FISCAL IMPACT REPORT

SPONSOR	Garratt/Dixon/Brown/ Hernandez	**ORIGINAL DATE** **LAST UPDATED**	2/4/22	**HB**	
SHORT TITLE	Charter School Facility Improvements			**SB**	78
				ANALYST	Liu

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Nonrecurring	Fund Affected
FY22	**FY23**		
	$10,000.0	Recurring	Public School Capital Outlay Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY22	FY23	FY24	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total		$831.3	$831.3	$1,662.6	Recurring	Public School Capital Outlay Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

Duplicates HB43
Relates to HB119

SOURCES OF INFORMATION
LFC Files

Responses Received From
Public School Facilities Authority (PSFA)
Public Education Department (PED)
New Mexico Finance Authority (NMFA)

SUMMARY

Synopsis of Bill

House Bill 43 requires school districts to make facilities not currently used for educational purposes and land not currently used or planned to be used for such purposes available for lease, lease purchase, or purchase by charter schools. The bill requires districts to notify charters of such availability and tasks PSFA with ensuring the notifications occur. The bill also expands the facilities eligible for the Public School Capital Outlay Council's (PSCOC) lease assistance program beyond classroom facilities. The bill further amends the Public School Capital Outlay Act to create a charter facility fund, which will be distributed by PSCOC to pay off lease-purchase agreements. In addition, the bill amends sections of the Public School Capital Improvements Act (commonly referred to as SB-9) and the Public School Building Act (commonly referred to as HB-33) to establish a process for charter schools to be included in school district resolutions under these acts.

The bill appropriates $10 million from the public school capital outlay fund (PSCOF) to the public project revolving fund (PPRF) to provide loans to charter schools to fund school facilities (including purchase, construction, renovation, and paying off lease-purchase agreements). NMFA must develop rules and policies regarding the distribution of these funds, including ensuring lease-purchase agreements are in compliance with the Public School Lease Purchase Act, ensuring the recipient school's charter has been renewed at least once, and reviewing the school's last two audits. There is no effective date of this bill. It is assumed the effective date is 90 days after adjournment of the Legislature.

FISCAL IMPLICATIONS

The appropriation of $10 million contained in this bill is a recurring expense to PSCOF. Any unexpended or unencumbered balance remaining at the end of the fiscal year shall not revert. This bill creates a new fund and provides for continuing appropriations. The LFC has concerns with including continuing appropriation language in the statutory provisions for newly created funds, as earmarking reduces the ability of the Legislature to establish spending priorities.

PSCOF is the source of funding for the standards-based and systems-based capital outlay programs for public schools statewide, as well as for the state match for the SB-9 program, lease assistance program, facility security program, master plan assistance program, and other programs under the Public School Capital Outlay Act. Revenues to the fund are derived from supplemental severance tax bonds and allocations from the fund are authorized by PSCOC.

Provisions of this bill change the calculation of lease assistance for charter schools by basing the formula on the total square footage of the facility rather than the eligible classroom and administrative net square footage. According to PSFA, using the term "facilities" as opposed to the more narrow terms of "classroom facilities" or "classroom space" results in eligibility of 100 percent of the charter school facility gross square footage, and therefore 100 percent of the eligible lease amount. State funding for charter school lease assistance typically only covers 69.4 percent of the total annual lease amounts statewide, resulting in 30.6 percent of the costs covered by charter schools.

Lease assistance awards are based on the lesser of two calculations: prior-year student membership (MEM) times a per-MEM rate, or actual reimbursement of the lease based on eligible net square footage (NSF), calculated as classroom square footage plus administrative square footage. According to PSFA, the proposed change will result in approximately 80 percent of charter schools being granted lease assistance awards based on MEM, as opposed to the 64 percent awarded based on MEM in FY22. In total, the amount of funds awarded will increase. An analysis of the FY22 lease assistance awards indicates the total award amount would have increased approximately $841.3 thousand if the proposed change had been implemented. Approximately 30 percent of the awards would increase in funding. The percentage of total lease amount funded by the program remains relatively consistent, at approximately 67 percent.

