Senate Bill 1232
Preliminary Transition Plan
September 1, 2021

Introduction

As required under Section 18.53, Conference Committee Report on Senate Bill 1, 87th Legislature, Regular Session, this plan summarizes the creation of the Texas Permanent School Fund Corporation (the Corporation) as authorized under Senate Bill (SB) 1232 and the transition of permanent school fund (Fund) investment and operational functions from the Texas Education Agency (TEA) and the General Land Office (GLO) to the Corporation. Related activities are grouped into the following four sections as it is expected that the planning, execution, and implementation of SB 1232 will occur across various time periods:

I. Legal Creation of the Texas Permanent School Fund Corporation
II. Initial Corporation Board Actions and Corporation Activities
III. Transferring Assets, Investment Functions, and Core Operations
IV. Establishing Administrative Functions within the Corporation

To comply with the deadlines of SB 1232 and to ensure continuity in the management of Fund assets, the transition of certain functions to the Corporation will require coordination and execution across the activities described in one or more sections of this plan. Further, the timing of actions during the transition will be materially affected by decisions made by the Corporation board of directors (the Board). Accordingly, this plan describes the unfolding of events in general terms only, focusing on high-level milestones and order-of-operations; in most cases, options that will be available to the Board and the Corporation are provided in lieu of known outcomes with firm dates.

Each section of this plan includes a narrative description and additional details listed in two tables. The first table lists actions necessary to implement the transition, a description of each action, and an estimated timeframe. The second table lists related incremental costs where applicable. The final section of the document discusses implications for the management of 2022-2023 appropriations and appropriations for future biennia.

Section I: Legal Creation of the Texas Permanent School Fund Corporation

The first step of implementation of SB 1232 includes approval of the creation of the Corporation by the State Board of Education (SBOE), followed by the appointment of Board members, and the creation and approval of corporate articles of incorporation and bylaws. To create the Corporation, the SBOE must (1) approve the creation of the Corporation and (2) approve the initial articles of incorporation. After the Corporation is created, members of the Board can be appointed. The Board will consider and approve the initial bylaws, which must then be approved by the SBOE.

Implementation Milestones

Item	Action	Description	Estimated Timeframe
I.1	Approve creation of Corporation and articles of incorporation	SBOE votes to create the Texas Permanent School Fund Corporation and adopts initial articles of incorporation for the Corporation.	Anticipated to occur by Spring 2022
I.2	Appoint Corporation Board of directors	SBOE appoints five members to the Corporation Board; the land commissioner joins the Board; and the land commissioner appoints one member, and the governor appoints two members, all three of whom must have substantial background and expertise in investments and assets management.	Following the legal creation of the Corporation, and anticipated to occur by Spring 2022
I.3	Consider and approve Corporation bylaws	The Board considers and approves bylaws and the SBOE approves those bylaws.	Following appointment of all Board members, and anticipated to occur by Summer 2022

Projected Section I Incremental Cost through August 31, 2023

Item			
I.1, I.3	Legal fees	Cost of fiduciary counsel's time to consult on and draft articles of incorporation and Corporation bylaws.	$75,000

Section II: Initial Board Actions and Corporation Activities

To prepare for the transfer of Fund assets, employees, and management to the Corporation (described in Section III) and to allow enough lead time to establish administrative operations at the Corporation (described in Section IV), the Board will need to begin planning for and executing a number of activities in calendar year 2022, likely including but not limited to: hiring the Corporation's chief executive officer (CEO); establishing the location of office space and physical facilities, which significantly impacts information technology (IT) and investment and administrative operations; adopting various policies, such as ethics and personnel; acquiring certain insurance; and preparing the Corporation's legislative appropriations request for the 2024-2025 biennium (addressed in the final section of this document). These start-up activities will result in Corporation expenditures or the accrual of expenditures to TEA and/or the GLO in calendar year 2022. Some expenditures will entail the selection and engagement of outside consultants and service providers.

