose would not be repaid with toll revenue.

The constitutional amendment concerning support for toll roads proposed in 1987 was rejected by the voters not only because it made no provision for repayment of state spending for toll road projects but also because it would have allowed certain counties and cities to levy property taxes to pay for toll road bonds to the extent that tolls were insufficient. Proposition 2 is a much more narrowly drawn amendment, without the local property tax provision and with a requirement that the State Highway Fund be reimbursed for any toll road support.

OPPONENTS
SAY:

State taxpayer dollars should not be used to subsidize any portion of toll-road projects. If anticipated tolls are insufficient to raise the revenue necessary to pay for these roads, then they should not be built in the first place, and the state should not be placed in the position of having to bail out short-sighted toll projects. Yet this proposal would allow state highway dollars to be used for projects that might fail financially, leaving the state holding the bag. The voters rejected a similar amendment in 1987 and should do so again.

Texas motorists who use the roads already pay gasoline taxes, which recently were raised another 5 cents to 20 cents per gallon, and three-quarters of the revenue is earmarked for building and maintaining state highways. (The other one-quarter goes to public education.) If the Department of Transportation were authorized to use motor fuel tax revenue for toll projects, taxpayers who use those toll roads would be paying twice.

Building more toll roads would be an inequitable way to meet Texas' transportation needs. Toll roads place a heavy burden on those drivers who live and work near those roads while sparing those who do not. When comparing locally paid tolls to gasoline taxes, which are paid by drivers across the state, the toll for a turnpike trip costs a driver many times what the same trip costs in gasoline taxes. Since toll roads are built with borrowed money, the debt service on bond repayments greatly increases their ultimate cost. Also, tolls have a way of lingering long after a project is paid for.

The recent track record of the TTA in choosing toll road projects does not bode well as far as the need for future state subsidies is concerned. The most recent project, the Houston Ship Channel bridge, was so poorly planned that it had to be refinanced in 1985 with high-interest junk bonds. Even if TTA is able to restructure this debt before the bonds come due, the fact that it had to resort to this kind of high-risk financing does not inspire confidence in the authority's ability to pick viable projects in the future.

Currently the activities of the TTA are financed through the proceeds of revenue bonds, and investors are unlikely to invest in bonds for projects if there is risk that tolls will not be sufficient to redeem the bonds within a reasonable period of time. Yet if state money were used to subsidize these projects, then those that are less financially sound would be more likely to be built.

If the constitutional prohibition against state support for toll roads were removed and the TTA later defaulted on any of its bonds, the state might be sued by turnpike bondholders.

While Proposition 2 provides for eventual repayment of revenue spent from the State Highway Fund to support toll roads, it does not provide for reimbursing state spending from *other* state revenue sources, such as general revenue. This loophole could be used to provide state support for toll roads "from any source available" without repayment from toll revenues. Although the Department of Transportation now receives most of its funding from the State Highway Fund, it may receive funding from other sources. Until the mid-1980s the highway department received extensive support from general revenue, and there is nothing to prevent this from happening in the future. Also, there is no provision for *when* the highway fund would be repaid from toll revenues and at what, if any, rate of interest.

OTHER
OPPONENTS
SAY:

Proposition 2 would encourage the construction of more roads, which is not the way to solve Texas' transportation needs. Building roads damages the environment, disrupts neighborhoods and encourages the use of automobiles that pollute the air. The state should devote more transportation resources to better alternatives, such as public transportation.

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Merging the TTA into the Department of Transportation, which could not occur without approval of this amendment, is not a good idea since a project that is financed with revenue bonds must be built quickly, with no bureaucratic delays, so that interest payments do not get out of hand. Potential investors in turnpike bonds might be leery of working with a large bureaucratic agency that is subject to political pressure.

The ballot language for Proposition 2 is misleading. Nothing is said about *allowing* state spending for toll roads, only that any Department of Transportation spending that does occur must be repaid with toll revenues. Voters reading the ballot proposal would have no idea that a 37-year-old constitutional prohibition against state subsidies for toll roads would, in effect, be repealed, nor would they know that only the State Highway Fund, not other revenue sources, would be repaid. The voters should also be told that by voting for this proposed amendment, they would be permitting the merger of the TTA into the Texas Department of Transportation.

NOTES:

In 1987 the Legislature submitted for voter approval a proposed constitutional amendment (HJR 65) that would have allowed joint highway projects by the Texas Turnpike Authority and the state highway department and allowed the state to contribute money from any source for such projects. It also would have allowed certain counties and cities to levy a property tax, with the revenue used to repay toll road bonds and construct and maintain toll roads, if tolls were insufficient for those purposes. On November 3, 1987 the voters rejected the proposed amendment by 951,130 in favor (46.1 percent), 1,111,903 against (53.9 percent).

SUBJECT: Removing limits on investment authority of the Veterans' Land Board

BACKGROUND: The Veterans Land Board is authorized by the Texas Constitution to sell more than \$2 billion in bonds and use the funds to help veterans buy land or homes. The money the board borrows by issuing bonds may be invested, pending its use in the land and housing programs, as specified in the Constitution.

The land program dates from 1946, when voters adopted Art. 3, sec. 49-b of the Texas Constitution, permitting the Veterans' Land Board (the land commissioner and two citizens appointed by the governor) to sell state bonds and use the proceeds to buy land for resale to Texas veterans at a below-market interest rate. Eligible veterans may qualify for a 30-year loan of up to \$20,000, including a \$1,000 down payment, to purchase five or more acres of land. (The Legislature has given the land board permission to raise the maximum loan to \$40,000, contingent on approval by the U.S. Congress.) The provision for the veterans' land programs has been amended numerous times and currently permits the board to issue \$950 million in state general-obligation bonds.

The housing program was approved in 1983, when voters adopted Art. 3, sec. 49-b-1 of the Constitution. This provision allows the land board to issue an additional \$1.3 billion in bonds, \$1 billion of which is to be used to make low-interest home mortgage loans of up to \$45,000 (up from \$20,000, effective September 1, 1991) to veterans through the Veterans' Housing Assistance Fund. The board makes fixed-rate loans for 15, 20, 25 and 30 years at 8.5 percent interest. In 1986 the program was expanded to include home improvement loans of \$4,000 to \$17,500. (The limit could be raised to \$25,000 if the U.S. Department of Housing and Urban Development increases its insurance coverage to that amount.)

The land program has purchased a total of 4.6 million acres at a cost of \$1.3 billion. The housing and home improvement programs have lent \$493.5 million. Some 129,600 land, housing and home improvement loans have been made since 1949. There were \$1.31 billion in land and housing bonds outstanding as of August 31, 1991.

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Until needed to purchase land or provide housing loans or to pay principal and interest on the bonds and other expenses, the proceeds from veterans' land and housing bonds may be invested. The Constitution limits the investments to "bonds or obligations of the United States." This restriction is also found in sec. 161.173 of the Natural Resources Code. As of August 31, 1991, the veterans' land and housing programs held investments in U.S. government securities with a market value of \$695.6 million.

DIGEST:

Proposition 3 would amend Art. 3, secs. 49-b and 49-b-1 of the Texas Constitution to permit the Legislature to determine how to invest proceeds of Veterans' Land Board bonds, eliminating the limitation on board investments to U.S. bonds or obligations. (Potential investments allowed under the implementing legislation for Proposition 3 are listed in the NOTES section.)

Proposition 3 also would permit the Legislature to delegate to the board other duties, responsibilities, functions and authority with respect to the board's *housing* program, as it already does for the land program.

The ballot proposal reads: "The constitutional amendment to authorize the legislature to further implement and enhance the administration of the veterans' housing assistance and land programs and to expand the investment authority of the Veterans' Land Board."

SUPPORTERS
SAY:

Proposition 3 would allow the Legislature to give the Veterans' Land Board the flexibility to earn more on its investments in order to boost earnings for the veterans' land and housing loan programs. Investment restrictions are more properly contained in statute rather than in the state Constitution, which can be amended only by a statewide vote.

Proposition 3 and its implementing legislation (SB 647 by Tejeda, approved during the Legislature's 1991 regular session) simply would grant the Veteran's Land Board the same investment authority the Treasury already has. This broader authority could increase the board's investment income by some \$1 million a year, according to land board estimates. The additional income could be used to retire outstanding bonds and to lower the interest rates charged to veterans for land and housing loans.

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In its 1989 regular session the Legislature attempted to define by statute the constitutional restriction to "bonds or obligations of the United States" for land board investments to include investments similar to those allowed to be made by the state Treasury. However, in July 1990 Attorney General Jim Mattox determined (JM-1201) that the board was constitutionally prohibited from investing in such safe investments as direct and reverse repurchase agreements, call option contracts and collateralized mortgage obligations, since these are instrumentalities of third parties, not of the United States government.

The law implementing Proposition 3 would allow the board to choose among a variety of stable and conservative investments — direct and reverse repurchase agreements (overnight secured loans), call option contracts (sale of the right to purchase securities at a specified price) and collateralized mortgage obligations (bonds created from mortgages). In addition, the bill would permit investments in insured certificates of deposit, municipal bonds and top-ranked commercial paper (short-term unsecured loans by businesses) and bankers' acceptances (short-term bank loans used to finance international trade).

It is unlikely that the Legislature would add any risky investments to the list of permissible investments. The Legislature has always been very conservative in controlling investments by state entities. Legislators would have to answer to the voters if they allowed bond proceed investments that could put at risk the popular veterans' land and housing loan programs.

Proposition 3 also would permit the Legislature to delegate to the board other duties, responsibilities, functions and authority with respect to the board's housing program. The Constitution already grants the Legislature this power with respect to the board's land program; the proposed amendment simply would create a sensible parallel for the housing program.

OPPONENTS
SAY:

Proposition 3 would eliminate all restrictions on the Legislature's grant of authority to the Veterans' Land Board to invest proceeds of bonds used to finance the veterans' land and housing programs. This would open the door to investments that might boost earnings in the short run but ultimately could put these important programs at risk.

Removing constitutional safeguards against shaky investments could threaten programs that provide access to land and affordable housing for thousands of veterans who have sacrificed to serve their county. The land and housing programs are too important to Texas veterans to risk on any but the most secure investments.

The attorney general's 1990 opinion indicated that the land board already is authorized to make a wide array of lucrative investments. It may invest in any obligation directly or indirectly guaranteed by the full faith and credit of the United States, securities and bonds issued by the Farm Credit System Financial Assistance Corporation, the Private Export Funding Corporation or the Export-Import Bank and insured certificates of deposit, as well as U.S. Treasury bonds. The board thus has available a variety of *safe* investments that provide reasonable returns without undue risk. Bond proceeds that are intended to provide housing and land loans to Texas veterans should not be risked just to boost investment returns by a few tenths of a percent.

Some of the investments that would be permitted by the implementing legislation are potentially insecure. For instance, commercial paper issued by Salomon Brothers would have fit the proposed qualifications for a permissible investment but could have left the land board holding debt issued by a firm facing severe legal problems. Similarly, questions have been raised about the financial strength of the Federal National Mortgage Association ("Fannie Mae"), Federal Home Loan Mortgage Corporation ("Freddie Mac") and Student Loan Marketing Association ("Sallie Mae"), whose obligations the Land Board would be able to purchase.

Proposition 3 would not prevent the Legislature from later amending the proposed list of permissible investments in the implementing statute to allow even riskier investments, such as real estate, junk bonds and futures trading. These classes of investment may appear secure when initially considered but each has proved vulnerable to unanticipated market conditions and created massive losses for investors.

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NOTES:

The implementing legislation for Proposition 3, SB 647 by Tejeda, would amend sec. 161.173 of the Natural Resources Code to expand the permissible investments of the Veterans' Land Board. The bill's provisions would take effect only if Proposition 3 is approved by the voters.

The bill would allow the board to invest any funds not needed immediately for paying off bonds, purchasing land or paying expenses in any of the following:

Certain direct and reverse repurchase agreements ("repos") made with Texas banks or Federal Reserve-approved primary dealers; obligations issued or guaranteed by the U.S. government or certain federally chartered agencies; investment instruments guaranteed by the full faith and credit of the U.S. government; bankers' acceptances with a maximum maturity of 270 days that are issued by a bank, have the highest short-term credit rating and are eligible for purchase by a Federal Reserve member; commercial paper with a maximum maturity of 270 days that has received the highest short-term credit rating; covered call options; state and local obligations and mutual funds of these obligations; investments insured by the federal bank or S&L insurance funds or secured by a U.S. government or agency obligation; collateralized mortgage obligations fully secured by mortgages or guaranteed by certain federally chartered agencies or a security issued by the Farm Credit System Financial Assistance Corporation, the Private Export Funding Corporation or the Export-Import Bank.

SB 647 would expand the land board's current investment authority by permitting investment in bankers' acceptances, commercial paper and state and local obligations. It also would permit the land board to make the investments that are included in current law but which the attorney general has stated are not currently constitutionally permissible: direct and reverse repos, call options and collateralized mortgage obligations.

In addition, the board could make any other investment authorized for the state Treasury by the Government Code. This clause is intended to allow the investment authority of the land board to track any future expansion of the investment authority of the Treasury. The Treasury's current investment authority is essentially identical to the authority proposed for the land board by SB 647.

Under SB 647, the land board also could not purchase the stock or bonds of a company doing business in South Africa unless the company had adopted the "Sullivan Principles" governing South African investments and had obtained a performance rating in categories 1 or 2 of the principles (*Statement of Principles for South Africa*, 1987) or has agreed to the U.S. State Department code of conduct and been rated "making satisfactory progress." The board could not invest in any business supplying strategic products to the South African government, military or police. (These restrictions are the same as now apply to investment by the state Treasury. No other state entity is subject to similar restrictions, although the Texas Growth Fund, a venture capital fund in which state pension funds may invest, must require businesses in which it invests to submit an affidavit disclosing whether the business has any direct financial investment in or with South Africa or Namibia (Texas Constitution, Art. 16, sec. 70).)

SUBJECT: \$1.1 billion in bonds for corrections, mental health/retardation facilities

BACKGROUND: The principal method by which the state borrows money is by issuing bonds. General-obligation bonds are backed by the full faith and credit of the state. The state guarantees that it will repay bondholders, with interest, with the first money coming into the Treasury each fiscal year.

