

## **BILL ANALYSIS**

C.S.H.B. 4209  
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Investments & Financial Services  
Committee Report (Substituted)

### **BACKGROUND AND PURPOSE**

Interested parties contend that legislation is needed to align the state's permissive investment strategies for political subdivisions under the state Public Funds Investment Act with rules promulgated by the federal Securities and Exchange Commission (SEC). The parties note that the SEC's rules will not be finalized until next summer but assert that legislation will ensure that political subdivisions are provided flexibility in allowable investments. Without this change to the Public Funds Investment Act, the parties maintain that municipalities and other political subdivisions will be constrained to only a few investment opportunities outside of the state-run TexPool. C.S.H.B. 4209 seeks to address this issue.

### **CRIMINAL JUSTICE IMPACT**

It is the committee's opinion that this bill does not expressly create a criminal offense, increase the punishment for an existing criminal offense or category of offenses, or change the eligibility of a person for community supervision, parole, or mandatory supervision.

### **RULEMAKING AUTHORITY**

It is the committee's opinion that this bill does not expressly grant any additional rulemaking authority to a state officer, department, agency, or institution.

### **ANALYSIS**

C.S.H.B. 4209 amends the Government Code to designate interest-bearing banking deposits that are guaranteed or insured by the Federal Deposit Insurance Corporation or its successor or the National Credit Union Share Insurance Fund or its successor as authorized investments for a governmental entity under the Public Funds Investment Act. The bill designates an investment in certain negotiable certificates of deposit issued by a bank that has a certificate of deposit rating of at least 1 or the equivalent by a nationally recognized credit rating agency, or that is associated with a holding company having a commercial paper rating of at least A-1, P-1, or the equivalent by a nationally recognized credit rating agency as an authorized investment for a governmental entity under the act.

C.S.H.B. 4209 revises the conditions under which a no-load money market mutual fund is considered to be an authorized investment for a governmental entity under the act by removing the condition that the mutual fund have a dollar weighted average stated maturity of 90 days or fewer, adding the condition that the mutual fund comply with federal Securities and Exchange Commission Rule 2a-7 promulgated under the federal Investment Company Act of 1940, removing the specification that the mutual fund include in its investment objectives the maintenance of stable net asset value of \$1 for each share, and instead requiring the mutual fund to include in its investment objectives the maintenance of net asset value shares determined in accordance with federal Securities and Exchange Commission Rule 2a-7.

C.S.H.B. 4209 makes an issuer's authority to agree to waive sovereign immunity from suit or liability in proceedings to authorize obligations or a credit agreement, or in a credit agreement, for the purpose of adjudicating a claim to enforce the credit agreement or obligation or for damages for breach of the credit agreement or obligation, applicable to the execution of a guaranteed investment contract and a guaranteed repurchase agreement by an investing entity.

C.S.H.B. 4209 includes a public funds investment pool's policy regarding holding deposits in cash among the minimum information to be included in an offering circular or other similar disclosure instrument the investment pool is required to furnish to the investment officer or other authorized representative of the governmental entity, for purposes of eligibility to receive funds from and invest funds on behalf of a governmental entity under the act.

C.S.H.B. 4209 removes the requirement that portfolio holdings of an investment pool created to function as a money market mutual fund, if the ratio of the market value of the portfolio divided by the book value of the portfolio is less than 0.995 or greater than 1.005, be sold as necessary to maintain the ratio between 0.995 and 1.005 and instead requires the governing body of such a public funds investment pool, if the ratio is less than 0.995 or greater than 1.005, to take action as the body determines necessary to eliminate or reduce any dilution or unfair result to existing participants, including the sale of portfolio holdings, to attempt to maintain the ratio between 0.995 and 1.005.

C.S.H.B. 4209 removes the requirement that a public funds investment pool, for purposes of eligibility as an authorized investment for a governmental entity under the act, be continuously rated no lower than AAA or AAA-m or at an equivalent rating by at least one nationally recognized rating service and instead requires such a public funds investment pool to be continuously rated no lower than the highest liquidity rating given to U.S. Treasury obligations by at least one nationally recognized rating service.