Implementation Milestones

Item	Action	Description	Estimated Timeframe
II.1	Hire the Corporation CEO	The Board hires the CEO and key staff to lead the transition and the transfer and management of Fund assets.	As soon as practicable after legal creation of the Corporation
II.2	Identify physical facility location and needs	The Board authorizes the CEO to take actions necessary to identify physical facility location and needs, including planning for IT infrastructure.	As soon as practicable after hiring of the Corporation CEO
II.3	Engage various service providers	The Board or CEO, in consultation with the Chief Investment Officers at TEA and GLO, selects the firm(s) to advise and provide consulting services in areas such as legal matters, operations, and/or employment.	As soon as practicable after hiring of the Corporation CEO
II.4	Prepare for transfer of assets	The Corporation begins updating contracts and documents with service providers, counterparties, and investment managers for both SBOE and School Land Board (SLB) assets.	Calendar year 2022

Projected Section II Incremental Cost through August 31, 2023

Item	Cost	Description	Estimated Amount
II.1	Initial staffing costs	Costs for Corporation to employ an estimated six to 10 full time equivalent positions (FTEs), including the CEO, beginning during fiscal year (FY) 2022 and continuing through the end of the 2022-2023 biennium, to prepare for and lead the transition of investment and administrative operations. It is possible that before the transfer some Corporation employees could remain within the PSF division at TEA, the Investment Management Division of GLO, or other areas of TEA, and provide support for the Corporation.	$2,500,000 to $3,000,000
II.2	Facility/location related costs	Expenses to secure and begin preparing a physical location for the Corporation, such as location/IT consulting services and rent. See Section IV for a discussion of the connection between physical facilities and IT infrastructure set-up costs.	$1,400,000 to $2,250,000
II.3	Consulting services	Cost for the Corporation to engage one or more firms to advise and provide legal, investment, and operational consulting services as the Corporation begins to implement the transition.	$500,000 to $700,000
II.4(a)	Preparation for transfer of SBOE assets	Legal and other expenses to begin updating SBOE contracts and documents with service providers, counterparties, and investment managers.	$750,000 to $1,500,000
II.4(b)	Preparation for transfer of SLB assets	Legal and other expenses to begin updating SLB contracts and documents with service providers, counterparties, and investment managers.	$800,000 to $1,400,000

Section III: Transferring Assets, Investment Functions, and Core Operations

Provisions of SB 1232 require certain transfers to the Corporation to occur on designated timeframes, beginning as early as January 1, 2023, on a date agreed to by the SBOE, TEA, SLB, and the Corporation The transfers in the table below relate to various aspects of the management and investment of the assets of the Fund. Most transfers in this section are interdependent and assumed to occur at or about the same time. It is important to note that the Corporation is authorized to delay one or more transfers if it determines that a transfer would have an adverse effect on the Fund or is not in its best interest.

The timing of some of these actions needs to be coordinated with activities described in Sections II and IV. For example, the transfer of assets to the management of the Corporation will require various changes with Fund service providers, external asset managers, and counterparties, and will vary for each type of asset. Such changes will require employees to be authorized to communicate with these entities and act on behalf of the Corporation and under the direction of the Board.

After the formal dates identified for the transfer of assets, it is expected that some residual Fund assets, income, receivables, expenses, and payables will need to be transferred or settled between the Corporation and TEA or the GLO. These issues can be addressed in contracts or memoranda of understanding between the Corporation and TEA and the GLO.

Item	Action	Description	Estimated Timeframe
III.1	Transfer asset management functions	Any power, duty, function, program, or activity related to the management and investment of the Fund transfers to the Corporation, except as delayed at the Corporation's discretion.[1]	One month, beginning in January 2023
	Transfer asset and operations management employees	All employees of the PSF division at TEA and the investment management division at the GLO become employees of the Corporation.	
	Transfer appropriations	Unexpended and unobligated appropriations to TEA and the GLO related to the list in Item III.1 transfer to the Corporation.	
III.2	Transfer SBOE assets	All Fund assets and investments and any related contracts held by the SBOE or TEA transfer to the Corporation.[2,3]	Expected to begin with III.1 in January 2023, but no later than March 31, 2023
III.3	Transfer SLB assets	All Fund assets and investments and any related contracts held by the SLB transfer to the Corporation.[2,3]	Expected to begin with III.1 in January 2023 and conclude by March 31, 2023

Notes: 1. Additionally, no later than January 31, 2023, but likely to be earlier, the SLB will provide a list of all SLB assets and related unfunded commitments that will transfer to the Corporation.

2. All Fund-related financial, contract, and investment records and documents must be provided by the SBOE, TEA, and SLB to the Corporation. It is assumed this will happen in conjunction with III.1, but with a deadline of March 30, 2023.

3. If the Corporation determines that any assets cannot be transferred expeditiously, then the transfer may be delayed beyond the deadline and the asset will continue to be held by TEA or SLB.