Since Art. 3, sec. 49 of the Texas Constitution prohibits most forms of state debt, a constitutional amendment is required to authorize the state to issue general obligation bonds.

Since 1946 the debt-limiting provision has been amended numerous times to allow bond sales for a variety of purposes, including a total of \$900 million in bonds for prisons and mental health facilities. Art. 3, sec. 49-h, approved in 1987, allows the Legislature to authorize issuance of up to \$500 million in general obligation bonds to finance construction and renovation of corrections and mental health and mental retardation facilities.

The \$500 million, plus interest earned on it, has been appropriated as follows: \$414.3 million to the Texas Department of Criminal Justice (TDCJ) to construct 15,378 new prison beds and to renovate and repair existing facilities; \$66.9 million to the Texas Department of Mental Health and Mental Retardation (TXMHMR); and the Texas Youth Commission (TYC), \$22.4 million.

Art. 3, sec. 49-h(c), approved in 1989, allowed the Legislature to authorize sale of an additional \$400 million in general-obligation bonds. The 1989 bond proceeds, plus interest, have been appropriated as follows: TDCJ, \$325.2 million to build 11,109 new corrections-facility beds and to renovate and repair existing units and \$23 million for prison industry-unit construction and renovation; TXMHMR, \$49.6 million; TYC, \$16.9 million; and the Department of Public Safety (DPS), \$4.3 million.

The state currently has about 52,200 prison beds available and is constructing an additional 15,600 beds, for a total of 67,800 beds by the mid-1990s.

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DIGEST:

Proposition 4 would add sec. 49-h(d) to Art. 3 of the Texas Constitution, allowing the Legislature to authorize the issuance of up to \$1.1 billion in general-obligation bonds to acquire, construct and equip facilities for corrections, youth corrections and mental health and mental retardation services; to repair or renovate existing TDCJ, TXMHMR or TYC facilities, or to repair or renovate other facilities for use as prisons or substance abuse felony punishment facilities.

Proceeds from bonds authorized by Proposition 4 could be appropriated only during the second called session of the 72nd Legislature or a subsequent session.

The ballot proposal reads: "The constitutional amendment authorizing the issuance of \$1.1 billion in general obligation bonds for acquiring, constructing, or equipping new prisons or other punishment facilities to confine criminals, mental health and mental retardation institutions, and youth corrections institutions, for major repair or renovation of existing facilities of those institutions and for the acquisition of, major repair to, or renovation of other facilities for use as state prisons or other punishment facilities."

**SUPPORTERS
SAY:**

Proposition 4, along with its implementing legislation (HB 93, see NOTES section), would allow the state to initiate badly needed construction, repair and renovation projects for prisons, substance abuse facilities, youth corrections facilities and mental health and mental retardation facilities, without requiring a major increase in taxes.

The bulk of the money authorized by Proposition 4, \$672.1 million, is earmarked by the implementing legislation for construction of 25,300 new correctional-facility beds, 12,000 of which would be in substance-abuse centers. The TDCJ is under federal court order based on the *Ruiz* decision not to exceed 95 percent of the capacity of state prison facilities. Because the system is often at this limit, jails in 54 counties now hold about 9,000 state inmates awaiting transfer to state prison. The construction financed by the bonds authorized by Proposition 4 would help relieve chronic overcrowding in the corrections system. Also, a portion of the money for the Texas Department of Mental Health and Mental Retardation could be

used to build facilities to house special-needs parolees, which would open up some prison beds.

The state should include drug and alcohol treatment programs in its criminal justice system to help break the cycle of crime by targeting substance abuse, which would reduce the recidivism rate. It is estimated that around 85 percent of the prison system's inmates have a history of substance abuse. The 12,000 substance-abuse facility beds would be the first statewide response to the role that alcoholism and drug abuse play in promoting criminal activity. These centers would be secure lock-up facilities used only as supplements to — not replacements for — standard correctional facilities. These beds would be used in the substance abuse felony punishment program recently created by the Legislature.

Some additional expansion of prison capacity also is necessary to help the state meet the growing demands on its criminal justice system. The 1989 criminal justice system revisions contained in HB 2335 by Hightower (71st Legislature) emphasize alternatives to incarceration, the use of community corrections facilities and changes in felony penalties. The criminal justice revisions in HB 93 by Hightower and Stiles (72nd Legislature, second called session; see NOTES), will further increase the effectiveness and efficiency of the state's criminal justice system and also help divert nonviolent offenders from the prison system. But even if those prison-diversion tools are used extensively, more prison beds will be needed if the state is to keep violent offenders locked up to serve a greater proportion of their sentence.

The lack of prison space is distorting the entire criminal justice process. The average *sentence* for inmates released in 1990 was 112.8 months. Because of insufficient capacity, the average *length of stay* for those inmates was 22.8 months, only about 20 percent of their sentences. Eighty percent of the inmates in the prison system are repeat offenders. Rehabilitation and other alternatives to incarceration do not always make hardened criminals change their ways. Expanding prison capacity would help ensure that the worst offenders will spend a longer time behind bars.

Lack of prison capacity also impedes law enforcement efforts and undermines the deterrent effect of prison on criminal activity. Since 1984

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the FBI Index crime rate has increased 30 percent while the rate for violent crime alone has increased 51 percent. The state should be able to protect its citizens by keeping dangerous criminals off the streets. Some law enforcement officers feel it is useless to arrest criminals who will serve only a fraction of their sentences. Prosecutors are frustrated by a growing tendency among convicted felons to choose prison time over probation because of the likelihood that their stay behind bars will be shorter than any period of probation.

Maximum security prisons can take over two years to complete, including site selection, design, bidding and construction. The state must act now to ensure that prison capacity will meet future needs.

The Proposition 4 bond proceeds that would be appropriated for TXMHMR facilities would provide \$23.2 million for about 57 maintenance and renovation projects necessary to meet federal standards and building codes. Another \$12.2 million in bond proceeds would be used to construct a psychiatric hospital in El Paso and a mental health facility in Lubbock County. Persons in need of psychiatric or mental health services in these areas currently have to drive over 100 miles to obtain care.

The Texas Youth Commission would get \$40.7 million in proceeds from Proposition 4 bonds to construct a 144-bed facility and to maintain, repair and renovate its facilities. Demand for space has increased, and the commission has been forced to release youths sooner than it would like, reducing the amount of counseling and rehabilitation that the commission can provide youth offenders.

It makes good fiscal sense to use money borrowed by issuing bonds to finance capital investments such as prison and mental health and mental retardation facilities that will be used over a long period. Use of bonds stretches the payment period over many years, allowing the state to avoid imposing another massive tax hike to pay for these projects out of current revenues. Just as local governments use bond proceeds to finance streets, parks, buildings and sewers, so the state should use this financing tool to expand prison capacity. Prisons and mental health and mental retardation facilities are designed for long-term use; it is only logical that they be paid

for over an extended time, rather than making today's taxpayers pay the entire amount up front.

The state can afford to incur additional debt for a justified purpose without risking financial jeopardy. Texas ranks 49th among states in terms of overall state debt per capita and has the fourth lowest general-obligation bond debt per capita of the 10 largest states. A provision in SB 3, enacted this year by the 72nd Legislature, prohibits the Legislature from authorizing additional state bond debt if the resulting annual debt service will be more than 5 percent of the average general revenue available to be spent for debt service over the preceding three fiscal years. State-bond debt service for 1991 is around 1 percent. Even in the highly improbable event that all \$1.1 billion of the bonds proposed in Proposition 4 were sold in 1992, the state's estimated fiscal 1992 debt service still would be less than 2.5 percent.

By authorizing a bond issue of this size, the voters would give the Legislature the flexibility to meet future demands. About \$350 million of this proposed issue has not been appropriated by the Legislature, allowing the state to have a reserve for future needs without having to return to the voters for another bond authorization. Since proceeds from Proposition 4 bonds could be used only for corrections, mental health and mental retardation and youth corrections facilities, voters may be assured that future bond issues will be used only for limited purposes.

OPPONENTS
SAY:

The state should not continue trying to build its way out of its prison capacity problem, especially by going deeper into debt with the largest single bond authorization in its history. The state needs to break its expensive prison-building habit because no amount of construction will ever meet the potential demand for prison space — the more prison beds are added, the more prisoners will be sentenced to fill them. Building more prisons is a short-term approach to a problem that can only be solved through long-term changes in public policy and society.

The state has been on a prison-building binge. Since 1988 about 26,230 beds have been built or are being built using general-obligation bond proceeds, a financing mechanism that generally *doubles* building costs. Money now poured into prison construction would be better used to divert

nonviolent offenders from prisons and into alternative facilities such as boot camps and regional rehabilitation facilities. This would create more room for violent offenders in existing facilities, helping to alleviate the pressure to grant early parole to make room for the newly sentenced. "Work punishment" sentences that punish offenders by requiring them to perform a specified number of community service hours should be instituted for nonviolent offenders; this would provide rehabilitation as well as reducing the demand for prison beds.

Another alternative to prison-construction spending would be to devote more resources to meeting the developmental needs of children and those judged to be "at risk" of committing future criminal acts. A larger proportion of criminal justice funding should be directed to programs to treat some of the root causes of crime, such as abuse of alcohol and illegal drugs. Studies have found that around 85 percent of Texas' felons have a substance-abuse problem, about 90 percent are school drop-outs and over 30 percent are illiterate.

Operating costs for new prison facilities are another "hidden cost" of this bond proposal. Every facility the state builds today carries with it the need for future general revenue funds to operate it that could result in a major tax increase. The Legislature should not commit future state budgets to this extent. The annual cost of operating a 2,250-bed unit is estimated at \$22 million. From 1984 to 1990 the prison system's annual operating budget grew by 168 percent, to \$618 million, and will continue to grow rapidly as new units now under construction come on line.

If new prison space and mental health and mental retardation facilities are needed, they at least should be paid for with current revenue instead of pushing the debt off on future generations by borrowing money through the sale of bonds. Interest costs for these bonds will almost double project costs. The fiscal note on Proposition 4, prepared by the Legislative Budget Office, estimates that once the entire authorized bond amount of \$1.1 billion is issued, the debt service will be \$101.9 million per fiscal year. Over the life of 20-year bonds, the taxpayers would have to pay a total of \$2.1 billion, almost twice as much as the face value of the bonds, due to the interest costs.

Adding another \$1.1 billion to state debt is unnecessary when other alternatives are available. As of May 31, 1991, state bond debt totaled \$7.7 billion, of which \$3.0 billion was in general-obligation bonds. This is up from \$2.7 billion in general-obligation bond debt at the end of fiscal 1990 and \$2.3 billion at the end of fiscal 1989. Another \$3.0 billion in general obligation bond debt has been authorized but not yet incurred.

Any new debt-creating measure needs to be examined in view of the overall state debt. Although Texas ranks low among states in terms of overall state debt per capita, the state ranks 18th among states in terms of debt per capita when debt carried by *local* government authorities also is considered. Of the 10 largest states, Texas has the highest local debt burden. The Legislature needs a comprehensive evaluation of the state's growing debt before more new debt is authorized, especially debt of this magnitude.

The prison system is not the only state program under court order to make improvements. Both TXMHMR and TYC have needs that are equally pressing. Yet the implementing legislation for this proposed amendment allocates almost 90 percent of the bond authorization to TDCJ.

OTHER
OPPONENTS
SAY:

Although the state may need to expand prison capacity, this bond issue would go too far and authorize more beds than necessary. Rather than approve the largest bond authorization in state history, it would be more prudent to approve a smaller bond issue that would not unduly burden future state budgets.

The voters should not be asked to approve a bond authorization without knowing how all the money would be used. The Legislature has appropriated just 68 percent of the bonds that would be authorized by Proposition 4. Approving a bond authorization with no mention of how about \$350 million will be spent would take away the voters' ability to monitor and approve the use of borrowed funds.

NOTES:

Contingent on approval by the voters of Proposition 4, HB 93 by Hightower and Stiles (72nd Legislature, second called session) appropriates to TDCJ \$672.1 million to construct a minimum of 6,750 maximum security beds, six 1,000-bed regional centers, one 550-bed psychiatric center

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and 12,000 drug treatment beds (25,300 beds total) and for maintenance and repairs of TDCJ facilities. (The fiscal note on HB 93 estimates the debt service on \$672.1 million in bonds to be \$42.8 million in fiscal 1992 and \$64.3 million annually after that. Over a 20-year period, debt service on the bonds would be over \$1 billion.)

Also contingent on approval of Proposition 4, HB 64 by Vowell (72nd Legislature, second called session) appropriates \$40.7 million from general-obligation bond proceeds to the Texas Youth Commission to construct, repair or remodel facilities and \$35.4 million to TXMHMR to construct, repair and remodel facilities.

HB 93 and HB 64 together would appropriate \$748.2 million of the \$1.1 billion in general-obligation bonds that would be authorized if Proposition 4 is approved.

HB 93 includes other provisions that are not contingent on approval of Proposition 4. It creates a new substance abuse felony punishment for certain defendants convicted of nonviolent felony offenses. These defendants would be sentenced to confinement and treatment in a substance-abuse treatment facility for six months to a year, followed by either release, probation or probation revocation resulting in two to 10 years in prison and a fine of not more than \$10,000. HB 93 also advanced by two years the previously authorized starting dates for TDCJ-ID to begin three- and six-month programs to treat and confine in special therapeutic prison units those inmates identified as needing drug and alcohol abuse treatment. The bill also includes a settlement of the overcrowding lawsuits brought against the state by 14 counties seeking reimbursement for the cost of holding convicted felons awaiting transfer to prison. It also repeals the Penal Code as of Sept. 1, 1994 and creates a commission to study criminal punishments, sentencing practices, parole laws in preparation for the 1993 regular legislative session and makes various other changes in the criminal justice statutes.

SUBJECT: "Freeport" property-tax exemption option for enterprise zones

BACKGROUND: **Enterprise zones.** The Texas Enterprise Zone Act permits the state and local governments to offer tax incentives and regulatory relief to induce businesses to locate or stay in certain depressed areas that have pervasive poverty, unemployment and economic distress.

Local governments establishing these areas, known as "enterprise zones," may grant property tax reductions or refunds, allow reduced fees, defer compliance with certain development ordinances, accelerate permit procedures or reduce public utility rates.