C.S.H.B. 4209 authorizes the governing body of an eligible entity, defined by the bill as a state agency or political subdivision designated as an issuer under statutory provisions governing obligations for certain public improvements, to enter into hedging contracts and related security and insurance agreements related to commodities investments used in the general operations of an eligible entity or used in connection with the acquisition or construction of a capital project by the eligible entity. The bill requires a hedging transaction to comply with the regulations of the federal Commodity Futures Trading Commission and the federal Securities and Exchange Commission. The bill authorizes an eligible entity to credit any amount the entity receives under a hedging contract or agreement against expenses associated with a commodity purchase. The bill authorizes an eligible entity's payment under a hedging contract to be considered an operation and maintenance expense, an acquisition expense, or a construction expense of the eligible entity. The bill requires the governing body of an eligible entity to establish its policy regarding hedging transactions and establishes that its provisions relating to hedging prevail if there is a conflict with the eligible entity's municipal charter, if applicable.

#### **EFFECTIVE DATE**

On passage, or, if the bill does not receive the necessary vote, September 1, 2015.

#### **COMPARISON OF ORIGINAL AND SUBSTITUTE**

While C.S.H.B. 4209 may differ from the original in minor or nonsubstantive ways, the following comparison is organized and formatted in a manner that indicates the substantial differences between the introduced and committee substitute versions of the bill.

INTRODUCED

SECTION 1. Subsection (a) of Section 2256.010, Government Code, is amended by deleting "and" at the end of clause (5), changing the period at the end of clause (6) to "; and", and adding a new clause (7), to read as follows:

"(7) interest-bearing banking deposits that are guaranteed or insured by the Federal Deposit Insurance Corporation or its successor or the National Credit Union Share Insurance Fund or its successor."

SECTION 2. Section 2256.010, Government Code, is amended by adding a new subsection (c), to read as follows:

"(c) In addition to the authority to invest funds in certificates of deposit under Subsections (a) and (b), an investment in certificates of deposit made in accordance with Section 2256.020(2) is an authorized investment under this section."

HOUSE COMMITTEE SUBSTITUTE

SECTION 1. Section 2256.009(a), Government Code, is amended to read as follows:

(a) Except as provided by Subsection (b), the following are authorized investments under this subchapter:

(1) obligations, including letters of credit, of the United States or its agencies and instrumentalities;

(2) direct obligations of this state or its agencies and instrumentalities;

(3) collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States;

(4) other obligations, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, this state or the United States or their respective agencies and instrumentalities, including obligations that are fully guaranteed or insured by the Federal Deposit Insurance Corporation or by the explicit full faith and credit of the United States;

(5) obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent; ~~and~~

(6) bonds issued, assumed, or guaranteed by the State of Israel; and

(7) interest-bearing banking deposits that are guaranteed or insured by:

(A) the Federal Deposit Insurance Corporation or its successor; or

(B) the National Credit Union Share Insurance Fund or its successor.

SECTION 2. Section 2256.010, Government Code, is amended by adding Subsection (c) to read as follows:

(c) An investment in negotiable certificates of deposit issued by a bank that has a certificate of deposit rating of at least 1 or the equivalent by a nationally recognized credit rating agency, or that is associated with a holding company having a commercial paper rating of at least A-1, P-1, or the equivalent by a nationally recognized credit rating agency, is an authorized

No equivalent provision. (But see SECTION 5 below.)

SECTION 3. Subsection (a), Clause (4), Section 2256.014, Government Code, is amended to read as follows:

(3) complies with Rule 2a-7, promulgated by the United States Securities and Exchange Commission ~~has a dollar weighted average stated maturity of 90 days or fewer;~~ and

(4) includes in its investment objectives the maintenance of ~~stable~~ net asset value ~~of \$1 for each~~ shares determined in accordance with Rule 2a-7, promulgated by the United States Securities and Exchange Commission.

SECTION 4. Subsection (c), Clause (2), Section 2256.015, Government Code, is amended to read as follows:

"(2) the entity must receive bids from at least two [~~three~~] separate providers with no material financial interest in the bonds from which proceeds were received;"

No equivalent provision. (But see SECTION 6 below.)

investment under this subchapter.

SECTION 3. Section 2256.011, Government Code, is amended by adding Subsection (e) to read as follows:

(e) Section 1371.059(c) applies to the execution of a repurchase agreement by an investing entity.

SECTION 4. Section 2256.014(a), Government Code, is amended to read as follows:

(a) A no-load money market mutual fund is an authorized investment under this subchapter if the mutual fund:

(1) is registered with and regulated by the Securities and Exchange Commission;

(2) provides the investing entity with a prospectus and other information required by the Securities Exchange Act of 1934 (15 U.S.C. Section 78a et seq.) or the Investment Company Act of 1940 (15 U.S.C. Section 80a-1 et seq.);

(3) complies with federal Securities and Exchange Commission Rule 2a-7 (17 C.F.R. Section 270.2a-7), promulgated under the Investment Company Act of 1940 (15 U.S.C. Section 80a-1 et seq.) ~~[has a dollar weighted average stated maturity of 90 days or fewer];~~ and

(4) includes in its investment objectives the maintenance of a [~~stable~~] net asset value determined in accordance with federal Securities and Exchange Commission Rule 2a-7 (17 C.F.R. Section 270.2a-7), promulgated under the Investment Company Act of 1940 (15 U.S.C. Section 80a-1 et seq.) [~~of \$1 for each share~~].

