# Texas Permanent School Fund Primer

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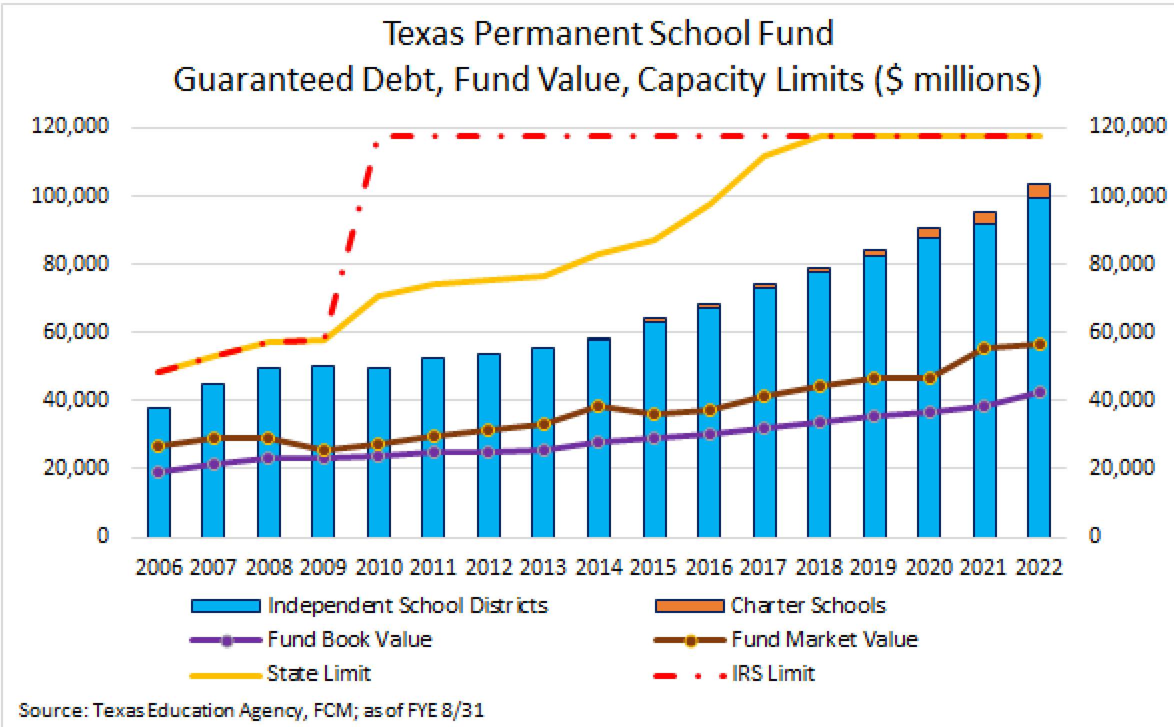
The Texas Permanent School Fund (PSF) was created with a $2,000,000 appropriation by the Texas Legislature in 1854 expressly for the benefit of the public schools of Texas. The Constitution of 1876 stipulated that certain lands and all proceeds from the sale of these lands should also constitute the PSF. Additional acts later gave more public domain land and rights to the PSF. Since its initial capitalization, the PSF has grown to a net market value of $56.7 billion as of December 31, 2022. As of that date, approximately 28% of the total amount of outstanding debt with a CUSIP issued in the State of Texas was PSF-guaranteed. The following points may be of interest to investors in evaluating the credit support provided by the PSF.

- The PSF serves Texas school districts by providing funding for education and guaranteeing debt issued by independent school districts (ISDs) and charter schools that meet program standards.
- The guaranteed bonds of ISDs are unlimited general obligation securities that are secured in the first instance by an annual property tax levied without legal limit against all taxable property within a district.
- Since the approval of a state constitutional amendment in 1983, which allowed the PSF to guarantee debt, there has never been any call on the guarantee because of the high credit quality of Texas school districts, the fund's credit quality parameters, and the state's strong oversight policies.
- The fund was created with a $2 million appropriation by the Texas Legislature in 1854 and had grown to $60.9 billion in gross market value of assets as of FYE 2022. PSF is made up of a diverse mix of assets, and as of FYE 2022 included a largely liquid $46.8 billion portion managed by the State Board of Education (SBOE) and a largely illiquid $14.2 billion portion managed by the School Land Board (SLB).
- The largely liquid portion of the fund provided significant resources relative to guaranteed debt, but did include potentially volatile equities, which represented 27.1% of total gross assets, and alternative investments, which accounted for another 27.4% of gross assets.
- The largely illiquid assets consist of real estate investments, sovereign and other lands, and mineral interests. While largely illiquid, these assets have been considerably more stable and generate income primarily through mineral leases and royalties.
- In addition to providing a guarantee on debt issued by local school districts, the PSF disperses funds from the SBOE portion of the fund to support school district operations. The amount of disbursements is limited by two tests: 1) distributions may not exceed 6% of the average market value of the fund, excluding real property, on the last day of each of the sixteen state fiscal quarters ending in the November before the regular legislative session begins, and 2) on a 10 year rolling average basis, 10 year distributions may not exceed 10 year total return (excluding income from the SLB portion of the fund); the SBOE portion of the fund disbursed $1.7 billion in fiscal 2022.