State agencies may exempt businesses in enterprise zones from agency regulations, except those relating to civil rights, equal employment, equal opportunity, fair housing rights, historical preservation or environmental health or regulations specifically imposed by law. Businesses in enterprise zones are entitled, in certain cases, to a refund of state sales taxes paid on equipment or machinery or on building materials used for remodeling, rehabilitating or constructing a structure in an enterprise zone. Businesses in enterprise zones also are entitled to a deduction from state franchise tax payments for a portion of capital investment in the zone or a partial refund of franchise tax payments.

An area may be nominated as an enterprise zone by a city or county if the area has a higher-than-average unemployment rate or population loss and is a low-income area eligible for federal urban development action grants, has a large proportion of residents with low incomes or has abandoned buildings, job losses or tax arrearages on buildings. An enterprise zone must contain at least one square mile, but cannot be larger than 10 square miles or 5 percent of the area of the municipality or county.

The governing body of the municipality or county nominating an area as an enterprise zone applies to the Texas Department of Commerce. If the department finds that the area meets the necessary criteria, the department negotiates with the governing body filing the application for agreements designating the zone, the zone's administrative authority, if any, and its duties and functions.

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At least one quarter of the workers at a business receiving enterprise zone benefits must be residents of the zone, unemployed persons, food stamp or welfare recipients, ex-offenders or handicapped workers.

Texas currently has 96 enterprise zones, divided almost equally between urban and rural areas. The state has approved 60 enterprise zone projects — businesses eligible for state tax incentives. Local governments may offer additional incentives to these businesses and to other firms operating in an enterprise zone and hiring residents of the zone or economically disadvantaged individuals.

Freeport exemption. In November 1989 the voters approved an amendment to the Texas Constitution (now Art. 8, sec. 1-j) that provides a property tax exemption for goods, wares, merchandise and ores — except oil, gas and petroleum products — that are acquired in or imported into the state, used for assembling, storing, manufacturing, processing or fabricating and shipped out of the state within 175 days of being acquired or imported. This exemption is known as the "freeport" exemption.

A city, county, school district or junior college district that acted before April 1, 1990 to override the "freeport" exemption may *continue* to tax freeport property. A taxing unit may rescind its decision to tax, but the rescission is irrevocable.

The State Property Tax Board reported in July 1990 that nearly three-quarters of eligible taxing units — 1,738 of 2,333 — elected to continue taxing freeport goods after 1990. Roughly four-fifths of all counties and school districts still tax such goods.

DIGEST:

Proposition 5 would amend the Constitution to permit a city, county or junior college district (not a school district) to exempt from taxation "freeport" tangible personal property (including oil, gas and petroleum products) within an enterprise zone.

The property would have to be acquired in or brought into a Texas enterprise zone to be forwarded outside the state, would have to be assembled, stored, repaired, maintained, manufactured, processed or fabricated inside the enterprise zone and would have to be transported

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outside the state within 175 days after being acquired or brought into a Texas enterprise zone.

An enterprise zone would have to be designated as such by the state agency responsible for economic development and would have to meet statutory qualifications, including being an area with pervasive poverty, unemployment and economic distress. A tax exemption could be granted only to a business that was actively engaged in a new venture in an enterprise zone or was expanding a business already active in the zone.

The taxing unit could grant the property tax exemption if it entered into a written agreement with the business receiving the exemption stating the duration and terms of the exemption.

The official action to exempt the property would have to be taken before April 1 of the first year in which the property would otherwise be taxed.

The ballot proposal reads: "The constitutional amendment authorizing the exemption from ad valorem taxes of certain property in an enterprise zone."

SUPPORTERS
SAY:

Proposition 5 would allow cities, counties and junior college districts to grant "freeport" property-tax exemptions to businesses in an enterprise zone without granting the exemption to *all* businesses in the taxing unit. This would let local communities enhance the attractiveness of local enterprise zones for economic development without granting a blanket tax exemption. Unlike the general freeport exemption, local taxing units would have complete discretion about when and how the freeport exemption in enterprise zones would be granted.

Enterprise zones have proved to be an effective economic development tool for improving blighted areas. According to the Texas Department of Commerce, enterprise zone incentives have created 10,750 jobs and \$1.4 billion in investment since their inception in 1989. The narrowly targeted freeport tax exemption that local taxing units would be allowed to grant to businesses agreeing to locate in enterprise zones would help enhance development in the zones and create jobs in areas of chronic unemployment.

Some local taxing units that want to attract new businesses to enterprise zones or to encourage expansion of existing businesses in these zones cannot offer a "freeport" exemption because an exemption for *all* "freeport" property within the jurisdiction would be too costly. Many of the communities that elected to continue taxing freeport property did so because they did not have time to find a substitute for the revenue that would be lost. Proposition 5 would give them the local option of offering an exemption narrowly targeted as an economic development incentive in enterprise zones only. Since the exemption would be given only for new investment, local governments would not suffer a loss of current revenue.

Business groups involved in attracting new jobs to Texas have indicated that the enterprise zone "freeport" option would help bring new jobs to the neediest communities in the state. Jurisdictions that offer tax exemptions anticipate that the net gain in new jobs and tax revenue would surpass the immediate cost of the exemption. However, the taxing units would be free to decide whether and how to offer this exemption within enterprise zones, areas that by definition need economic incentives the most. Unlike the general freeport exemption, the enterprise zone exemption would not be automatic and would not have to be overridden by local action.

Allowing school districts to offer this exemption might unduly complicate implementation of the proposed new state school-finance system. The new county education districts already must grant the freeport exemption, since they were created after the April 1, 1990 deadline for taxing units to override the exemption and tax freeport property. If independent school districts granted a freeport exemption for their component of school taxes, the guaranteed-yield feature of the school-finance system would shift the cost of the exemption directly to the state. (Under the guaranteed yield system, the state guarantees that each penny of the district's property tax rate will raise a certain amount of revenue per student; if property were exempted from taxation by a school district, then local revenue per student would drop and the state would have to make up the difference.)

OPPONENTS
SAY:

Proposition 5 would create another special-interest tax exemption that would deprive cities, counties and junior colleges of a portion of their tax base just when they are squeezed for revenue. The lost revenue and

increased costs for local entities would have to be made up with higher taxes on other property or reductions in services.

Businesses often lure local communities into a "bidding war" in which the localities compete for scarce new jobs by offering tax breaks, such as enterprise zones and the "freeport" exemption, as an attraction for businesses to locate in their area. Yet most objective studies have determined that local tax rates are irrelevant to the general level of investment in economically depressed areas, such as those designated as enterprise zones. Business-location decisions are chiefly influenced by the educational level of the local workforce and the availability of good roads and railways. Nevertheless, if a business tax break is available, local governments often feel compelled to grant it rather than risk losing a perceived competitive edge, even though the business planned to locate in the community all along.

Texas communities could attract more businesses by taxing all companies equally and spending the revenues on education and transportation than by offering special tax breaks to certain businesses in selected neighborhoods. Job training would create skills that remain in a community, even after a specific company closes its doors. In comparison, tax breaks do nothing to change the underlying causes of economic distress and break the cycle of poverty that grips depressed areas.

OTHER
OPPONENTS
SAY:

School districts, which now may grant "freeport" exemptions districtwide, should also be allowed to grant freeport exemptions in enterprise zones only. Given an 'all or nothing' option, districts interested in providing a local economic development incentive can only grant a freeport exemption covering the entire district, which would result in a greater tax loss (and cost to the state) than would an exemption narrowly targeted to just an enterprise zone.

NOTES:

Among the largest municipalities that would be affected by the amendment (since they have continued to *tax* freeport goods) are Houston, Arlington, Lubbock, Garland, Irving, Plano, Pasadena, Beaumont, Abilene, Mesquite and Grand Prairie. The largest counties taxing freeport goods include Harris, Dallas, Bexar, Hidalgo, Nueces, Collin, Cameron, Jefferson, Fort Bend, Lubbock and Galveston.

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Among the largest municipalities that would not be affected by the amendment (since they did not override the freeport exemption and therefore *do not* tax freeport goods) are Dallas, San Antonio, El Paso, Austin, Fort Worth, Corpus Christi, Amarillo, Laredo, Waco, Brownsville and Wichita Falls. The largest counties not taxing freeport goods include Tarrant, El Paso, Travis, Denton, Montgomery, Webb, Tom Green, Potter and Randall counties.

SUBJECT: Appointing the Texas Ethics Commission, allowing it to set legislative pay

BACKGROUND: **Ethics commission.** During the 1991 regular session the Legislature enacted SB 1 by Glasgow, which abolishes the dormant State Ethics Advisory Commission and creates the Texas Ethics Commission. The Legislature appropriated \$2.8 million to finance the commission in fiscal 1992-93.

On January 1, 1992 the new eight-member ethics commission will assume the secretary of state's duties regarding reports of campaign spending and contributions, lobby registration and expenditures and financial-disclosure statements by state officials and issuing advisory opinions. The commission must computerize and cross-reference all reports and permit electronic access to the public by January 1, 1993. The commission will study campaign finance laws and judicial campaigns and provide ethics training for legislators and state employees. The commission may employ a staff to perform these functions, including an executive director and a general counsel.

The commission may investigate formal complaints against state officials and may initiate its own investigations if six of the eight commissioners agree. It may hold hearings, issue subpoenas, agree to the settlement of issues and initiate civil enforcement actions and refer cases to the appropriate prosecuting attorney. All proceedings leading up to a formal hearing on a complaint must be confidential. Revealing facts about a preliminary investigation or filing a frivolous complaint will result in a \$10,000 civil fine.

To enforce ethics laws the commission may issue and enforce cease-and-desist orders, impose civil fines up to \$5,000 and deny, suspend or revoke a lobbyist's registration.

Legislative pay. Art. 3, sec. 24 of the Texas Constitution sets the pay of members of the Legislature. Since 1975 the monthly salary has been \$600 (\$7,200 a year). Legislators also receive \$30 a day (called "per diem") when the Legislature is in regular session (140 days in odd-numbered years) and special session (up to 30 days, whenever called by the governor).

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In computing their federal income-tax liability, state legislators who reside more than 50 miles from the Capitol building may deduct an amount for living expenses incurred when doing legislative business in the state's capital city. The maximum deduction varies among state capitals and is based on the amount that federal civil servants receive as reimbursable travel expenses. The amount currently allowed for Austin is \$85 per day. Legislators may claim the \$85 per day maximum federal income tax deduction without documenting their actual expenses.

In addition to monthly salary and per-diem pay, the House and the Senate allow legislators to claim reimbursement for living expenses related to legislative business that requires them to spend time in Austin away from their permanent residence. The legislative expense reimbursement equals the \$85 maximum federal income tax deduction rate set by the IRS. (The House does not allow members residing within 50 miles of the Capitol to claim reimbursement for legislative business in Austin.)

Until this year legislators could not receive the \$85 per day legislative expense reimbursement for days when the Legislature was in session. The expense reimbursement was allowed only between sessions, when the \$30 per-diem payments ceased. However, on May 2, 1991 Attorney General Dan Morales issued an opinion, DM-23, determining that the legislative expense reimbursement may be paid at any time, regardless of whether the Legislature is in session. The attorney general noted prior judicial rulings that the \$30 constitutional per-diem payment is considered to be legislative pay and therefore does not preclude other payments made as reimbursement.

The Constitution also specifies that legislators are entitled to travel mileage at the same rate set in law for state employees. The attorney general noted in the May opinion that members are entitled to mileage expenses for "all travel necessary for attendance at legislative sessions or in carrying out other official business of the Legislature."

The speaker of the House, who is elected by fellow House members, receives the same pay as any other legislator. The lieutenant governor, who is elected statewide and presides over the Senate, receives the same salary as members of the Legislature, except when substituting for an

absent governor; on those days the lieutenant governor receives the governor's pay.

DIGEST:

Proposition 6 would establish the Texas Ethics Commission as a constitutionally created agency. It also would allow the commission to propose to the voters legislative-salary amounts above \$600 a month and to independently set the amount of legislative per diem pay.

Appointment of the commission. The eight-member commission would include:

- two members of different political parties appointed by the governor from a list of at least 10 names submitted by each of the party caucuses in the House of Representatives and two members appointed by the governor from a list of at least 10 names submitted by each of the party caucuses in the Senate. (Members from those political parties required by law to hold a primary election could caucus and submit nominees.) The governor would have the right to reject all the names on any list submitted and to require that a new list be submitted.
- two members appointed by the speaker of the House from a list of at least 10 names submitted by each of the party caucuses in the House of Representatives.
- two members appointed by the lieutenant governor from a list of at least 10 names submitted by each of the party caucuses in the Senate.

Commission members would serve four-year terms, although the governor, the speaker and the lieutenant governor would each make one of their initial appointments for a two-year term. Commissioners who served one term and part of another would be ineligible for reappointment. Vacancies for unexpired terms would be filled in the same manner as the original appointment. The members of the commission annually would elect a chair.

Legislative pay. The ethics commission could propose to voters that legislative salaries be set at more than \$600 a month and could recommend that the salaries of the speaker of the House and the lieutenant governor exceed those of legislators.

The commission's salary recommendations would be submitted to voters at the next general election for state and county officers. If approved, the recommended salary would take effect on January 1 of the next odd-numbered year.

The amount of per-diem pay received by legislators would no longer be specified in the Constitution but would be set by the commission. Per-diem pay could not exceed the amount allowed as a federal income-tax deduction by a state legislator for living expenses connected with legislative business, disregarding any exception for legislators who reside near the Capitol. The per diem amount would have to reflect reasonable estimates of costs and could be raised or lowered biennially as necessary to pay those costs.

Increasing the emoluments (payments and benefits) of the lieutenant governor would not disqualify a legislator from serving in that office during the term for which the legislator was elected.

The ballot proposal reads: "The constitutional amendment creating the Texas Ethics Commission and authorizing the commission to recommend the salary for members of the legislature and the lieutenant governor, subject to voter approval, and to set the per diem for those officials, subject to a limit."

**SUPPORTERS
SAY:**

Ethics commission. A strong, balanced ethics commission with record-keeping, investigatory and enforcement authority is a prerequisite to ethical state government. Authorizing the commission in the Constitution, as well as in statute, would help enable it to operate autonomously, without fear of being dissolved by the Legislature in the future.