No equivalent provision.

SECTION 5. Section 2256.015, Government Code, is amended by adding Subsection (d) to read as follows:

(d) Section 1371.059(c) applies to the execution of a guaranteed investment contract by an investing entity.

SECTION 5. Section 2256.011, Government Code, is amended by adding a new subsection (e), to read as follows:

"(e) The repurchase agreement may provide that the investing entity may agree to waive sovereign immunity from suit or liability for the purpose of adjudicating a claim to enforce the repurchase agreement or for damages for breach of the repurchase agreement."

SECTION 6. Section 2256.015, Government Code, is amended by adding a new subsection (d), to read as follows:

"(d) The guaranteed investment contract may provide that the investing entity may agree to waive sovereign immunity from suit or liability for the purpose of adjudicating a claim to enforce the guaranteed investment contract or for damages for breach of the guaranteed investment contract."

SECTION 7. Subsection (b), Section 2256.016, Government Code, is amended to renumber current subsections (6) through (12) as subsections (7) through (13), and to add a new clause (6), to read as follows:

No equivalent provision. (*But see SECTION 3 above.*)

No equivalent provision. (*But see SECTION 5 above.*)

SECTION 6. Sections 2256.016(b), (f), and (h), Government Code, are amended to read as follows:

(b) To be eligible to receive funds from and invest funds on behalf of an entity under this chapter, an investment pool must furnish to the investment officer or other authorized representative of the entity an offering circular or other similar disclosure instrument that contains, at a minimum, the following information:

- (1) the types of investments in which money is allowed to be invested;
- (2) the maximum average dollar-weighted maturity allowed, based on the stated maturity date, of the pool;
- (3) the maximum stated maturity date any investment security within the portfolio has;
- (4) the objectives of the pool;
- (5) the size of the pool;
- (6) the names of the members of the advisory board of the pool and the dates their terms expire;
- (7) the custodian bank that will safekeep the pool's assets;
- (8) whether the intent of the pool is to maintain a net asset value of one dollar and the risk of market price fluctuation;
- (9) whether the only source of payment is the assets of the pool at market value or whether there is a secondary source of payment, such as insurance or guarantees,

"(6) its policy as to holding deposits in cash:"

SECTION 8. Subsections (f) and (h), Section 2256.016, Government Code, are amended to read as follows:

"(f) To be eligible to receive funds from and invest funds on behalf of an entity under this chapter, a public funds investment pool ~~created to function as a money market mutual fund~~ must mark its portfolio to market daily, and, to the extent reasonably possible, stabilize at a \$1 net asset value. If the ratio of the market value of the portfolio divided by the book value of the portfolio is less than 0.995 or greater than 1.005, the governing body of the public funds investment pool shall take such action as it may determine is necessary to eliminate or reduce to the extent reasonably practicable any dilution or unfair results to existing participants, including the sale of portfolio holdings [shall be sold as necessary] to attempt to maintain the ratio between 0.995 and 1.005."

"(h) To maintain eligibility to receive funds from and invest funds on behalf of an entity under this chapter, an investment pool must be continuously rated no lower than the highest liquidity rating given to United States Treasury obligations [AAA or AAA-m or at an equivalent rating] by at least one nationally recognized rating service."

and a description of the secondary source of payment;

(10) the name and address of the independent auditor of the pool;

(11) the requirements to be satisfied for an entity to deposit funds in and withdraw funds from the pool and any deadlines or other operating policies required for the entity to invest funds in and withdraw funds from the pool; ~~and~~

(12) the performance history of the pool, including yield, average dollar-weighted maturities, and expense ratios; and

(13) the pool's policy regarding holding deposits in cash.