- A constitutional amendment approved by voters in 2019 permits the SLB to disburse up to $600 million directly per year to support school district operations; the SLB's direct contribution was $415 million in fiscal 2022.
- The PSF is limited by an IRS ruling that requires the amount of guaranteed debt to not exceed 5 times the book value of PSF assets as of December 16, 2009. The state also imposes a cap that the legislature has changed from time to time, and which stood at 3.5 times at FYE 2022. Due to growth of the fund since 2009, the guarantee capacity is currently capped by the IRS limit unless the IRS revisits the ruling, a change that could require a multi-year process. The state may increase the capacity of the program up to the IRS limit if it does not prevent the guarantee from maintaining the highest available credit ratings, according to PSF policy.
- Additionally, state law allows for and the PSF has elected to reserve 5% of capacity as determined above from use in guaranteeing bonds. As of December 31, 2022, guaranteed debt exhausted 95.8% of the IRS-imposed cap less the 5% reserve.
- The amount of charter school capacity is limited to the percentage of charter enrollment as a percent of statewide enrollment, which was 7.0% for the 2021-22 school year. As of December 31, 2022, the program guaranteed charter school debt totaling $3.9 billion, or 3.7% of total PSF-guaranteed debt.
- To obtain a PSF guarantee, school districts must apply and meet certain criteria, as described in the Texas Education Code. The code requires that school districts notify the PSF five days before a debt service payment if the district expects to be unable to satisfy the payment, and PSF is required to advance funds "immediately upon notice" directly to the paying agent. Once the PSF advances funds on behalf of a district, the code requires the first state monies payable to the district be intercepted to reimburse the PSF.
- The Commissioner of Education can order a school district to set a tax rate capable of reimbursing the PSF and pay future debt service, appoint a new board of managers, or merge a distressed district into another district. If repeated defaults occur, the Commissioner may request the Attorney General to institute appropriate legal action to ensure reimbursement.
- The PSF guarantee has never been tapped as the state has strong oversight of school districts and the PSF program reviews individual audits to ensure districts are financially sound. The PSF guarantee remains in place for the life of the bonds independent of whether the ISD remains in existence. Equally, the guarantee for charter school debt remains in place for the life of the bonds independent of whether the school's charter remains in force.
- The size, diversity and credit quality of the underlying school districts' general obligation debt are important credit considerations for the PSF's Aaa/AAA/AAA credit ratings.
- As of December 31, 2022, the PSF guaranteed $106.4 billion in outstanding debt. And at FYE 2022 the guarantee covered the bonds of 867 Texas ISDs and 31 charter schools. The weighted average credit quality of guaranteed districts was Aa3/AA-, and the top 10 participants, representing 20.5% of outstanding par, had a median rating of Aa1/AA+.
- State aid as a share of general fund revenue was approximately 30% for the ten largest districts, providing access to substantial divertible resources to reimburse the PSF in case of a default.




| 10 Largest Total Debt Outstanding Guaranteed Under the Program at August 31, 2022 | | | | |
|---|---|---|---|---|
| District Name | Moody's/S&P Rating | Moody's/S&P Outlooks | Balance | Percent of Total PSF Guaranteed Debt |
| Dallas ISD | Aa1/AA+ | stable/stable | $3,264,160,000 | 3.16% |
| Cypress-Fairbanks ISD | Aa1/AA | stable/stable | $3,081,345,000 | 2.98% |
| Northside ISD (Bexar) | Aa1/AA+ | stable/stable | $2,299,690,000 | 2.23% |
| Frisco ISD | Aa1/AA+ | stable/stable | $2,247,740,227 | 2.18% |
| Katy ISD | Aa1/AA | stable/stable | $2,114,761,367 | 2.05% |
| Houston ISD | Aaa/AA+ | stable/stable | $1,847,190,000 | 1.79% |
| Lamar CISD | Aa3/AA | stable/negative | $1,705,940,000 | 1.65% |
| Conroe ISD | Aa1/AA+ | stable/stable | $1,600,365,000 | 1.55% |
| Fort Bend ISD | NR/AA+ | stable | $1,536,300,000 | 1.49% |
| San Antonio ISD | Aa2/AA | stable/negative | $1,488,519,988 | 1.44% |

Source: Texas Education Agency, Bloomberg Finance LLP, FCM; as of August 31, 2022

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