In order to ensure a truly bipartisan commission, its members should be appointed by the state's top three leaders from nominations made by the legislative party caucuses. The structure of the commission — four Democrats and four Republicans — would ensure that no one would be a

victim of partisan attacks. While questionable ethical behavior would be closely scrutinized, the commission would be balanced enough to avoid political witch hunts. Other political parties would be represented when they elect members to the Legislature and their voting strength is sufficiently high that they are required to hold a primary (under current law, a party must hold a primary when its candidate for governor in the last election received over 20 percent of the vote.)

Allowing the speaker of the House to directly appoint two ethics commissioners would balance the nominating process between both houses of the Legislature. As one of the Legislature's two leaders, the speaker should have the same powers of appointment as the Senate's presiding officer, the lieutenant governor. For these reasons, this narrow exception to the constitutional separation of powers between the legislative and executive branches is wholly justified.

Legislative pay. Proposition 6 would establish a more objective means of setting legislative compensation, allowing the ethics commission to set the amount of salary and per diem pay for legislators. Given the many duties legislators perform and the financial sacrifices they must make on behalf of the state, the current legislative salary of \$7,200 per year and the \$30 per diem pay during sessions are inadequate. The legislative salary was set too low when it was last raised in 1975, and inflation has since eroded it considerably. Since 1975, legislative salaries have increased in every other state except New Hampshire and Rhode Island. Moreover, most other states compensate their legislative presiding officers for their additional leadership duties, which are full-time jobs with statewide significance.

The days of the part-time legislator are over. Serving in the Legislature has become a demanding, full-time job. Special sessions occur more frequently as issues facing state government grow more complex. Interim work, such as serving on study committees and assisting constituents, has expanded in scope and now requires the attention of legislators even when the Legislature is not in session.

An independent commission, rather than the Legislature, could objectively review the compensation paid to state lawmakers and submit proposals to the voters. A more flexible mechanism for setting legislative salaries is

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long overdue. A neutral commission could recommend legislative pay based on objective criteria, rather than having the legislators themselves propose their own salaries by the cumbersome means of a constitutional amendment. The voters still would ultimately decide whether to approve any salary proposal.

Proposition 6 also would allow the ethics commission to establish a more realistic level of per diem pay for state lawmakers, which could be no more than the federal income-tax deduction allowed for legislative expenses. Once a per diem level was established that better reflects the actual cost to legislators of serving away from home, each house could then decide whether to continue to allow legislators to claim additional reimbursement of legislative expenses during a session. (Under the current procedure many, but not all, legislators claim expense reimbursement for time spent in Austin when the Legislature is in session.)

Since the cost of serving in the Legislature fluctuates over time, the ethics commission should determine the appropriate level of per diem compensation, rather than locking into the Constitution an arbitrary amount that can be changed only with great difficulty and expense. There is no need to place a per-diem proposition on the statewide ballot every time the commission notes some small fluctuation in legislative costs. The per diem amount set by the commission would be subject to a limit objectively and conservatively established by a neutral entity, the Internal Revenue Service.

Proposition 6 also includes a "cleanup" provision clarifying that members of the Legislature who vote to increase the emoluments of the office of lieutenant governor may serve in that office. (Art. 3, sec. 18 of the Constitution bars legislators from serving in an office during the entire term for which they were elected if the Legislature increased the "emoluments" for that office.) In 1990 the Texas Supreme Court, in *Brown v. Meyer*, 787 S.W.2d 42, narrowly defined "emoluments" to mean only actual pecuniary gain, not retirement benefits or other indirect benefits. Since the ethics commission and the voters, not the Legislature, would set the salary of the lieutenant governor, the possibility is remote that a legislator could have a conflict of interest by voting to provide some monetary gain to the lieutenant governor's office, then running for that office in order to obtain that benefit.

OPPONENTS
SAY:

Ethics commission. Since the Texas Ethics Commission already has been created by statute, there is no real need to establish it in the Constitution. Creating the commission in the Constitution would not guarantee that it would be given any effective authority to regulate political funds or prevent conflicts of interest, as the toothless ethics law passed by the Legislature this year demonstrates. The State Ethics Advisory Commission was established with great fanfare in 1983 but has been moribund since 1986 because the Legislature cut off its funding; it could do the same to the new ethics commission, regardless of whether it is in the Constitution.

SB 1, the law implementing the ethics commission, is riddled by omissions, such as its failure to limit lobby spending on legislators for food and drink. Voters should reject enshrining the commission in the Constitution until the many defects in the implementing law are corrected.

Granting the speaker of the House — a legislator — the authority to make appointments to the ethics commission — an executive-branch agency — would subvert the "separation of powers" doctrine, a fundamental tenet of American democracy established to prevent the over-concentration and potential abuse of power in one branch of government. The speaker is not truly equivalent to the lieutenant governor, who is a member of the executive branch and is elected by, and accountable to, the voters statewide. Rather, the speaker is but one member of the House elected by the voters of a single state-representative district and chosen as speaker by his House colleagues. The checks and balances between the executive and legislative branches, which are meant to prevent arbitrary exercise of government power, should not be blurred by authorizing a legislative official to make executive appointments.

Legislative pay. Proposition 6 would grease the skids for a legislative pay increase on the heels of recent increases in legislative retirement benefits and expense reimbursements. No longer would the Legislature have to get a two-thirds vote in both the House and the Senate in order to propose salary increases to the voters. Instead, a group of unelected appointees — the Texas Ethics Commission — could put a salary increase on the ballot. Moreover, the authority to set the per-diem amount paid to legislators during legislative sessions would be taken away from the voters entirely and given to the unelected ethics commission.

It has not been definitively proved that legislators *need* a pay raise. In addition to their salaries they receive plenty of other benefits that are neither set in the Constitution nor subject to voter approval. Many of the states paying annual salaries exceeding \$7,200 also have legislatures that work more than 140 days every two years. In off years, Texas legislators receive their full legislative salary, even if no special sessions are called and interim duties are relatively light.

Even when they are not in Austin, lawmakers benefit from intangibles such as greater access to potential employers, widespread name identification and enhanced business opportunities. The House and Senate each provide monthly operating accounts to the members to pay for staff support and other costs of operating Capitol and home district offices. In addition, members may use political funds, known as "officeholder accounts," to defray certain expenses arising from legislative service. The generosity of lobbyists and other contributors has allowed many legislators to stretch their official income further still. The Internal Revenue Service allows legislators generous standards for offsetting their legislative income through expense and travel deductions. In addition, legislators receive handsome retirement benefits, recently increased, that are based not on the level of their own salary but on that of district judges.

In 1989, when the Legislature last tried to remove legislative pay levels from the Constitution, the voters clearly stated that they want to have the final say on legislative pay. Yet this proposed amendment would remove the voters from the process of setting the per diem payment to legislators and instead transfer that power to an unelected commission appointed by the legislative leaders and the governor from nominees submitted by the legislators themselves. Commission members beholden to the Legislature for their appointments would be setting the per-diem amount and recommending salary levels for those who appointed them.

The attorney general's May opinion already has cleared the way for a large increase in *expense reimbursements*, which now may be paid to legislators year-round, including when the Legislature is in session. For most legislators, this means that they may claim \$85 per day when they are in Austin while the Legislature is in session *in addition* to their \$30 per diem pay. An increase in both salary and per-diem pay on top of this extra

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reimbursement is unwarranted, especially since the voters no longer would have any say in setting the per diem amount.

Authorizing the ethics commission to increase legislative per diem from the specific amount of \$30 per day to an amount decided by the IRS could cause legislative compensation to skyrocket. Per diem pay is an *income supplement*, not an expense reimbursement, as the attorney general already has ruled. Under the current IRS limit, the commission could set per diem pay as high as \$85 a day, while the House and the Senate could allow members to claim an *additional* \$85 as expense reimbursement, for a total of \$170 per day. The IRS maximum reimbursement is adjusted upward every year, virtually ensuring that legislative compensation would increase steadily (from *two* different sources — per diem and expense reimbursement) without the voters having any say.

Allowing legislators who vote to increase the emoluments of the office of lieutenant governor also to run for that office and receive the benefits they voted to provide would create a conflict of interest. Legislators should have to wait until their term has ended before running for another office for which they have voted to increase the benefits.

OTHER
OPPONENTS
SAY:

Proposition 6 would assemble a highly partisan ethics commission composed of four commissioners from each party. By allowing politically charged legislative caucuses to screen and nominate the ethics commissioners, this amendment would set up an ethics commission whose members are more loyal to the politicians that select them than to the public they are supposed to serve. The Texas Ethics Commission could become like the highly partisan and ineffective Federal Elections Commission, whose six members also are picked on the basis of party loyalty and almost always deadlock along party lines. The secretary of state or some neutral member should be given a voting seat on the commission at least to break the inevitable 4-4 deadlocks.

The structure of the commission would shut out independents and most third parties, since the Democratic and Republican parties would have an exclusive monopoly on commission appointments. This would unfairly leave many voters unrepresented.

The new ethics law contained in SB 1 will establish a procedure for appointing the commission similar to that in Proposition 6, but as a statute SB 1 could be revised simply by enacting another law. But if this proposed constitutional amendment is approved, the commission's inherently flawed nominating process will be locked into the state Constitution, requiring another constitutional amendment to change it.

If legislative pay increases are to be recommended, then the voters should be assured that potentially corrupting outside sources of income resulting from legislative duties will be limited or eliminated. The Legislature could bolster public support for higher compensation by strictly limiting lobby gifts and campaign finances.

Other ethics commission provisions contained in SB 1 further undermine the new commission's ability to act as a strong ethics watchdog. For example, the commission cannot take any significant action without six of the eight commissioners' consent and cannot investigate complaints during an election. In addition, the commission may levy exorbitant fines against citizens who make "frivolous complaints," and most of the commission's activity is exempt from the Open Meetings Act and the Open Records Act. The defeat of Proposition 6 would resoundingly state that the people of Texas reject the watered-down ethics law passed by the Legislature.

Proposition 6 should include a more definite limit on the amount of per diem pay. It says that per-diem pay would be capped at the amount allowed as an expense deduction on federal income-tax returns for *legislators*, without specifying *Texas* legislators. By reading the amendment broadly, the ethics commission possibly could set a substantially higher limit. The deduction limit for Austin, Texas for 1990 was \$85, while the limit for Alaska legislators serving in the state capital of Juneau was \$166, the highest amount of any state. Such an indefinite cap creates a potential loophole that could be scarcely better than no limit at all.

The implementing law for this amendment was so hastily drafted that it contains many oversights and errors. For instance, the section of SB 1 calling for a voter referendum on proposed legislative salary increases will be *repealed*, rather than implemented, if the amendment is adopted. While it is possible that the constitutional language on the referendum might be

self-enacting, eliminating the need for a specific provision in state law, this is not clear.

NOTES:

If Proposition 6 is not approved by the voters, SB 1 — the implementing legislation for the amendment — still will create a state ethics commission. However, the commission would not be authorized to recommend legislative salary increases to the voters or to set legislative per diem pay. Moreover, if Proposition 6 is not approved, the speaker of the House would not be able to directly appoint two of the eight commissioners. Instead, the two members would be appointed by the governor from a list of 10 names chosen by the speaker of the House from a list of at least 20 names submitted by both party caucuses in the House of Representatives. All other provisions of SB 1 will take effect regardless of whether Proposition 6 is approved by the voters.

In recent years Texas voters have considered constitutional amendments on subjects similar to those in Proposition 6. In 1971 the Legislature proposed SJR 15, which would have established a State Ethics Commission composed of nine members, three appointed by the chief justice of the Supreme Court, three by the presiding judge of the Court of Criminal Appeals and three by chairman of the Judicial Qualifications Commission, plus two ex officio members, one each from the House and the Senate, elected by the membership. Among other duties, the commission could have set the salary, per diem and travel allowance for members of the Legislature and could have set higher salaries for the speaker and the lieutenant governor. Commission recommendations could have taken effect only if approved by a resolution adopted by a record vote of both houses. The voters rejected SJR 15 at an election held on May 18, 1971 by 273,191 in favor (35.3 percent), 500,981 against (64.7 percent).

Two subsequent attempts to amend the Constitution to raise legislative salaries were unsuccessful. On November 7, 1972 the voters rejected HJR 58, which would have raised legislative salaries from \$400 per month (\$4,800 a year) to \$8,400 per year, by 1,251,713 in favor (46.6 percent), 1,436,910 against (53.4 percent). On November 6, 1973, the voters rejected SJR 8, which, in addition to providing for annual legislative sessions, would have raised legislative salaries to \$15,000 per year and per

diem from \$12 per day to \$18 per day, by 259,918 in favor (43.3 percent), 340,046 against (56.7 percent).

A third try at raising legislative pay was successful. At an election held on April 22, 1975, the voters by 313,516 in favor (57.9 percent), 227,786 against (42.1 percent), approved HJR 6, which increased legislative salaries from \$400 per month to \$600 per month (\$7,200 a year) and increased per diem from \$12 per day to \$30 per day.

Also in 1975, as part of a proposed new Constitution, the Legislature proposed that a nine-member salary commission annually review and recommend legislative compensation and allowance amounts. Compensation and allowances could not have exceeded recommended levels, and no compensation change could have taken effect prior to the first regular session following a general election. The commission would have been appointed on a nonpartisan basis by the governor, lieutenant governor, House speaker, attorney general and chief justice of the Supreme Court, acting together. The salary commission was included in Proposition 1, affecting the executive and legislative departments and separation of powers, which was rejected by the voters on November 4, 1975 by 299,646 in favor (25.6 percent), 870,844 against (74.4 percent).

At the November 6, 1984 election, the voters by 1,233,314 in favor (33 percent), 2,504,733 against (67 percent), rejected HJR 22, a proposed constitutional amendment that would have set per diem pay to legislators at the maximum amount allowed to state legislators as a federal income tax deduction for legislative expenses.