Projected Section III Incremental Cost through August 31, 2023

Item	Cost	Description	Estimated Amount
III.2	Transfer of SBOE assets	Costs to complete updates of SBOE contracts and documents with service providers, counterparties, and investment managers.	$250,000 to $350,000
III.3	Transfer of SLB assets	Costs to complete updates of SLB contracts and documents with service providers, counterparties, and investment managers.	$300,000 to $400,000

Section IV: Establishing Administrative Operations within the Corporation

Currently, the SBOE and SLB portions of the Fund are housed within TEA and the GLO, respectively. This plan assumes that the Corporation will be established as a stand-alone entity that will carry out all of its own administrative functions or pay for outsourced services. However, a transition period of indeterminate length will be necessary, during which support will continue to be provided by TEA while the Corporation assumes the administrative functions described below in a staged manner.

The initial Corporation actions described in Section II will determine the pace of the transition of administrative functions, making incremental costs and FTE needs difficult to predict at this time. The estimates given below are based on the projected maximum potential overlapping staffing and position-level operating costs for an eight-month transition period beginning January 2023 and continuing through the end of the 2022-2023 biennium, focusing on anticipated staffing needs in addition to those described in Section II. Other costs, such as IT infrastructure set-up, are to be determined. Potential strategies for addressing incremental costs, along with appropriations considerations applicable to future biennia, are discussed in the final section of this document.

Human Resources, Financial Services, and Other Support Functions

TEA and the GLO's human resources (HR), financial services (budget, accounting, and procurement), legal services, and governmental relations divisions provide support to all business units of their respective agencies, including the investment and operational teams that will transition to the Corporation Certain finance functions and legal services are already provided directly by operational staff within the SBOE/TEA portion of the PSF. This plan assumes that those functions will continue to be delivered at their current levels while other functions are added.

TEA and the GLO anticipate that the Corporation will initially adopt practices and systems currently used by TEA (merging former GLO employees into those systems) and will gradually modify those practices and systems over time to suit its own needs and purposes. TEA staff will continue to provide HR, financial services, and other indirect support to the Corporation while the Corporation's leadership establishes the procedures, policies, processes, systems, and personnel that will guide these functions, and determines the sequence and pacing of transferring functions from TEA. This support will continue for an indeterminate period leading up to and through the completion of the transition, as negotiated by the parties involved.

Item	Action	Description	Estimated Timeframe
IV.1	Establish human resources functions within the Corporation	The Corporation establishes functions in the areas of workforce management (such as recruitment, hiring, compensation practices, and employee engagement), talent development (such as performance management, training, and professional development), and employee relations (such as policies and procedures, employee support, and employee discipline), including hiring additional FTEs as needed.	Sometime after the Corporation CEO is hired and anticipated to complete in no more than six months, with gradual modifications anticipated over the first one to three years of independent operations.
IV.2	Establish remaining financial services functions within the Corporation	The Corporation establishes functions not already provided in the areas of accounting (such as payroll, accounts payable, travel, and vendor maintenance), budget (such as appropriation management, base reconciliation, and internal/external operating budgets), and procurement/contracting (such as procurement of goods and services, contract development and assignability, and records management), including hiring additional FTEs as needed.	Sometime after the Corporation CEO is hired and anticipated to complete in no more than eight months, with gradual modifications anticipated over the first one to three years of independent operations.
IV.3	Increase other indirect and general support functions within the Corporation	The Corporation adds staff as needed in legal services, government relations, and administrative assistance areas, if not addressed in Section II actions.	Sometime after the transition is initiated and continuing until all necessary staff are hired.
IV.4	Address information systems and records needs	The Corporation CEO and senior management decide which TEA systems used to support indirect functions will remain in use, establish access to external systems (such as USAS and ABEST), and develop a plan for migrating away from any systems that the Corporation will not adopt. Examples of key systems include CAPPS HR/PR and in-house HR and records management systems, and TEA's hub version of CAPPS Financials.	Initial decisions anticipated to occur during the (up to) eight-month transition period, with more significant decisions expected to occur gradually over the first one to three years of independent operations.

Information Technology

TEA's Information Technology (IT) division provides support to the PSF division of TEA in the areas of application and database support, infrastructure, data backup, access management, desktop support, security monitoring, statutory technology filings, and policies and procedures. Other IT services and functions—such as management and investment application support, end-user desktop and software support, custom application management, and investment data management—are provided by the division's own IT staff. At the GLO, investment staff receive IT services through a central IT function. This plan assumes that services already provided within the SBOE/TEA portion of the Fund will continue and recognizes that the Corporation has the option to establish all other IT functions to operate within the Corporation or to outsource some functions. The manner in which the Corporation exercises those options will determine precise staffing needs.