Lease Assistance Analysis

	FY22 Lease Assistance Awards	HB43 Change to "Facilities" Term	Difference	
Total	$17,689,559	**$18,718,253**	$841,318	105%
Number of Awards **based on MEM**	66	83	+ 17	
	64%	80%	125%	
Number of Awards **based on Eligible NSF of Lease**	36	19	- 17	
	36%	20%	55%	
Percent of Total Lease Amount Funded	69.4%	67.3%	2.1%	

The bill proposes to pay off of lease purchase agreements (LPAs) from a revolving fund appropriated from PSCOF and administered by PSFA. In FY22, 30 charter schools sought lease assistance using a PED approved LPA. Each LPA total pay off cost is approximately $5 million to $20 million. PSFA notes the $10 million appropriation in the bill would be inadequate to pay-off all LPAs in the first year of implementation.

SIGNIFICANT ISSUES

PED notes charter schools that choose to purchase or construct a new facility have limited financing options. The Public School Capital Outlay Act focuses primarily on making needs-based awards for schools in the poorest condition in the state. Many charter schools do not meet the eligibility threshold for needs-based awards from PSCOC and instead resort to private financing of renovations or new construction. The bill would create two new public financing options, one administered by PSFA and PSCOC and another managed by NMFA.

Each year, school districts generate more than $100 million in local capital funds through SB-9 and HB-33 bond elections. Current law allows charter schools to submit information to school districts for inclusion in local bond elections, but does not have a detailed process by which this information must be used. This bill clarifies the process in current law by establishing a June 1 deadline for charter school requests and requiring school districts to establish a point of contact for bond resolutions. These adjustments ensure charter schools have a predictable legal process by which they may receive a portion of school districts' bond revenues.

Given difficulties with purchasing or constructing school-owned spaces, charter schools typically enter lease or lease-purchase agreements with school districts or private property owners. The charter school lease assistance program distributes PSCOF to charter schools to pay a portion or all of a charter school's lease. Charter schools must use other operational funding to cover the remaining portion of their lease not covered by the lease assistance program. By increasing the amount of facility space eligible for coverage by the lease assistance program, PED notes the bill may result in more operational funding directed to the classroom. PSFA notes the bill proposes a charter facility fund for the purchase, construction, expansion or renovation of facilities. Many charter schools are leased from private owners and depending on the circumstances, the funds used for the expansion or renovation of a privately owned facility may violate the New Mexico Constitution's anti-donation clause.

According to PED, the creation of a PSCOF loan program specifically for charter schools may circumvent the statutory public school capital outlay awards processes, a needs-based process which prioritizes state funding for schools in the worst condition in the state. The current needs-based system was created as the result of the *Zuni* capital outlay lawsuit, where the court found differences in local property wealth among school districts contributed to inequitable revenues for school facilities. Using PSCOF to make awards directly to charter schools may dilute the funding available for needs-based standards and systems awards and challenge the state's ability to meet the requirements of the *Zuni* lawsuit. However, given that charter schools cannot raise local taxes, a dedicated funding source may be what charter schools need to ensure their facility funding is equitable with school districts.

Provisions of the bill require NMFA to adopt policies for the PPRF to provide loans to charter schools for the purchase, construction, expansion or renovation of facilities or to pay off lease-purchase agreements. NMFA notes PPRF already has charter school policies that encompass what is required in the bill. NMFA's PPRF charter school policies recognize that charter school funding is subject to general fund appropriation, must be renewed every year, and can result in termination of leases on relatively short notice should the charter school decide to cease operations. PPRF has never had a loan payment default in its history due to its strong loan structuring policies, an important factor in the PPRF's AAA/AAA and Aa1/Aa2 ratings by Standard & Poor's and Moody's, respectfully. Under PPRF policies, only the most robust charter schools now qualify for loans from the PPRF. NMFA is unlikely to change its existing PPRF charter school policies as a result of the bill or $10 million appropriation.