At the November 7, 1989 election, the voters rejected two proposed amendments concerning legislative compensation; both were included in HJR 102. Proposition 1, which would have set the salary of legislators at one-quarter of the governor's salary (which is set by the Legislature) and the salary of the speaker and the lieutenant governor at one-half of the governor's salary, was rejected by 424,704 in favor (36.7 percent), 732,417 against (63.3 percent). Proposition 11, which, like HJR 22 in 1984, would have set the per diem level at the maximum amount allowed to legislators as a federal income tax deduction for legislative expenses, was rejected by 531,550 in favor (47.3 percent), 592,412 against (52.7 percent).

SUBJECT: Broadening the investment authority of state retirement systems

BACKGROUND: The investment policies of the state's Employees Retirement System (\$7.4 billion in assets as of August 31, 1991) and Teacher Retirement System (\$26.5 billion in assets as of August 31, 1991) are governed by Art. 16, sec. 67(a)(3) of the Texas Constitution, which allows the system boards to invest system funds in "such *securities* as the board may consider prudent."

A 1980 attorney general's opinion (MW-152) determined that the term "securities" includes "evidences of debt," such as a mortgage certificate backed by real estate, but does not include *direct* investments in real estate. The opinion concluded that "a constitutional amendment would be necessary to enable the board of trustees of the Teacher Retirement System to invest its funds in real property."

The "prudent-person rule" governing retirement fund investments requires that trustees "exercise the judgment and care under the circumstances then prevailing that persons of ordinary prudence, discretion and intelligence exercise in the management of their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income therefrom as well as the probable safety of their capital."

The Constitution permits the Legislature to further restrict a board's investment discretion. However, the statute defining the duty of care for the Employees Retirement System (Government Code, sec. 815.307) only restates the prudent-person rule, while the statute regulating investment by the Teacher Retirement System (Government Code, sec. 825.103(b)) merely refers to the constitutional provisions.

DIGEST: Proposition 7 would amend Art. 16, sec. 67(a)(3) of the Constitution to permit the Teacher Retirement System (TRS) and the Employees Retirement System (ERS) to invest system assets in such *manner* as their boards may consider *prudent*, rather than in such *securities* as their boards may consider *prudent investments*.

The ballot proposal reads: "The constitutional amendment to allow the board of trustees of a statewide public retirement system to invest funds of the system in a manner that the board considers prudent."

**SUPPORTERS
SAY:**

Proposition 7 would grant additional flexibility to allow the state retirement system boards to make a wider range of prudent investments to diversify system holdings and boost the return on system funds, to the benefit those served by the systems. It would permit the Teacher Retirement System (TRS) and Employees Retirement System (ERS) to directly invest in real estate and investment vehicles such as private placements and limited partnerships that could increase the investment return on retirement funds without undue risk.

Other state funds that are governed solely by the prudent-person rule, such as the Permanent School Fund and Permanent University Fund, already have the authority to make direct real-estate investments; no problems have occurred with either of these funds. Texas pension fund trustees have been extremely conservative in their past investments and are unlikely to be lured into unreasonable risks in the future. The prudent-person standard is widely accepted as an adequate safeguard and limitation on investment authority, ensuring wise investments in the long-term interest of the beneficiaries of the funds.

The State Pension Review Board has recommended, in its *1989-90 Biennial Report, Vol. 2*, that "all constitutional or statutory restrictions on real estate investment by public retirement funds should be amended to permit such investment." Many investment professionals feel that real estate is an appropriate investment for public funds, since it helps diversify a large portfolio, balancing it against downturns in the stock and bond markets. Over long periods of time, real estate has produced better total returns than other acceptable investments.

Banks and savings and loans ran into trouble in making real estate investments by competing for risky loans in raw land and speculative projects. The statewide retirement funds, with their large cash reserves, would be able to select only the best real estate projects for investment. Financial institutions often were pressured by over-zealous regulators or nervous stockholders to terminate their investments prematurely. In

contrast, a pension fund has a long-term perspective that would permit it to wait for real estate values to recover, even if it took 10 years.

The real estate currently held by the TRS is performing adequately. Although the properties were not obtained by direct investment, the fund's ownership of real estate has not damaged the fund's total investment returns. Recent appraisals show that the properties are still worth nearly the amount loaned by the fund, and the cash flow has been sufficient to sustain the properties without draining money from the fund. Under State Pension Review Board recommendations, a fund could invest up to 20 percent of its assets in real estate — double the TRS' current stake — without a significant increase in risk.

Direct real estate investments would allow the pension funds to receive rental income that would grow with inflation, while mortgage loans are limited to the fixed payments determined at the beginning of the loan. Direct investments also would permit the systems to control the management of a property, rather than relying on a developer's business decisions.

OPPONENTS
SAY:

Investment managers should not be allowed to take risks with money that is dedicated to supporting retired state employees and teachers. Many private investors, banks and savings and loans have gone bankrupt because of their speculative investments in Texas real estate in the past decade. This recent experience should not be ignored in determining permissible retirement fund investments.

The Teacher Retirement System already owns \$2.3 billion of real estate, accumulated when mortgage loans made by TRS went bad. When the borrowers went bankrupt or could not continue the mortgage payments, the TRS foreclosed on the loans and took possession of the buildings. TRS currently owns one of the largest shopping malls in El Paso, one of the largest office buildings in Austin, a 20-story building in Las Colinas near Dallas and warehouses in Houston, plus property in Florida, Georgia, Arizona and California. Real estate holdings already account for nearly 10 percent of the system's assets; there is no need to authorize further concentration of TRS assets in this unstable area.

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Proposition 7 would leave the door wide open for TRS and ERS trustees to gamble the pension funds of thousands of teachers and state employees with real estate speculators. Direct real estate investments are even riskier than the mortgage loans that currently afflict TRS. Since developers invest some of their own money in real estate projects, a pension fund making a mortgage loan to the developer has some margin of safety against loss. (A loan for 80 percent of the value of a project is fully protected as long as the value of the real estate drops by less than 20 percent.) In contrast, a direct investment in real estate offers no buffer against losses — any drop in the value of the real estate would be reflected directly in a decrease in the system's assets.

Proposition 7 also would permit pension fund investments in such risky ventures as futures and commodity trading, venture capital investments, oil and gas exploration, timberland purchases and similar speculative undertakings. Such investments would be limited only by a pension fund board's concept of prudence, unless the Legislature acts in the future to limit TRS and ERS investments. The "prudent person" standard is an unreliable shield from questionable investments. For instance, state pension funds in New York, Oregon, Washington and other states have placed hundreds of millions of dollars in leveraged-buyout funds that have destroyed many healthy companies with junk-bond-financed hostile takeovers.

SUBJECT: Allowing state bond debt without a constitutional amendment

BACKGROUND: The principal method by which the state borrows money is by issuing bonds. General-obligation bonds are backed by the full faith and credit of the state. The state guarantees that it will repay bondholders, with interest, with the first money coming into the Treasury each fiscal year. Because creditors are given these assurances of safety, they generally will accept lower interest payments than on state revenue bonds, which do not pledge the state's full faith and credit.

Since Art. 3, sec. 49 of the Texas Constitution prohibits most forms of state debt, a constitutional amendment is required to authorize the state to issue general-obligation bonds. (Since the state's credit is not pledged to repay revenue bonds, those bonds are not considered state debt and may be authorized by statute.) Constitutional amendments are proposed to voters by the Legislature, after approval by at least two-thirds of both the House and the Senate. The wording of the ballot proposals is decided by the Legislature.

Voters approved the first general-obligation bonds in 1946, to finance loans to veterans to purchase land. The amendments to the Constitution that have authorized general-obligation bond debt include:

Veterans land program (Art. 3, sec. 49-b), \$950 million; the veterans housing program (Art. 3, sec. 49-b-1), \$1.3 billion; water development (Art. 3, secs. 49-c and 49-d through d-7), issues of \$100 million, \$200 million, \$200 million, \$980 million, \$400 million and \$500 million; agricultural water conservation (Art. 3, sec. 50-d), \$200 million; park development (Art. 3, sec. 49-e), \$75 million; farm and ranch land purchases (Art. 3, sec. 49-f), \$500 million; superconducting super collider (Art. 3, sec. 49-g), \$500 million; corrections and mental health/retardation facilities (Art. 3, sec. 49-g), \$900 million; rural development (Art. 3, sec. 49-i), \$30 million; college student loans (Art. 3, secs. 50b, 50b-1 and 50b-2), \$85 million, \$200 million and \$75 million; farm and ranch security (Art. 3, sec. 50-c), \$10 million; and new product development and production, \$25 million, and small business incubator funds, \$20 million (Art. 16, sec. 71).

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About \$3.0 billion of the \$7.7 billion total state bond debt outstanding on May 31, 1991 was in the form of general-obligation bonds, while the remainder was in revenue bonds. Another \$3.0 billion in general-obligation bonds and \$2.2 billion in revenue bonds were authorized but unissued.

DIGEST:

Proposition 8 would amend Art. 3, sec. 49 of the Constitution to allow creation of state debt through propositions that would be submitted to the voters but would not amend the Constitution.

A proposition to create state debt would have to be authorized by a joint resolution approved by at least two-thirds of the membership of each house of the Legislature. The joint resolution could be approved during any regular legislative session or during any special legislative session in which the governor allowed the subject of the proposition election to be considered. Elections could be held on any date, with the same notice that is required for elections to amend the Constitution.

Propositions would be required to describe the amount, purpose and repayment source of the debt. After the debt was created, it could not be exceeded or renewed unless stated in the proposition; however, refunding bonds could be issued if permitted under the proposition.

The ballot proposal reads: "The constitutional amendment authorizing the voters of this state to consider state debt questions in the form of ballot propositions that must clearly describe the amounts, purposes, and sources of payment of the debt only after approval of the propositions by a two-thirds vote of each house of the legislature."

Proposition 8 would take effect January 1, 1992.

**SUPPORTERS
SAY:**

Proposition 8 would give the voters more information about state bond proposals without taking away any authority from the voters to control and monitor state debt. Currently, ballot proposals to create state debt only tell the purpose of the bonds, not necessarily the amount or the method of repayment, which can mislead or confuse the voters. This proposed constitutional amendment would require complete disclosure in

bond proposals by requiring that proposals describe the amount, purpose and repayment source.

This proposed amendment would help keep the Constitution, which already contains more than 300 amendments comprising thousands of words, from becoming even more cluttered each time the state needs to borrow funds. As long as strict limitations on state debt remain intact, and voter approval of bond issues is required, cluttering the Constitution with detailed, redundant bond provisions is unnecessary.

Proposition 8 would require the same legislative and voter approval to create new state debt as does the current constitutional-amendment process. Two-thirds of the membership of each house of the Legislature would still have to approve each proposal, and the state's voters would still have the final say.

There is no need to include a cap on bond debt in the Constitution as a special precaution. During this year's first special session the Legislature approved SB 3 by Montford, which sets a limit on the amount of state general revenue that may be used to repay state bond debt. Debt service now may not exceed 5 percent of the three-year average amount of general revenue that is not constitutionally dedicated to specific purposes. (Debt service payments currently are around 1 percent of the general revenue average.)

OPPONENTS
SAY:

Creating new state debt is a serious matter, as is amending the Constitution. Each time the Legislature proposes to create a new exception to the constitutional prohibition against state debt by authorizing new general-obligation bonds, it is fitting that a specific constitutional amendment should be required. Each new bond debt authorization should be inscribed in the Constitution, where it will be part of a complete record for posterity. Getting more information about bond proposals to voters could be achieved more easily if the Legislature adopted clearer ballot language proposing each amendment. Essential information about state debt should be in the Constitution.

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OTHER
OPPONENTS
SAY:

While the Constitution need not be amended for every new bond authorization, the Constitution should contain a ceiling on the creation of new debt by means of propositions. A reasonable debt cap as part of a debt-proposition amendment would reduce the number of times the Constitution has to be amended while still maintaining a constitutional restraint on the total amount of state debt. A statute setting a cap on state debt could be evaded simply by changing the statute, while the voters would have to be consulted to amend a constitutional limit.

NOTES:

Two proposed amendments also on the November 5 ballot would add a total of \$1.4 billion in general-obligation bond authority. Proposition 4 would authorize \$1.1 billion for corrections and mental health/mental retardation facilities, and Proposition 13 would add \$300 million for college student loans.

The proposed 1975 revision of the Constitution included a similar provision that would have permitted the authorization of state debt without amending the Constitution. Under the proposed constitution, debt could have been authorized by law if approved by two-thirds of the membership of each house and a majority of qualified voters. This provision was part of Article 8, the proposed Finance article, which was rejected by the voters on November 4, 1975 by 289,772 in favor (25.2 percent), 871,080 against (75.7 percent).

SUBJECT: Giving title ("land patents") to state land to presumed owners

BACKGROUND: A "land patent" is an original land title granted by the state. In 1900 all unpatented Texas land not granted to individuals or dedicated for other purposes reverted to the School Land Fund. However, in some cases the legal requirements for securing patents were not met in the 1800s, and some persons have belatedly learned that land they thought they had purchased years ago and on which they have been paying taxes does not belong to them but actually belongs to the state School Land Fund. To acquire a valid land patent, these individuals would have to purchase the land from the state.

In 1976 Attorney General John Hill determined (H-881) that the Legislature was powerless to make a free grant of school lands without a constitutional amendment explicitly granting that authority. In 1981 the Legislature proposed, and the voters approved (by 79 percent in favor, 21 percent against), a temporary constitutional amendment authorizing the General Land Office to issue patents for public school land if a person met specific criteria, such as acquiring the land without knowledge of any title defect and a recorded deed and continuous payment of taxes for over 50 years. The amendment, Art. 7, sec. 4A, expired January 1, 1990; according to the General Land Office, around 15 people applied for patents under the provision.

In 1989 the 71st Legislature enacted SB 1840, entitling persons to receive a land patent if they met the criteria set out in the 1981 constitutional amendment but had failed to file an application on time. Under the bill the General Land Office was to place another tract of state-owned land into the School Land Fund in exchange for the land to be patented. However, Attorney General Jim Mattox determined (JM-1242) that the bill was unconstitutional because it attempted to extend by statute an expired constitutional provision and failed to state specifically how the General Land Office was to choose other state-owned land to exchange for patented land from the School Land Fund.

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DIGEST:

Proposition 9 would authorize the General Land Office to issue to qualified applicants a patent for land from the School Land Fund.