TEA and the GLO anticipate that the Corporation will initially adopt practices and systems currently used by both TEA (general IT functions and investment-related systems) and the GLO (investment-related systems), requiring an interface between existing systems. There will be a gradual migration of those systems during the initial period of independent operations. This will encompass a discovery phase of the applications and licenses utilized in the investment processes. Network infrastructure transition planning cannot begin until the physical location of the Corporation has been identified. This factor will meaningfully affect the IT cost and implementation timeline, as setting up a new environment often requires six to nine months.

Due to the number of unknowns and the complexity of migrating IT functions, TEA and the GLO cannot presently estimate the cost or duration of the transition. The agencies anticipate that TEA staff will continue to provide IT support to the Corporation for an indeterminate period of time, as negotiated by the parties involved, while the Corporation and its leadership determine the sequence and pacing of transferring systems and functions.

Item	Action	Description	Estimated Timeframe
IV.5	Transfer information technology assets and equipment to the Corporation	IT assets and equipment transfer to the Corporation pursuant to memoranda of understanding with TEA and the GLO. Some assets and equipment transition immediately (such as individual employee devices), while the timing of other transfers (such as application and database servers, infrastructure servers, software licenses and subscriptions) is dependent on certain decisions made by the Board and Corporation IT management. As noted, network infrastructure transition planning cannot begin until a physical location for the Corporation has been identified.	Sometime after hiring of the Corporation CEO and IT management and continuing for an indeterminate period of time, with some assets transferring immediately.
IV.6	Establish remaining information technology functions within the Corporation	The Corporation establishes functions not already provided internally in the areas of IT systems and management (such as application and database support, infrastructure, data backup, access management, desktop support, security monitoring, technology statutory fillings, and policies and procedures), including hiring additional FTEs as needed.	
IV.7	Address information systems and records needs	The Corporation CEO and other management decide which TEA and GLO systems used to support the information technology functions will remain in use, develop systems interfaces as needed to maintain data access, and establish a plan for migrating away from any systems that the Corporation will not adopt. Examples of key systems include M365 Admin console, file servers, web content management software, and security end-user management tools.	

Projected Section III Incremental Cost through August 31, 2023

As indicated above, the pace at which administrative activities and functions transfer to the Corporation cannot be predicted with any precision at this time, but it is expected that TEA the GLO will continue to provide support for an indeterminate period as the Corporation establishes the functions described in this section. As a result, during FY 2023 there will be overlapping costs between the parties involved.

Provisions of SB 1232 require that unexpended and unobligated appropriations to TEA and the GLO related to the activities and functions that are transferring to the Corporation to be provided to the Corporation on a date determined by the SBOE, TEA, SLB, and the Corporation That date and the amount of the appropriations to be transferred are currently unknown. To the extent Corporation leadership decides to fulfill some or all administrative functions independent of TEA or the GLO, those agencies may be without adequate appropriations to cover expenses for administrative services for the remainder of FY 2023. The table below describes incremental costs for administrative operations during the transition period, to the extent that these can be estimated at this time. The GLO expects to transfer an amount to pay a proportionate share of indirect costs; other potential strategies for addressing incremental costs, along with appropriations considerations applicable to future biennia, are discussed in the final section of this document.

<table>
<tr><th>Item</th><th>Cost</th><th>Description</th><th>Estimated Amount</th></tr>
<tr><td>IV.1-3, IV.6</td><td>Overlapping staffing and operating costs</td><td>Potential overlapping staffing costs and operating expenses (such as hardware leases) between TEA indirect services positions and new positions at the Corporation (including the Corporation CEO), for a transition period beginning January 2023 and continuing through the end of the 2022-2023 biennium, in addition to staffing needs identified in Section II.</td><td>$1,200,000</td></tr>
<tr><td>IV.4, IV.7</td><td>Information systems and records</td><td>Costs to migrate away from shared information systems supporting TEA and/or GLO human resources, financial services, and information technology services; transfer records and/or develop application interfaces to maintain access to historical data; and/or implement new solutions to replace information systems that the Corporation decides not to adopt.</td><td rowspan="2">Costs in these areas cannot be estimated at this time because they rely on several decisions that must be made by the Board and Corporation leadership. Furthermore, costs may be incurred over the course of several years rather than within a short or known timeframe. Network infrastructure set-up alone may require six to nine months.</td></tr>
<tr><td>IV.5</td><td>Transferring IT assets and equipment and network infrastructure buildout</td><td>Costs to transfer physical assets and equipment and to set up network infrastructure to support a standalone environment for the Corporation. As noted, network infrastructure transition planning cannot begin until a physical location for the Corporation has been identified. This factor will meaningfully affect the cost and implementation time.</td></tr>
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Implications for Current and Future Appropriations