(f) To be eligible to receive funds from and invest funds on behalf of an entity under this chapter, a public funds investment pool created to function as a money market mutual fund must mark its portfolio to market daily, and, to the extent reasonably possible, stabilize at a \$1 net asset value. If the ratio of the market value of the portfolio divided by the book value of the portfolio is less than 0.995 or greater than 1.005, the governing body of the public funds investment pool shall take action as the body determines necessary to eliminate or reduce any dilution or unfair result to existing participants, including a sale of portfolio holdings to attempt [shall be sold as necessary] to maintain the ratio between 0.995 and 1.005. In addition to the requirements of its investment policy and any other forms of reporting, a public funds investment pool created to function as a money market mutual fund shall report yield to its investors in accordance with regulations of the federal Securities and Exchange Commission applicable to reporting by money market funds.

(h) To maintain eligibility to receive funds from and invest funds on behalf of an entity under this chapter, an investment pool must be continuously rated no lower than the highest liquidity rating given to United States Treasury obligations [AAA or AAA-m or at an equivalent rating] by at least one nationally recognized rating service.

SECTION 9. Section 2256.019, Government Code, is amended to read as follows:

"A public funds investment pool must be continuously rated no lower than the highest liquidity rating given to United States Treasury obligations [AAA or AAA m or at an equivalent rating] by at least one nationally recognized rating service."

SECTION 10. Chapter 2256, Government Code, is amended by adding a new section 2256.02015, to read as follows:

"Sec. 2256.02015. Authorized Investments: Eligible Entities.

(a) An eligible entity may enter into hedging contracts, and related security and insurance agreements, to protect against economic loss related to price fluctuations of commodities used in the general operations of the eligible entity or used in connection with the acquisition or construction of capital projects by the eligible entity. A hedging transaction must comply with the regulations of the Commodity Futures Trading Commission and the Securities and Exchange Commission.

If there is a conflict between the municipal charter of the eligible entity and this chapter, this chapter prevails.

(b) A payment by an eligible entity under a hedging contract may be considered: (i) an operation and maintenance expense of the eligible entity; (ii) an acquisition expense of the eligible entity; or (iii) a construction expense of the eligible entity.

The eligible entity may credit any amount it receives under the contract or agreement against expenses associated with commodity purchases.

(c) The governing body of the eligible entity may set policy regarding hedging transactions.

(d) As used in this section:

SECTION 7. Section 2256.019, Government Code, is amended to read as follows:

Sec. 2256.019. RATING OF CERTAIN INVESTMENT POOLS. A public funds investment pool must be continuously rated no lower than the highest liquidity rating given to United States Treasury obligations [AAA or AAA m or at an equivalent rating] by at least one nationally recognized rating service.

SECTION 8. Subchapter A, Chapter 2256, Government Code, is amended by adding Section 2256.0206 to read as follows:

Sec. 2256.0206. AUTHORIZED INVESTMENTS: HEDGING TRANSACTIONS.

(d) An eligible entity may enter into hedging contracts and related security and insurance agreements related to commodities investments used in the general operations of an eligible entity or used in connection with the acquisition or construction of a capital project by the eligible entity. A hedging transaction must comply with the regulations of the federal Commodity Futures Trading Commission and the federal Securities and Exchange Commission.

(b) This section prevails to the extent of any conflict between this section and an eligible entity's municipal charter, if applicable.

(f) An eligible entity's payment under a hedging contract or agreement may be considered to be:

- (1) an operation and maintenance expense of the eligible entity;
- (2) an acquisition expense of the eligible entity; or
- (3) a construction expense of the eligible entity.

(e) An eligible entity may credit any amount the entity receives under a hedging contract or agreement against expenses associated with a commodity purchase.

(c) The governing body of an eligible entity shall establish its policy regarding hedging transactions.

(a) In this section:

(1) "Eligible entity" means those state agencies and political subdivisions described in Section 1371.001(4), Government Code; and

(2) "Hedging" means entering into an offsetting position in a related security or using a financial agreement as a protection against loss due to price fluctuation."

No equivalent provision.

SECTION 11. This Act takes effect immediately if it receives a vote of two-thirds of all the members elected to each house, as provided by Section 39, Article III, Texas Constitution. If this Act does not receive the vote necessary for immediate effect, this Act takes effect September 1, 2015.

(1) "Eligible entity" means a state agency or political subdivision that is an issuer as defined by Section 1371.001.

(2) "Hedging" means acting to protect against economic loss due to price fluctuation of an investment by entering into an offsetting position in a related security or by using a financial agreement.

SECTION 9. The changes in law made by this Act apply only to authorized investments of public funds governed by Chapter 2256, Government Code, as amended by this Act, that are made on or after the effective date of this Act. An authorized investment of public funds made before the effective date of this Act is governed by the law in effect immediately before that date, and that law is continued in effect for that purpose.

SECTION 10. Same as introduced version.