

Testimony of William H. McRaven
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***Delivered remarks often deviate from prepared remarks*

Chairman Hancock, Chairman Ashby and Members.

My name is Bill McRaven and I'm the Chancellor of The University of Texas System.

Thank you for the opportunity to appear this morning to discuss the Permanent University Fund as you explore how the State of Texas can best fund and support our institutions of high education.

When the authors of the 1876 Texas Constitution set aside land in West Texas to support the University of Texas and Texas A&M systems of higher education, they had expectation that this arid brush land would become an unprecedented revenue generator. They expected that the land would be sold at some point and the proceeds of the sale invested to create an endowment. Striking oil changed everything, and that once-unpromising brush land has made the PUF and these two systems what they are today.

We have provided the committee with several documents describing the PUF and the fund into which its revenues flow, the Available University Fund. Let me hit the high points.

First, the Texas Constitution stipulates that one-third of the benefits of the PUF go to Texas A&M and two-thirds to the University of Texas.

The PUF itself consists of two parts – the 2.1 million acres of land that are dedicated to it and a permanent endowment, the corpus of which under the Constitution constitutes the oil and gas royalties that flow from those lands and the return on the investment of those revenues.

The PUF Lands are managed by one of the offices of UT System Administration, and the endowment is managed by a 501(c)(3) corporation, the University of Texas/Texas A&M Investment Management Company, or UTIMCO, both under the authority of the UT System Board of Regents.

The West Texas lands also generate a smaller but significant amount of surface revenue from grazing, hunting, wind farm and other leases and from fees for easements for pipelines and electricity distribution lines. This money goes straight into the AUF.

One of the two principal uses of the PUF prescribed by the Texas Constitution is to back bonds that pay for capital purchases. Both the UT and A&M systems can issue bonds guaranteed by the PUF, up to a limit prescribed by the Constitution. Within the UT System, these PUF-backed bonds may be issued for the benefit of all our 14 institutions, but may only be used to finance capital expenditures, specifically the construction or acquisition of new buildings or land or the purchase of long-term durable equipment, like an MRI.

Because the PUF is a large, stable and permanent fund, creditors see these bonds as extremely safe. This enables UT and A&M to sell the bonds and borrow money at very low interest rates, saving us millions of dollars each year. It's important to emphasize that the corpus of the PUF is not expended to pay these bonds; it simply guarantees that the bonds are good and that the money we borrow will be paid back.

The bonds are instead repaid from the Available University Fund, the AUF. The AUF consists of the annual surface income from the PUF Lands and an annual distribution in an amount determined by the UT Board of Regents, within constitutional limits, from the total return on investment (revenue plus capital gains) of the PUF. The size of this distribution is usually 4.75 percent or 5 percent, and by law it cannot exceed 7 percent of the market value of the PUF's investments. The 2018 distribution from the PUF to the AUF was \$887 million, or 5 percent of the market value of the PUF's investments.

The Constitution requires that the AUF first be used to pay principal and interest on PUF bonds. The remainder may be used for support and maintenance at UT Austin and for UT System Administration, with the latter used strategically for the benefit of all our institutions through centralized services and system-wide contracts. The Constitution does not allow the AUF to be used directly for operational expenses for the other UT institutions.

I give you all this background to support one fundamental message: every dollar of support that flows from the PUF through the AUF to UT and A&M institutions is a dollar that doesn't come from students, parents, taxpayers, or donors.

You can see from the chart at the bottom of the front of the Overview of the Permanent University Fund how many capital projects the PUF has helped finance at UT institutions. Without the PUF, even with the Legislature's generous periodic support for capital projects through tuition revenue bonds, we could never provide enough classrooms and laboratories for the ever-growing number of students who are being educated within the UT System.

The PUF also allows us to recruit the most talented faculty from around the nation into our classrooms and labs through our STARs program, where we use PUF bond proceeds to purchase

the capital equipment these faculty need to support their teaching and research. The chart on the back of the Overview includes a review of the results of the STARs program. It shows an 8.8-to-1.0 return on this investment, as the faculty recruited from FY 2005 to FY 2014 with \$195 million in equipment and renovations have generated \$1.9 billion in research funding.

You may ask why, given the size of the PUF, the Legislature needs to support UT and A&M with state General Revenue. This is because of the size and scale of these two systems. Together we educate more than 376,000 students, almost 25% of the state's total, with the two flagships in Austin and College Station alone educating more than 100,000 students.

And the PUF only keeps pace with the state's vital commitment to the fund that supports schools outside the UT and A&M systems, the Higher Education Assistance Fund, or HEAF. You can see from the final chart on the Overview that with the most recent increase in state appropriations to the HEAF, it actually provided more resources for capital projects on a per student basis at our academic institutions than did the PUF for 2017 and the most recent five or ten year periods. The HEAF has the additional advantage of receiving a constitutionally guaranteed revenue stream, while the PUF and AUF are ultimately subject to the condition of the markets.

The funding stream for UT and A&M through the PUF and AUF is unlike any other in American higher education. We owe it to Texas, and to the pioneers who created this unique funding mechanism, to be careful, responsible stewards of the PUF and to use this resource to advance higher education and the good of our state, to make a real difference for our young men and women and their families. We believe we do this at UT, and I'm happy to answer any questions you may have.