Addressing Incremental Cost through August 31, 2023

This plan identifies known costs of transitioning the SBOE and SLB portions of the Fund to a fully operational and independent Corporation and estimates those costs to the extent possible. Incremental expenses discussed above total a range of between $7.8 million and $10.9 million through the end of the 2022-2023 biennium. However, certain costs, such as network infrastructure setup, cannot be estimated at this time for the reasons noted. There are three primary sources of potential funding to cover incremental expenses:

- Unexpended balances of appropriations from Permanent School Fund 0044 to TEA during the 2020-2021 biennium and fiscal year 2022 that are intentionally left unspent and carried forward to fiscal year 2023, to the extent not needed for regular, ongoing Fund operations.
- Funding transferred from the GLO to the Corporation (or, if necessary for timing reasons, to TEA) to support one-time costs, investment operations, and a proportionate share of new administrative expenses.
- A supplemental appropriation to the Corporation and/or TEA by the Texas Legislature for the purpose of addressing incremental costs of the transition.

TEA and the GLO anticipate that a combination of these sources will be needed. The two agencies will have a greater sense of the funds available from TEA unexpended balances and funds transferred from the GLO by approximately Fall 2022. Around that same time, more will be known about the actual cost of the transition because the Board will have been formed, will have taken initial actions, and the Board and/or Corporation senior leadership will have made key operational decisions needed to better estimate transition costs.

Implications for Appropriations for Future Biennia to the Corporation

This plan assumes that the Corporation will receive direct appropriations for operations during the 2024-2025 biennium and beyond, along with its own FTE allocation that is sufficient to allow for investment and administrative functions transferred from TEA, and investment operations transferred from the GLO. As noted elsewhere, the precise funding needs of the Corporation will be affected by actions taken by the Board and Corporation senior leadership during the 2022-2023 biennium. As historical precedent for the provisions of SB 1232 is extremely limited, TEA and the GLO are unable to predict the Corporation's funding needs for the 2024-2025 biennium. The Corporation will seek guidance from the Legislative Budget Board regarding how to submit its request.

Over time, the Corporation is expected to require additional operational funding and FTEs as the Fund assets grow and investment activities further diversify, with expenses remaining well within the anticipated General Appropriations Act (GAA) target of 16 basis points of combined net Fund assets managed. The Texas Legislature may wish to consider providing flexibility to the Corporation to increase its appropriation authority within the performance target through a finding of fact by the Board, especially for the purpose of addressing unanticipated transition costs.

Implications for Appropriations for Future Biennia: GLO and TEA

Permanent School Fund 0044 (Fund 0044) is currently used as a method of finance for certain administrative activities at the GLO and TEA. SB 1232 allows the GLO to retain revenues that would otherwise transfer to the Corporation, to continue paying for those administrative activities. The bill did not specifically address appropriations to TEA, where Fund 0044 pays approximately $8 million per year in administrative costs across numerous TEA support divisions. Of this total, $1.1 million and five FTEs are reduceable once the Corporation is established and fully independent.

The remaining $6.9 million in TEA's costs per year are non-reduceable. These expenses are predominately attributable to IT areas (approximately $5.0 million per year), including data center services. Remaining non-reduceable expenses (about $1.9 million per year) are spread across the agency in areas where services to the PSF division staff are not distinguishable from services to other divisions, where workload will not meaningfully change following the transition, and/or where segregation of duties requirements are a consideration. There are three primary sources of potential funding to address this gap in TEA's administrative budget:

- Base adjustments through the legislative appropriations request process that make more general revenue funding within the agency's existing limit available for administrative purposes.
- Continued appropriations from Permanent School Fund 0044 to TEA for activities allowable under the state constitution and state law.
- Appropriations to TEA from another source—for example general revenue or the Available School Fund—to replace lost appropriations from Fund 0044.

TEA anticipates proposing a combination of these sources through the legislative appropriations process so that its $6.9 million funding gap can be resolved by the 88th Legislature.