Creating funds to assist in the financing of priority projects in the state water plan

6
Proposition

SJR 1 by Williams (Pitts, Ritter)

Background

The state water plan is designed to meet water needs during times of drought. Its purpose is to ensure that cities, rural communities, farms, ranches, businesses, and industries have enough water during a repeat of 1950s drought conditions. In Texas, each of 16 regional water-planning groups is responsible for creating a 50-year regional plan and refining it every five years so conditions can be monitored and assumptions reassessed. The Texas Water Development Board (TWDB) uses information from regional plans to develop the state plan, which includes policy recommendations to the Legislature.

The 2012 state water plan includes the cost of water management strategies and estimates of state financial assistance required to implement them. Regional water-planning groups recommended water management strategies that would account for another 9 million acre-feet of water (an acre-foot of water is 325,851 gallons) by 2060 if all strategies were implemented, including 562 unique water supply projects. About 34 percent of the water would come from conservation and reuse, about 17 percent from new major reservoirs, about 34 percent from other surface water supplies, and about 15 percent from various other sources.

Among TWDB's recommendations to the Legislature to facilitate implementation of the 2012 state water plan is the development of a long-term, affordable, and sustainable method to provide financing assistance to implement water supply projects.

Existing state funding for water management strategies within the state water plan relies primarily on general obligation bond issuances that finance loans to local and regional water suppliers. On November 8, 2011, voters approved a constitutional amendment (Prop. 2) authorizing additional general obligation bond authority not to exceed $6 billion at any time. With this authority, the TWDB may issue additional bonds through ongoing bond authority, allowing it to offer access to financing on a long-term basis. Bonds issued by the TWDB are either self-supporting, with debt service that is met through loan repayments, or non-self-supporting, which requires general revenue to assist with debt service payments, as directed by the Legislature through the appropriations process.

Digest

Prop. 6 would amend the Texas Constitution to create the State Water Implementation Fund for Texas (SWIFT) and the State Water Implementation Revenue Fund for Texas (SWIRFT) as special funds in the state treasury outside the general revenue fund.

Money in the funds would be administered, without further appropriation, by the Texas Water Development Board (TWDB) for the purpose of implementing the state water plan, with oversight by the Legislative Budget Board.

Money in the funds and any money appropriated from the Economic Stabilization Fund, also known as the "Rainy Day Fund," would be dedicated for the purpose of complying with constitutional provisions that exempt constitutionally dedicated funds from counting toward the spending cap.

The SWIFT and the SWIRFT would consist of:

- money transferred or deposited by law to the credit of the funds, including money from any source transferred or deposited at the TWDB's discretion;
- the proceeds of any state fee or tax that by statute was dedicated for deposit to the credit of the funds;
- any other revenue that the Legislature by statute dedicated for deposit to the credit of the funds; and
- investment earnings and interest earned on amounts credited to the funds.

In addition, money would be transferred to the SWIFT under a bond enhancement agreement, and proceeds from the sale of bonds, including revenue bonds, would provide money for the SWIRFT. The SWIRFT also would consist of money disbursed to the fund from the SWIFT.

The Legislature, by general law, could allow the TWDB to enter into bond enhancement agreements to provide additional security for general obligation bonds or revenue bonds, the proceeds of which would be used to finance state water plan projects. The TWDB could also provide direct loans for water projects in the state water plan.

The Legislature, by general law, could allow the TWDB to issue bonds and enter into related credit agreements payable from all revenues available to the SWIRFT.

Any bond enhancement agreements or obligations would have to be payable solely from the SWIFT or from amounts in the SWIRFT and would not be constitutional state debt payable from the general revenue of the state.

The TWDB would be required to set aside amounts sufficient to make payments that became due that fiscal year.

A statement of legislative intent in Prop. 6 holds that the proposed amendment is intended only to establish a basic framework and not to be a comprehensive treatment of the SWIFT or the SWIRFT. The Legislature would have full power to delegate duties, responsibilities, functions, and authority to the TWDB as necessary.

The ballot proposal reads: "The constitutional amendment providing for the creation of the State Water Implementation Fund for Texas and the State Water Implementation Revenue Fund for Texas to assist in the financing of priority projects in the state water plan to ensure the availability of adequate water resources."

Supporters say

Prop. 6 would constitutionally create two funds for the implementation of water projects in the state water plan. It would work together with two bills recently enacted by the 83rd Legislature — HB 4 by Ritter and HB 1025 by Pitts. HB 4, the enabling legislation, contains the mechanics of the funds, including the prioritization of projects that would receive funding. HB 1025 would make the appropriation from the Rainy Day Fund for the initial capitalization of the SWIFT, contingent on voter approval of the proposed amendment.

Prop. 6 would constitutionally create the SWIFT to assist in the financing of priority projects in the state water plan. The SWIFT would serve as a water infrastructure bank to enhance TWDB's financing capabilities. The fund would serve as a source of revenue for debt service payments in place of general revenue or as security for principal and interest payments on general obligation bonds or revenue bonds to finance or refinance projects included in the state water plan. It also would provide a revolving cash flow mechanism that would recycle money back to the fund to protect the corpus. Money in the fund would be available immediately to provide support for low-interest loans, longer loan repayment terms, incremental repurchase terms for projects in which the state owned an interest, and deferral of loan payments. Prop. 6 also would constitutionally create the SWIRFT to manage revenue bonds issued by the TWDB and supported by the SWIFT.

These funds would be special funds created inside the treasury but outside the general revenue fund, without further appropriation, but with oversight from the Legislative Budget Board. The proposed amendment would ensure that establishing these funds did not create state debt by providing that any bond enhancement agreement or obligation was payable solely from the two funds and would not be constitutional state debt payable from the general revenue of the state. Also, money in the funds would be constitutionally dedicated. Any money appropriated from the Rainy Day Fund also would be dedicated for the purpose of complying with constitutional provisions that exempt constitutionally dedicated funds from counting toward the spending cap.