To qualify, applicants would have to prove to the School Land Board that they had acquired the land without knowing that the title was defective and that they and any predecessors have held a recorded deed to the land and paid all applicable taxes continuously for at least 50 years as of January 1, 1991. If a patent were denied, an applicant could sue the School Land Board in a district court in the county in which the land was located.

The provisions would not apply to beach land, submerged land, or islands and could not be used to resolve a boundary dispute. They would not apply to any land interest determined by prior court ruling to belong to the state. A patent would reserve mineral rights to the state if there were mineral production within five miles of the land.

The application would have to be filed before January 1, 1993. The amendment would be self-executing (requiring no separate statute implementing the amendment).

The ballot proposal reads: "The constitutional amendment authorizing the commissioner of the General Land Office to issue patents for certain public free school fund land held in good faith under color of title for at least 50 years."

**SUPPORTERS
SAY:**

Proposition 9 would simply revive for a limited period of time a mechanism for correcting an inequity. In a handful of cases, persons who purchased land in good faith face the prospect of having to buy it again, from the state, because of some error or oversight made decades ago. This proposal would provide a means for landowners to gain clear title without any loss of land currently under state control.

Under the amendment, persons applying for a patent would have to meet specific, restrictive criteria, such as holding a recorded deed and paying taxes on the land for at least 50 years. This would ensure that no one could take advantage of the state and apply for undeserved land patents.

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A very similar constitutional amendment, Art. 7, sec. 4A, was approved by the Legislature in 1981 and overwhelmingly endorsed by the voters. However, it expired on January 1, 1990. A new amendment is needed for those who, for a variety of reasons, were unable to take advantage of the expired provision. Nevertheless, this special mechanism should not be open-ended or else it could be subject to abuse — despite the equities involved in clearing these land titles, the patents are, in effect, a gift from the state and should be strictly limited.

If Proposition 9 is approved, the General Land Office plans to try to notify qualified landowners so that all land patents can be cleared up once and for all. The GLO is considering publishing notices in newspapers throughout the state, notifying tax assessors and title companies and searching computer data bases for land that is not patented.

OPPONENTS
SAY:

Under the state Constitution, the land in question legally belongs to the state. This amendment would effectively be making a gift of state lands. The voters should not be asked to amend the Texas Constitution just to benefit as few as one or two people who happen to have land title problems.

OTHER
OPPONENTS
SAY:

The eligibility requirements in Proposition 9 are too rigid and would apply only to a small number of persons, excluding those in similar — but not identical — circumstances who may also be worthy of land patents.

Rather than set in the Constitution a specific, very limited, expiration date for the land patent program, the Legislature should be given the discretion of setting the expiration date as needed. The problem with the 1981 amendment was that the patent program did not last long enough for all those affected to take advantage of it, requiring that this constitutional amendment be submitted to extend the deadline for another year. Some landowners might remain unaware of any question about their land title until they seek to sell or convey their land or have other reason to check their title, *after* the new deadline has passed. The expense and bother of repeated amendment elections changing deadlines could easily be averted.

SUBJECT: Property-tax exemption for nonprofit water supply corporations

BACKGROUND: Art. 8, sec. 1 of the Texas Constitution requires that taxation be equal and uniform and that property be taxed in proportion to its value unless exempted from taxation by the Constitution. Art. 8, sec. 2 allows the Legislature to exempt from taxation "institutions of purely public charity." Sec. 11.18 of the Tax Code exempts from ad valorem taxation (property taxes) the property of "charitable organizations," including those engaging exclusively in "acquiring, storing, transporting, selling or distributing water for public use."

State law (VACS art. 1434a) authorizes three or more people to form a non-profit water supply corporation to furnish water or sewer service, flood control or drainage systems to towns, cities, other political subdivisions, private corporations, military bases and camps or individuals. A water supply corporation can obtain money from cities, counties, political subdivisions, the federal government or other sources to acquire, construct and maintain projects and improvements. Many non-profit water supply corporations obtain funding from the federal Farmer's Home Administration.

The Texas Water Commission estimates that over 800 non-profit water supply corporations operate in the state, mostly in rural areas.

The Texas Supreme Court ruled on February 20, 1991 (in *North Alamo Water v. Willacy County*, 804 S.W.2d 894) that nonprofit water supply corporations are not "purely public charities" under the Constitution and therefore are not entitled to tax-exempt status under the Tax Code. The court, in a unanimous opinion, held that "unlike the benefits provided by charities entitled to this exemption, the benefits dispensed by these corporations do not in any way inure to the entire community but only to individual water district 'members' who are able to pay for those benefits. These corporations are not organized to provide charitable services to the community as a whole but are organized solely for the purpose of selling water to those within the boundaries of the district who can afford to pay the costs assessed."

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DIGEST:

Proposition 10 would add a provision to Art. 8 of the Constitution allowing the Legislature to exempt property owned by a nonprofit water or sewer corporation from ad valorem taxation. To qualify, the property would have to be reasonably necessary for and used in the acquisition, treatment, storage, transportation, sale or distribution of water or the provision of wastewater service.

In order for a corporation to qualify for this exemption, its bylaws would have to provide that if the corporation were dissolved, after payment of its debts its assets would be transferred to another entity that provides water or sewer service and is exempt from ad valorem taxation.

The ballot proposal reads: "The constitutional amendment authorizing the legislature to exempt from ad valorem taxes certain property of a nonprofit corporation that supplies water or provides wastewater service."

**SUPPORTERS
SAY:**

Proposition 10 would let the voters decide whether rural non-profit water supply corporations should be exempt from ad valorem taxes, as most other water suppliers are.

Of the various entities that deliver water and wastewater service to Texans — city utilities, municipal utility districts, water conservation and improvement districts and water supply corporations — only water supply corporations must pay property taxes. The Legislature recognized the unfairness of the situation and amended the Tax Code to define water supply corporations as "charitable" organizations eligible for exemption from property taxes. However, the Texas Supreme Court recently ruled that nonprofit water corporations do not fit the constitutional definition of charities and therefore are not eligible for tax-exempt status. Proposition 10 would allow the voters to grant a specific tax exemption for these nonprofit corporations, resolving the legal issue beyond question.

Customers of a municipally owned utility pay rates that reflect its tax-exempt status, while taxes that a nonprofit utility pay are passed on to its customers in the form of higher rates. This is unfair to the many rural ratepayers who depend upon those nonprofit corporations for their water and sewer service. Under the implementing legislation for Proposition 10 (SB 325 by Ratliff, see NOTES), all savings from a tax exemption would

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have to be passed on to water supply corporation customers, which could reduce water and sewer bills by some 10 percent for the 2.5 million rural Texans who receive their service from nonprofit water supply corporations. No tax savings would go for higher salaries or bureaucracy at the corporations.

The tax savings reflected in lower water and sewer rates would be especially beneficial for low-income residents of the colonias — unincorporated communities along the border — where these non-profit corporations can be used to provide badly needed water and sewer service.

Unlike water districts — which often are used as a land development tool, can issue bonds and impose taxes, and as government entities are tax-exempt — water supply corporations are community-based entities set up solely to supply water and sewer services, *not* to make a profit. The Legislature and local taxing units long have recognized the quasi-charitable nature of these non-profit corporations, and Proposition 10 would simply ensure that they could continue to receive that recognition.

School districts, counties and other local taxing entities would lose little, if any, revenue from this tax exemption. Only half of water supply corporations currently are taxed, partly because of the confusion over their legal status. If this proposed amendment fails and local taxing entities *did* attempt to tax water supply corporations, the corporations might convert to special utility district status to escape further taxation; these districts could levy their own property taxes, adding to the local tax burden. Rural communities would gain more from the economic development stimulated by reasonable water charges than from the small amount of revenue that could be derived from taxing the property of water supply corporations.

Approval of Proposition 10 would activate its implementing legislation, which provides that water supply corporations would be subject to the Open Meetings Act and the Open Records Act. This change would make these corporations more accountable to the public.

OPPONENTS
SAY:

Proposition 10 would erode the tax base in primarily rural communities served by water supply corporations. The tax base of rural school districts and local governments already has been hit hard by declining tax values.

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Approval of Proposition 10 not only would reduce the tax base of certain communities, it might also result in higher property-tax rates, since school districts and counties might have to raise their rates to compensate for the tax loss from the exemption. Property taxes are already going up; they should not be boosted even more to lower water rates for certain consumers.

Private water supply corporations siphon off paying customers from local governments, which sometimes are unable to set up a system because those who would pay have already hooked into private systems supplied by water supply corporations.

Water supply corporations are large utility systems established as private businesses without voter approval. Paying property taxes should be a cost of doing business for these corporations, as for other corporations. If water supply corporations receive a special tax break, rural electric and telephone co-ops and other similarly situated may try to lobby for a similar exemption.

The Legislature proposed similar constitutional amendments in the past (SJR 25 in 1973 and SJR 6 in 1969), which were soundly rejected by Texas voters. Texans already have had ample opportunity to give water supply corporations a tax break and have rejected granting this special privilege.

OTHER
OPPONENTS
SAY:

The state should not encourage creation of water supply corporations by granting tax exemptions. The state already faces difficulty including water supply corporations in any state water plan it might adopt, since many of the districts have contracts and lending agreements with the Farmer's Home Administration that limits their flexibility in complying with state mandates.

NOTES:

SB 325 by Ratliff, the implementing legislation for Proposition 10, would exempt from taxation certain property owned by nonprofit water supply or sewer service corporations and require those corporations that received tax exemptions in 1992 to reduce their rates by the value of the exemption. It also would subject tax-exempt water supply corporations to open records and open meetings requirements. SB 325 would take effect January 1, 1992, contingent on approval of Proposition 10.

In 1969 the Legislature approved a proposed constitutional amendment, SJR 6, that would have granted a property tax exemption for nonprofit water supply corporations, but the proposal was rejected by the voters on Aug. 5, 1969 by 283,915 in favor (46.8 percent), 322,720 against (53.2 percent). In 1973 the Legislature approved a proposed constitutional amendment, SJR 25, that would have allowed the Legislature to grant a property tax exemption for nonprofit water supply corporations and cooperatives, but the voters rejected the proposal on Nov. 6, 1973 by 248,412 in favor (43.4 percent), 323,993 against (56.6 percent).

SUBJECT: Authorizing a state lottery

BACKGROUND: Art. 3, sec. 47(a) of the Texas Constitution requires the Legislature to prohibit lotteries. Sec. 47(a) says, "The Legislature shall pass laws prohibiting lotteries and gift enterprises in this State other than those authorized by Subsections (b) and (d) of this section. Subsection (b), which was added in 1980, authorizes laws permitting bingo. Subsection (d), added in 1989, authorizes laws permitting charitable raffles by certain nonprofit groups.

Penal Code sec. 47.03(a)(5) makes it a criminal offense to set up or promote a lottery for gain or to sell, offer for sale, transfer or possess for transfer any card, stub, ticket, check or other evidence of lottery participation.

For additional background see House Research Organization Special Legislative Report No. 165, *A State Lottery For Texas?*, February 5, 1991.

DIGEST: Proposition 11 would amend Art. 3, sec. 47 of the Constitution to allow the Legislature to authorize the state to operate lotteries and contract with one or more legal entities to operate lotteries on the state's behalf.

The ballot proposal reads: "The constitutional amendment authorizing a state lottery."

SUPPORTERS SAY: A lottery would be a popular way to raise much-needed state revenue, reduce the need for higher state taxes and help avoid a state income tax. For years every survey of public opinion in Texas has shown overwhelming support for this voluntary method of raising revenue. The voters should be allowed to decide whether Texas should join 33 other states and the District of Columbia in operating a lottery.

The Comptroller's Office estimates that if Proposition 11 is approved lottery ticket sales could begin by July 1992. (Instant-win games using paper cards would begin first, followed in approximately six months by computerized "lotto" games.) The comptroller estimates that a lottery would bring in approximately \$462 million in net general revenue to the

state Treasury during the current budget period, fiscal 1992-93. Fully implemented, the lottery would raise an estimated \$781.4 million in additional state revenue in fiscal 1994-95 and \$622.8 million in fiscal 1996 alone.

Lottery revenue already has been factored into the state budget for the next two years. If Proposition 11 is not approved, then state agency budgets will be slashed by \$471 million (based on an earlier revenue estimate), which could result in a reduction in services to people in need.

A lottery would help forestall the need for other unpopular and unfair measures, such as imposing an income tax or increasing the state sales tax, already one of the highest in the country at 6.25 percent.

A lottery is a certain source of sustained revenue. Even though lottery revenue, like tax receipts, may fluctuate from year to year, no state has ever lost money on a lottery, and over the long run state lottery revenue has risen steadily. In 1990 government lottery revenue in the United States totaled \$7.7 billion. Lottery revenue is no more unpredictable than other sources of state revenue that fluctuate yearly, such as sales taxes, which depend on consumer spending, and oil and gas severance taxes, which are affected by price swings.

Lotteries not only produce revenue but also entertain those who choose to play and therefore should not be compared to taxes, which are involuntary payments. Since participation in a lottery is voluntary, no one, poor or rich, is "victimized" — no one is obligated to buy a lottery ticket.

A lottery does not target the poor, as some claim. Studies show that people from all income classes play the lottery and that the middle class, not the poor, plays more than any other group. Studies purporting to show that the lottery is a regressive tax are flawed and should focus on the "average" or "typical" lottery player. Many state taxes — including sales and excise taxes — are regressive. The lottery is "horizontally" equitable, since everyone who buys a ticket pays the same amount to the state. A reduction in state services or a tax increase

would be far more serious threats to the well-being of the people of Texas than any purported "evil" from a lottery.

A lottery would capture Texas money spent on lotteries run by other states and countries. The Louisiana state lottery that started in September will capture revenue from Texas players that should go into Texas state coffers.

A lottery would benefit retailers by drawing customers into stores to buy tickets, creating incidental sales and paying vendors commissions for selling tickets. An increase in retail sales could create jobs. Other economic benefits would accrue to retailers when lottery winners used prize money to purchase goods, services and more lottery tickets.

Lotteries are too passive a game to attract compulsive gamblers, who are drawn to more stimulating games. Besides, if the state prohibited all activities that are abused it would have to outlaw such things such as alcohol, tobacco and credit cards. Lotteries offer a legal, aboveboard alternative to illegal gambling. People will gamble regardless of legality, and state-run lotteries give the government a chance to regulate the games and profit from them. State lotteries have good records for being scandal-free and well-run.

Because players are drawn by different factors when deciding between a lottery ticket or a pari-mutuel bet, a lottery would not provide serious competition for gambling dollars with the pari-mutuel racing industry. The pari-mutuel industry has been operating for almost two years now and should be able to stand on its own feet regardless of any small loss due to a lottery. And even if pari-mutuel betting dollars *were* diverted to a lottery to any great extent, the state would still benefit, since it would keep a larger proportion of lottery wagers than it gets from racing wagers. Moreover, the Legislature recently reduced the tax rate on pari-mutuel winnings and now will collect only a graduated tax based on the level of earnings by the tracks; this tax reduction should more than offset any loss to the racing industry from a lottery.

The law that will implement the lottery (see NOTES) if this amendment is adopted includes some of the toughest restrictions in the country.

HB 52 by Wilson (72nd Legislature, first called session) will ensure that the state runs a clean and fair lottery. The bill prohibits state officers or employees from using the lottery to publicize themselves; prohibits improper influence and lobbying of public officials and political contributions from the lottery industry; prohibits purchasing tickets over the telephone, with credit, through the mail or with food stamps or welfare checks; requires independent audits of lottery accounts, transactions and security; requires demographic studies of lottery players; prohibits granting ticket-sale licenses to persons convicted of felonies or other crimes involving gambling; prohibits granting licenses to pari-mutuel race tracks and those with on-premises alcoholic beverage licenses; requires that odds of winning a prize be printed on tickets and displayed where the tickets are sold; states that advertising should not unduly influence any person to purchase a ticket; and requires research, education and treatment to counter compulsive gambling.

The lottery would not be costly to administer. The implementing legislation, as of September 1, 1993, would cap lottery administrative costs at 15 percent of gross revenues. Administrative costs would come out of lottery-ticket revenue. The Comptroller's Office, the state's revenue collector, has the expertise and resources to oversee a lottery division and ensure the games are run honestly. Independent review of lottery regulations is unnecessary; the comptroller is an elected official who is accountable to the voters, and the implementing legislation requires annual reports on the lottery to the Legislature and the governor.

Allowing the lottery director to determine the amount of lottery prizes would give the director flexibility to structure jackpots to stimulate interest in the games. The director would be authorized to consider factors such as public accessibility to ticket sales and the number of available sales agents in particular areas when granting ticket-sale licenses in order to ensure that ticket outlets are fairly and equitably distributed.

OPPONENTS
SAY:

Establishing a state lottery in Texas would be bad public policy that would carry considerable social and economic costs. Voters should consider the harm that could be done by a state-run gambling operation and should not be swayed by any slick campaign financed by the big corporations that would profit from selling lottery supplies and expertise.

A lottery is an unstable and inefficient source of revenue that would do little to solve the state's fiscal problems. Even the most optimistic estimates show a state lottery would raise only a small fraction of the state's expenses. Creating a lottery would merely obscure the real need for a more equitable tax system and more cost-effective spending of taxpayer dollars.

Lottery revenue is expensive to collect. It can cost as much as 37.5 cents to raise a dollar of lottery revenue. By comparison, most state taxes can be collected for only two or three cents per \$1 of revenue. Conservative estimates of the cost to the Comptroller's Office of administering a state lottery, even if many functions were contracted out to the private sector, are \$189.4 million in fiscal 1992-93 and \$319.4 million in fiscal 1994-95, with costs expected to rise steadily thereafter. The state would have to hire at least 186 new employees.

Lottery revenue is unpredictable and may fluctuate widely from year to year, as public interest waxes and wanes. For example, revenue from the California lottery dropped by 27 percent in the second year of operation. To rekindle public interest in the lottery, states have had to spend more on advertising, promotion and grander prizes. It would be irresponsible to plan to finance state government and critical public services with this uncertain revenue. It took years for pari-mutuel racing to turn any profit for the state, despite being sold to voters with rosy promises of quick and easy revenue.

Public interest in lotteries in general is declining. State income from lotteries declined in seven states in 1990, and in some of the states that had increases, the percentage increase was less than the inflation rate. California, which is used as the basis for many of the projections of a Texas lottery, saw net lottery income drop by 10 percent in 1990.

It is inappropriate for the state to promote gambling and operate a gambling enterprise. Promoting gambling to raise state revenue is the equivalent of the state encouraging alcohol and tobacco consumption in order to collect more from liquor and tobacco taxes. If lottery gambling is justified as public entertainment, why not also establish state-run movie houses or pool halls?

Lotteries undermine the work ethic by promoting a "something for nothing" mentality and cheapen state government in the public eye. The lottery often becomes the most visible and highly publicized activity of the state.

The state should not promote a game most players will lose. A lottery ticket is a bad deal, with the odds against winning often in the millions. The odds of being killed by lightning (1 in 1.9 million) are better than the odds (14 million to 1) of the popular lottery game "pick 6." The state should not acquire revenue by P.T. Barnum's "sucker-born-every-minute" philosophy. The only true winners in a lottery are the companies that supply lottery goods and services.

Numerous studies have shown that lotteries are regressive taxes that take a larger portion of total income from the poor than from the rich. Duke University lottery analysts examined data from seven studies of lottery taxation and concluded that, without exception, the studies revealed that the implicit tax imposed by lotteries is regressive. One well-known report by Daniel Suits found lotteries to be twice as regressive as sales taxes. Regressive taxation works against the aims of programs benefitting low- and moderate-income people.

Lottery advertising is deceptive and uses sophisticated marketing techniques to manipulate the poor and uninformed. Lottery advertisements often target the poor with "get-rich-quick" enticements encouraging betting against improbable odds. Enticing the poor to pay more than their fair share of the state budget would be grossly unfair.

For the state to raise \$462 million in fiscal 1992-93, ticket sales would have to total \$1.263 billion, according to the comptroller's fiscal estimates. This means every man, woman and child in Texas would

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have to spend around \$60 a year on lottery tickets. Because this money would have to come from disposable income currently spent on other items, retail sales or the entertainment industry could suffer, leading to a loss of jobs. In turn, the state would have to pay unemployment benefits to those who lose their jobs, further eroding any revenue gain from a lottery.

Money spent on goods and services, which cycles through the economy many times and raises additional sales tax, would go instead to the lottery. With reduced retail spending, sales tax revenue to the state and local governments would decline — the Comptroller's Office estimates that the state would lose \$39.3 million in sales tax revenue in fiscal 1992-93 and \$83.1 million in fiscal 1994-95 due to the lottery. No new jobs would be created by a lottery because retailers would not need any additional workers to sell tickets along with other merchandise.

Lotteries are dangerous for people susceptible to becoming compulsive gamblers. While most players spend only a small amount on lottery tickets, researchers have found that overall, about 20 percent of the players account for approximately 60 percent of the ticket sales.

Young people often get their first taste of gambling by illegally purchasing lottery tickets. Laws prohibiting sales to minors are rarely enforced, and youths in other states have been seduced into gambling by slick lottery advertisements.

By whetting the public appetite for gambling, the lottery could lead to increased organized crime. A January 1990 analysis by two Indiana University professors of the impact on crime of a state lottery concluded that the adoption of a lottery could be associated with a 3 percent increase in the state crime rate.

The lottery implementing legislation that will take effect if Proposition 11 is approved by the voters does not provide enough oversight or regulation and would result in a poorly run lottery that could be unfair and unethical. Voters should not approve a constitutional amendment allowing a lottery unless the law is specific on

OTHER
OPPONENTS
SAY:

every aspect of the lottery's operation, instead of leaving numerous policy decisions to a bureaucracy.

The implementing bill contains no checks and balances on the comptroller, who would make and enforce lottery rules. The rules should have to be reviewed by an independent source outside the Comptroller's Office and should be subject to public comment.

People who buy lottery tickets should be guaranteed a set percentage of ticket sales to be returned as prizes. The implementing legislation does not contain sufficient oversight of lottery advertising, which should be subject to review by an independent body such as a state ethics commission, to insure that it does not promote the lottery as a way out of economic hardship. The legislation should ensure that all areas of the state have equal access to lottery tickets.

A lottery would increase competition for discretionary income spent at pari-mutuel tracks, which would result in lower profits for race track owners and lower purses for animal owners. The creation of a lottery could reduce wagering at pari-mutuel tracks by 20 percent to 30 percent.

It was irresponsible for the Legislature to include revenue from a lottery in the state budget until the voters decided whether to approve Proposition 11. Alternative revenue sources should have been earmarked to replace speculative revenue from a lottery rather than requiring that state agency budgets be slashed arbitrarily if the lottery is voted down.

NOTES:

HB 54 by Wilson (72nd Legislature, first called session) would establish a state lottery if Proposition 11 is approved by the voters. A division of the Comptroller's Office would be established to operate the lottery. The comptroller would appoint a director of lottery operations who would adopt rules concerning lottery operations, including rules about the types of games, the division of ticket-sales receipts into prizes and state revenue, the price of tickets, the amount of prizes, the frequency of drawings, security for a lottery and advertising. The comptroller would be authorized to contract with private companies or persons for any lottery function. Ticket sales would have to begin no later than the

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240th day after Proposition 11 took effect. (Proposition 11 would take effect when the votes are canvassed — between the 15 and 30 days after the election — so ticket sales would have to begin by around late July or early August of 1992.)

State revenue from the lottery would be deposited in the General Revenue Fund. Under specific conditions, when monthly lottery revenues exceeded the comptroller's estimates, some of the difference would be deposited in a Lottery Stabilization Fund that would be used to make up the difference if lottery revenue fell below estimates. In any month that net lottery revenue exceeded \$10 million and fell below 90 percent of the estimated monthly revenue, the difference between the estimated revenue and actual revenue would be transferred from the Lottery Stabilization Fund to the General Revenue Fund. On the first day of each budget period, half of the Lottery Stabilization Fund would be transferred to the General Revenue Fund.

Transfers from the state lottery account to the Lottery Stabilization Fund could not be made before September 1, 1993; and transfers from the stabilization fund to general revenue could not begin until December 1, 1993.

During each two-year budget period the administrative costs of running the lottery could not exceed 15 percent of the gross ticket sales (20 percent during the first two years of operation). An independent audit of all lottery accounts, transactions and security would have to be conducted each year. It would be illegal to sell a lottery ticket to someone under 18 years old. Video lottery games would be prohibited. Lottery ticket agents would have to be licensed, and persons convicted of felonies or gambling offenses would be prohibited from selling tickets, as would corporations with directors, stockholders or others convicted of such offenses.

HB 1, the General Appropriations Act for fiscal 1992-93, provides in Art. 5, sec. 142 that \$471 million in general revenue to pay for spending in the state budget is contingent on adoption and implementation of a state lottery. Should a state lottery not be adopted, the Legislative Budget Board is to direct the comptroller to reduce agency budgets by

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\$471 million. (The \$471 million figure was based on an earlier estimate of lottery revenue; the comptroller has since estimated lottery revenue for fiscal 1992-93 at \$462 million.)

SUBJECT: Expanding bond authorization for colonias water and sewer projects

BACKGROUND: In 1985 the Legislature adopted a comprehensive state water plan authorizing issuance of general-obligation bonds to finance local projects for water conservation, water development, wastewater facilities, flood control, drainage, subsidence control, aquifer recharge, chloride control and agricultural soil and water conservation. The Texas Water Development Board issues the bonds and administers the programs of financial assistance.

Art. 3, sec. 49 of the Texas Constitution prohibits most forms of state debt, so a constitutional amendment is required to authorize state borrowing by issuing general obligation bonds. Voters have authorized issuance of a total of \$1.88 billion in bonds to implement the 1985 water development plan: in 1985, \$980 million (Art. 3, sec. 49-d-2); in 1987, \$400 million (Art. 3, sec. 49-d-6); in 1989, \$500 million (Art. 3, sec. 49-d-7).

The 1989 constitutional amendment provides that up to 20 percent of the \$500-million issue (\$100 million) may be used to provide subsidized loans and grants for water and sewer systems to economically distressed areas. In 1989 the Legislature authorized financial assistance to economically distressed areas in qualifying counties whose residents cannot pay for sewer and water services. The assistance is directed primarily to unincorporated subdivisions known as "colonias."

Colonias are residential subdivisions usually found in unincorporated areas of counties along the Texas-Mexico border. They often lack sewers, water, electric or gas service and paved roads, even though such services may have been promised to homeowners by the land developer. The improper disposal of raw sewage has led to a high incidence of infectious diseases in these communities. As many as 250,000 people live in Texas colonias, by some estimates.

Using the bond money authorized by the 1989 constitutional amendment, the Texas Water Development Board is purchasing local bonds from qualifying local public agencies to provide funding for water and sewer projects in economically distressed areas. The Water Development Board cannot waive repayment of more than 50 percent of the loan assistance it

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provides to a local agency unless the Department of Health finds a nuisance dangerous to public health.

The Texas Water Development Board has approved funding for preliminary engineering for 13 colonia water and sewer projects and has committed to construction of a project in which the City of Edinburgh will provide water and sewer service for the Lull colonia. The projects being considered will cost about \$100 million to serve an estimated 50,000 people in the colonias.

DIGEST:

Proposition 12 would amend Art. 3, sec. 49-d-7(e) of the Texas Constitution to provide that up to 50 percent (\$250 million), rather than 20 percent (\$100 million), of the \$500 million in water development bonds authorized in 1989 may be issued for subsidized loans and grants for water and sewer projects in economically distressed areas.

The ballot proposal reads: "The constitutional amendment to increase from 20 percent to 50 percent the percentage of Texas water development bonds previously authorized by Texas voters that may be issued for economically distressed areas."

**SUPPORTERS
SAY:**

Proposition 12 would provide much-needed additional assistance for residents in economically distressed areas, specifically the colonias along the Rio Grande border. The \$100 million already obligated for colonia projects will help an estimated 50,000 people, but at least 150,000 more are still desperately in need of basic water and sewer service. Allowing up to \$150 million more to be used for these projects would help finish the job of providing basic services to these areas without detracting from water development in other areas of the state.

No new bond debt would be authorized by Proposition 12. The bonds already have been authorized; this amendment would merely increase the percentage of the bonds that may be earmarked for colonias.