According to TWDB, critical water shortages will increase during the next 50 years, requiring a long-term, reliable funding source to finance water and wastewater projects. The state water plan has identified projects intended to help avoid catastrophic conditions during a drought. However, rising costs for local water providers, the capital-intensive investment required to implement large-scale projects, and the financial constraints on some communities necessitate a dedicated source of funding to help develop those projects. The capital cost to design, build, or implement the recommended strategies and projects between now and 2060 will be $53 billion, according to TWDB, and municipal water providers are expected to need nearly $27 billion in state financial assistance to implement these strategies. Any delay in funding would put long-term planning of water projects in jeopardy and increase the overall cost to customers.

Unless the state fully implements its state water plan, 50 percent of Texans by 2060 will lack an adequate supply of water during times of drought. Without an adequate supply of clean, affordable water, the state's economy and public health would be irrevocably harmed. Water shortages during drought conditions cost Texas business and workers billions of dollars in lost income every year. If Texas does not implement the state water plan, those losses could grow to $116 billion annually. Until the state identifies and dedicates a permanent source of revenue to pay for the water infrastructure projects outlined in the state water plan, the future of the state's water supply will be in jeopardy.

The Rainy Day Fund would provide an ideal source of funding for the initial capitalization of the SWIFT. This investment would seed a revolving fund that could grow with only limited need for further state allocations. A one-time, $2 billion capitalization of the SWIFT could be used in conjunction with the TWDB's existing $6 billion evergreen bonding authorization to provide a meaningful funding solution for larger Texas water projects and financing for many of Texas' smaller communities. Without the initial capitalization of $2 billion from the Rainy Day Fund, revenue would have to be raised elsewhere, such as with a fee or tax.

Providing a funding program for water infrastructure to ensure an adequate water supply would be an appropriate use of the Rainy Day Fund. It was created as a savings account from which the Legislature may appropriate funds in times of emergency, and the state is on the cusp of a drought worse than the 1950s drought of record.

Use of the Rainy Day Fund would not jeopardize the state's credit rating or ability to handle an emergency. The Rainy Day Fund is expected to reach $11.8 billion by the end of fiscal 2015, according to the comptroller's January 2013 Biennial Revenue Estimate. A transfer of $2 billion from the fund would leave a comfortable balance for handling an emergency while preserving the state's superior credit rating. Given that the boom in the oil and gas sector shows no sign of slowing, any funds appropriated from the Rainy Day Fund would be replenished quickly. In addition, spending down a portion of the fund to support urgently needed water projects would help prevent the eventual spillover of Rainy Day funds into general revenue for spending on less pressing priorities.

Many entities that have the credit rating to finance projects on their own typically are not interested in using state financial assistance that is currently available due to the administrative burden and additional oversight involved. Financing projects through the SWIFT, by contrast, would offer several loan enhancements that would make financial sense to such entities, such as a lower loan rate and a deferral of principal and interest for a specified amount of time. This would encourage development and build-up of projects ahead of the critical need, which would facilitate the timely implementation of the state water plan.

Opponents say

If Prop. 6 won voter approval, the SWIFT would be capitalized initially by a one-time, $2 billion transfer from the Rainy Day Fund, which would not be an appropriate source of funding. Taking $2 billion out of the fund could result in a credit downgrade and curtail the state's ability to deal with a revenue shortfall, a natural disaster, or a school finance case decision that required additional state spending on public education. The provision in Prop 6 that would constitutionally dedicate the money in the funds, including money used to capitalize the funds, would allow the Legislature to circumvent the constitutional spending limit on undedicated funds.

Texas has a Moody's Aaa bond rating, which allows tens of millions of dollars a year in lower borrowing costs for the state. Texas needs to keep sufficient revenue in the Rainy Day Fund, and this large an appropriation out of the fund could put at risk the state's ability to maintain its Aaa bond rating and could imperil what has become a major state asset.

The comptroller estimates that the Rainy Day Fund will reach $11.8 billion by the end of fiscal 2015. However, deposits into the Rainy Day Fund have been historically hard to estimate, and the last seven estimates have been off by an average of 166 percent, with the closest estimate off by 23 percent. The Rainy Day Fund primarily is funded by oil and natural gas production tax revenue. The oil and gas industry is both cyclical and volatile, and it would not be responsible for the state to act in a way that assumes the fund will continue to grow at its current rate.

Funding another water lending program would be unnecessary and an inefficient use of Rainy Day funds because entities needing water infrastructure project funding already have tremendous access to capital. TWDB has several lending programs for water infrastructure through bonding programs that use the state's superior credit rating to guarantee water debt, enabling TWDB to offer inexpensive financing on a long-term basis. TWDB recently received approval for ongoing general obligation bond authority not to exceed $6 billion at any time. This financing is available even though many entities that are asking for help with projects in the state water plan already have a sufficient credit rating to complete a project without financial assistance from the state. Spending Rainy Day funds for infrastructure projects that already have access to capital would be inappropriate, given that there are several other critical needs in the state with limited funding options.

Notes

Prop. 6 would work together with two bills recently enacted by the 83rd Legislature — HB 4 by Ritter and HB 1025 by Pitts. HB 4, the enabling legislation, contains the mechanics of the funds, including the prioritization of projects that would receive funding. HB 1025 would make the appropriation from the Rainy Day Fund for the initial capitalization of the SWIFT. These provisions of HB 4 and HB 1025 are contingent on voter approval of Prop. 6.