Long-term financing is the most appropriate way to fund water projects because the infrastructure built by these projects will be used for many years to come. Most local water systems are financed by bonds, not appropriations. A water system is expensive to build, and the capital cost

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is usually spread out over several years rather than appropriated all at once and thereby competing for scarce funding with other worthy programs.

Most of the colonias were established by unscrupulous developers preying on low-income residents seeking inexpensive housing. The home buyers have not been provided with the water and sewer service that was promised. Since the areas are outside of cities, it is difficult to enforce minimum sanitation standards and land-use controls.

Texans should be ashamed to allow "Third World" conditions to endanger the health of residents of the state. An estimated 250,000 Texans now live in colonias with inadequate water and sewer facilities. Diseases spread rapidly in these neighborhoods because of the improper disposal of raw sewage. To get to school, some children must walk through raw sewage, which often backs up in water around the houses, and residents sometimes bathe in irrigation ditches contaminated with pesticides. Doctors have noted the frequent incidence of diseases such as tuberculosis, dysentery, encephalitis and hepatitis. Some of these diseases can spread quickly throughout schools and the workplace.

This relatively small additional investment of state money would finance state loans and grants to provide water and wastewater facilities to improve basic living conditions in the colonias. The residents of these areas have tried to solve the problems on their own, but they do not have a large enough property-tax base to support repayment of local bonds issued by municipal utility districts or other local taxing entities.

Colonia residents who receive financial assistance for water improvements are required to pay back as much as they can afford to local units of government, which in turn repay the loans. The residents have an excellent record of paying their debts, but they need a way to finance water and sewer systems in order to raise their living conditions to a level that most people take for granted.

The Water Development Board has determined that this is a good use for these funds; no other more pressing projects would suffer as a result of this proposal. The state board would administer the use of these funds and ensure they were being used for the purpose intended.

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An additional bond authorization is not likely to be needed in the future because the growth of colonias has largely been stopped due to a 1989 law (SB 2) authorizing counties to adopt regulations prohibiting new developments in unincorporated areas and giving the attorney general and the counties the authority to enforce the new rules (the "model rules"). A newer law (SB 1189, enacted during the 1991 regular session), prohibits new development without water and sewer services on tracts of five acres or less (rather than one acre) and allows cities and counties to exempt subdivisions from the "model rules" *only* if the city or county provides the subdivision with water and sewer services that meet the standards in the model rules.

It is short-sighted to insist that water and sewer projects currently planned with the existing bond authorization be completed before more financing is authorized, since the need for potable water is pressing and lack of it presents a serious health risk. The state should have prevented the growth of colonias in the first place by regulating development in unincorporated areas, and it bears responsibility for cleaning up this problem without delay.

The federal government is negotiating a free trade agreement with Mexico, which would have significant economic impact on the border region. It is of vital importance to have adequate infrastructure in these areas in order for Texas to remain competitive. The residents of colonias are hard-working people, an asset to the Texas economy, and Proposition 12 would ensure that most of these communities have an adequate supply of potable water.

OPPONENTS
SAY:

The state cannot afford to add to its soaring debt burden by authorizing general-obligation bonds that would not be self-supporting. The purpose of limiting to 20 percent the proportion of the 1989 bonds used for grants and subsidized loans to distressed areas was to ensure that this program would not create too great a drain on general revenue. The Legislative Budget Office estimates that expanding the authorization for this grant program could result in draws from general revenue of as much as \$215 million over the period of 1995-2020.

Expanding the water-development bond program to provide grants to clean up the colonias would undermine the "pay-as-you-go" nature of the current

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water development program. Recipients of the subsidized loans will not be able to repay the full amount, requiring that more taxpayer dollars be used to make up the difference when the state bonds must be repaid. The Legislative Budget Office assumes that general revenue will have to be used to pay back 75 percent of the debt.

Other water development programs financed with state bond proceeds involve loans to local governmental entities that are repaid with interest, allowing the bond money to be used as a revolving fund; Proposition 12 would allow more bond money to be diverted from these programs. Allowing the colonias program to use up to half of the \$500 million in water-bond revenue authorized in 1989 would only invite another constitutional amendment in the near future seeking even more in water bond authorization to replace the extra bond capacity used by the colonias program.

The colonias are a local problem that should be dealt with locally. Homeowners in these areas should organize municipal utility districts or nonprofit water supply corporations or else find some other means of local financing.

No more money should be authorized for colonia projects until the first projects are completed and their effectiveness can be fully evaluated. In this way subsequent projects can avoid any pitfalls that may be encountered during the first projects. Also, until it can be determined whether or not the construction of new colonias has been stopped by regulations approved in 1989, no more money should be authorized for colonia water and sewer services. Otherwise, unscrupulous developers will continue to build colonias, promising residents that the state will build sewer and water connections.

OTHER
OPPONENTS
SAY:

If an extra \$150 million is needed for colonia projects, it should be provided from current revenue, rather than through borrowing money. The interest paid on these bonds will boost the ultimate cost far beyond the actual cost of the projects.

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NOTES:

SB 1193 by Montford, the implementing legislation for Proposition 12 enacted by the Legislature during the 1991 regular session, authorizes the use of 50 percent rather than 20 percent of the water bonds approved by the voters in 1989 for subsidized loans and grants for water and sewer systems in economically distressed areas. SB 1193 is contingent on approval of Proposition 12.

HB 1, the General Appropriations Act for fiscal 1992-93, prohibits the Texas Water Development Board from issuing and selling bonds for projects in economically distressed areas that would require spending more than \$4 million during the current two-year budget period. The Legislative Budget Office estimated that the increased proportion of the 1989 bonds allowed to be used for colonias projects by Proposition 12 would require no general revenue until fiscal 1995, when \$1.7 million would be needed.

SUBJECT: Authorizing \$300 million in state bonds for student loans

BACKGROUND: The principal method by which the state borrows money is by issuing bonds. General-obligation bonds are backed by the full faith and credit of the state. The state guarantees that it will repay bondholders, with interest, with the first money coming into the Treasury each fiscal year. Because creditors are given these assurances of safety, they generally will accept lower interest payments than on state revenue bonds, which do not pledge the state's full faith and credit.

Since Art. 3, sec. 49 of the Texas Constitution prohibits most forms of state debt, a constitutional amendment is required to authorize the state to issue general-obligation bonds. (Since the state's credit is not pledged to repay revenue bonds, those bonds are not considered state debt and may be authorized by statute.)

Since 1946 Art. 3, sec. 49 has been amended numerous times, to allow bond sales for a variety of purposes. Art. 3, sec. 50b, adopted in 1965, authorized the Legislature to allow the Texas Higher Education Coordinating Board to issue up to \$85 million in general-obligation bonds for loans to Texas residents who attend public or private institutions of higher education in Texas. Another \$200 million for these loans was authorized in 1969, by sec. 50b-1, and an additional \$75 million was authorized in 1989, by sec. 50b-2.

Several student loan programs are administered through the Texas Opportunity Plan Fund by the coordinating board under the umbrella of the Hinson-Hazlewood College Student Loan Program. The Hinson-Hazlewood program offers federally guaranteed student loans backed by the U.S. Department of Education, supplemental loans made primarily to students without family financial support whose need exceeds what they can borrow under the guaranteed loan programs, health education assistance loans (some backed by the U.S. Department of Health and Human Services) and College Access Loans, which are made primarily to middle-income students.

To qualify for the loan programs, students must be Texas residents or eligible to pay in-state tuition and, except for the College Access Loans,

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must be financially needy. In fiscal 1990 about 26,000 students received about \$81 million in loans. All loans are guaranteed by the federal government, the state or a co-signer.

During its 1991 regular session the Legislature proposed to voters a constitutional amendment authorizing the Legislature to allow the coordinating board to issue up to \$300 million in general-obligation bonds to finance educational loans to college and university students. The ballot proposal read: "The constitutional amendment providing for the issuance of general obligation bonds to provide educational loans to students." The proposition was rejected by the voters at the August 10, 1991 election by 433,116 in favor (49.6 percent), 440,763 against (50.4 percent) at the August 10, 1991 election.

DIGEST:

Proposition 13 would add sec. 50b-3 to the Constitution, authorizing the Legislature to allow the Texas Higher Education Coordinating Board to issue up to \$300 million in general-obligation bonds to finance educational loans to college and university students.

The maximum interest rate would be set by law. An interest and sinking fund would be established to pay the principal and interest due on the bonds. The Legislature could provide for the investment of bond proceeds and the interest and sinking fund.

The ballot proposal reads: "The constitutional amendment providing for the issuance of general obligation bonds not to exceed \$300,000,000 to continue existing programs to provide educational loans to students, with repayments of student loans applied toward retirement of the bonds."

**SUPPORTERS
SAY:**

The \$300 million general-obligation bond sale proposed by Proposition 13 would allow the Texas Higher Education Coordinating Board to meet the growing demand for student loans to financially needy students at a lower cost than it otherwise could. The state has used general-obligation bonds to make self-supporting student loans since 1965, and the program has an excellent record. It serves about 26,000 students a year who might otherwise be unable to attend college. Hinson-Hazlewood loans are especially helpful to financially pressed students because the interest rate

students pay is generally 1 to 4 percentage points below that charged by commercial lenders for student loans.

Lack of information and misunderstanding concerning the state's student-loan program led to defeat at the polls in August of this much-needed bond issue. Voters perhaps confused the Hinson-Hazlewood programs with the federal student loan program, which has a much higher default rate, and may have mistakenly believed that approval of the amendment would result in a tax hike or other cost to the state.

Unlike state bonds for financing prisons or the superconducting super collider, student loan bonds are "self-supporting" — they are paid back, with interest, by borrowers, *not* by state taxpayers. The default rate on Hinson-Hazlewood loans is low, about 6 percent, compared to a default rate of about 16 percent on loans in the federal program. Almost all of the coordinating board's student loans are insured by the federal government, so repayment is assured even if students default on payments. The few loans not guaranteed by the federal government or the state have a co-signer who can be held responsible for the loan if the student defaults.

The Hinson-Hazlewood program operated for 11 years as a revolving, self-supporting fund, with loan repayments, plus interest, used to retire bonds and to provide new loans. But because the demand for loans has increased dramatically in recent years and most of the numerous loans made in recent years are not yet due, the loan fund has not been replenished with loan payments. The bonds issued under this amendment would help fund the program until payments on recent loans come due.

In January 1991 the coordinating board sold \$25 million in general-obligation bonds, exhausting its current general-obligation bond authority. If voters approve this amendment, the board could continue its loan program for at least three years with less expense. Current law (SB 104 by Barrientos, regular session) will limit bond sales to \$100 million a year, enough to cover current annual demand of \$80 million, plus an anticipated \$20-million increase in loan requests.

General-obligation bonds cost the state less than revenue bonds, which the coordinating board also can use to finance student loans. General-

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obligation bonds are guaranteed by the state, making them a secure investment that is attractive to buyers. This allows the state to offer buyers less interest than it offers on revenue bonds, which are not backed by the full faith and credit of the state. The Legislature authorized the coordinating board (in HB 686 by Cavazos, regular session) to issue up to \$75 million a year in revenue bonds for student loans. In July 1991 the board sold its first \$75 million in revenue bonds for loans. The board estimates that it will run out of loan funds from the July issue by April 1, 1992.

The coordinating board estimates that in the long term it costs the program an additional \$25 to \$30 million to issue \$100 million in revenue bonds than to issue \$100 million in general-obligation bonds. The higher cost of revenue bonds is borne by students who must pay higher interest rates on their loans. Under the law the coordinating board could not issue additional, more expensive, revenue bonds if voters approve general-obligation bonds.

The bonds that would be authorized by Proposition 13 would be even more attractive to buyers than college-loan bonds sold in the past. SB 103 by Barrientos, regular session, allows the coordinating board to issue the college bonds as part of the limited amount of "private activity" bonds that the federal government allows the state to issue annually. Although the bonds proceeds are used for private purposes, the interest income the bonds pay to investors is tax exempt, an advantage that allows the state to pay lower interest and still attract buyers.

Changes in federal financial aid programs and the 1987 creation of the College Access Loan Program (designed to give students from middle-class families loans for college educations) have caused the demand for Hinson-Hazlewood loans to increase from \$12 million in 1986 to about \$80 million in 1990. These factors, along with the increasing cost of a college education and increasing numbers of students, will cause the demand for Hinson-Hazlewood loans to continue to increase.

College Access Loans were suspended in September 1990 because of a shortage of funds. The program was reinstated in September 1991 but could be discontinued again if funds dry up. This loan program is

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important to many middle-class families who face high college costs but are ineligible for guaranteed student loans. The bonds that would be authorized by Proposition 13 would be used to continue the College Access Loan program.

**OPPONENTS
SAY:**

The voters rejected a proposed constitutional amendment identical to Proposition 13 at the August 10 election. By submitting the same amendment again so soon after its rejection, the Legislature mistakenly assumes that the voters did not know what they were doing.

The state should not sink further into debt. As of May 31, 1991 the state bond debt totaled \$7.7 billion, of which \$3.0 billion was in general obligation bonds. This is up from \$2.7 billion in general-obligation bond debt at the end of fiscal 1990 and \$2.3 billion at the end of fiscal 1989. Another \$3.0 billion in general-obligation bond authority has been approved, but the bonds have not yet been issued.

Any new debt-creating measure needs to be examined in view of overall governmental debt in the state. Although Texas ranks 49th among states in terms of state debt per capita, the state ranks 18th among states in total government debt per capita when debt carried by local governmental agencies also is considered. Of the 10 largest states, Texas has the highest local debt burden. The Legislature needs a comprehensive evaluation of the state's debt structure and its future before more new debt is authorized.

The Legislative Budget Board estimates that annual debt service on \$300 million in bonds would be approximately \$28.5 million. Borrowing money by issuing bonds will eventually cost the state twice as much as the initial bond issue once all the interest costs are factored in. Even though student loan repayments would be used to retire the bonds, the state should not rush into further debt.

**OTHER
OPPONENTS
SAY:**

Although the cost of revenue bonds is somewhat higher than that of general-obligation bonds, the revenue bonds already authorized by law should be sufficient to raise the money necessary to keep the student loan program afloat without amending the Constitution to increase the state's general-obligation bond debt.