The $10 million appropriation will need to be accounted for as a fund within the PPRF and will likely cause PPRF charter school loans to be limited to $10 million in total outstanding at any time. Under current PPRF policies and PPRF bond indentures, appropriation loans are limited to approximately $66 million outstanding at any time, with these funds now allocated to Ft. Bayard Medical Center and several Administrative Office of the Court loans. With a separate $10 million charter school fund available, released appropriation capacity would likely not be used for additional charter school loans.

PERFORMANCE IMPLICATIONS

A 2016 LFC evaluation of six selected charter schools found little difference in student performance between charter schools and traditional public schools in New Mexico. The report noted charter schools tended to serve a lower percentage of Hispanic, economically disadvantaged, and English learners compared with traditional public schools. Challenges existed with school grading, as some charter school missions were unique and did not align well with criteria set by PED. In FY15, selected charter schools had more experienced teachers, lower teacher turnover rates, and higher average teacher salaries than the statewide average. Oversight by state and local authorizers was inconsistent and revocations of charters were rare, despite poor charter school performance. The report recommended additional guidance for authorization and accountability of charter schools and separate funding formulas for charter schools. The report also recommended new formula funding and accountability structures to address virtual schools, due to issues of cost-effectiveness and learning outcomes.

A 2019 study by Stanford University found that in a year's time, the typical charter school student in New Mexico makes similar progress in both reading and math compared to the educational gains that the student would have made in a traditional public school. This result represents an improvement in the charter sector compared to earlier periods in which the performance of charter school students lagged behind that of traditional public schools. Further probing reveals the aggregate results are negatively influenced by the performance of online charter school students. Enrollment in online charter schools is associated with substantially weaker learning gains in both reading and math and that the inferior performance of online charter schools offsets the positive impact of brick-and-mortar charter schools on student growth in reading. The learning gains of charter school students in various subgroups are comparable to the gains of their peers in traditional public schools in the same subgroup.

ADMINISTRATIVE IMPLICATIONS

PSFA notes the bill requires proof of certain items for a loan, one of which is the review of audit reports for the prior two years; however, the bill is silent regarding the type of audit required and whether a loan should be denied if the audit results in significant audit findings. Although PSCOC requires applicants to indicate the status of their audit reports, PSFA does not review the audits. In this situation, the audit results are important to assess the financial standing and capacity of a charter school. Therefore, the loan should be dependent on the type of audit issued. However, PSFA does not have staff with the expertise to review audits for this purpose.

PSFA and NMFA will need to ensure a charter school is not receiving duplicative funding for the same lease agreement, construction, expansion, or renovation loan in any given fiscal year. PED currently reviews charter school lease purchase agreements. The bill would likely have little bearing on this process, but would require the PED to communicate with NMFA, PSFA, and PSCOC to ensure loans are made only to charter schools with LPAs in compliance with the law.

Provisions of the bill require school districts to notify charter schools by May 1 about available land or one or more available facilities not currently used for other educational purposes, and for PSFA to ensure verification of this notification. PSFA notes there is no requirement nor mechanism provided for charters to accept and use available facilities or land. With respect to the land, if the charter school decides to use it to construct a facility, the bill does not set forth any guidelines for conveyance of the land. There is no indication that facilities offered must meet the educational program of the charter, nor if the facilities must meet statewide educational adequacy standards set by PSCOC. PSFA does not keep data on school districts' unused or non-education facilities, and can therefore not verify the availability or condition of potential available facilities offered to charter schools.

Eliminating the "classroom facilities" definition for eligibility for lease assistance, would greatly simplify the administration of the lease assistance program by PSFA, but may lead to other implications. Changing the space definition from "classroom space" to "facilities" would eliminate the annual process of verifying the eligible classroom square footages due to charter school space modifications, expansions, new construction, or relocations.

NMFA is structured and staffed to underwrite, analyze, approve and close PPRF and other loans totaling well over $200 million per year. As such, the $10 million appropriation in this bill can be easily accommodated at NMFA.

DUPLICATION, RELATIONSHIP

This bill is a duplicate of House Bill 43. The bill relates to House Bill 119, which changes the formula for SB-9 state distributions.

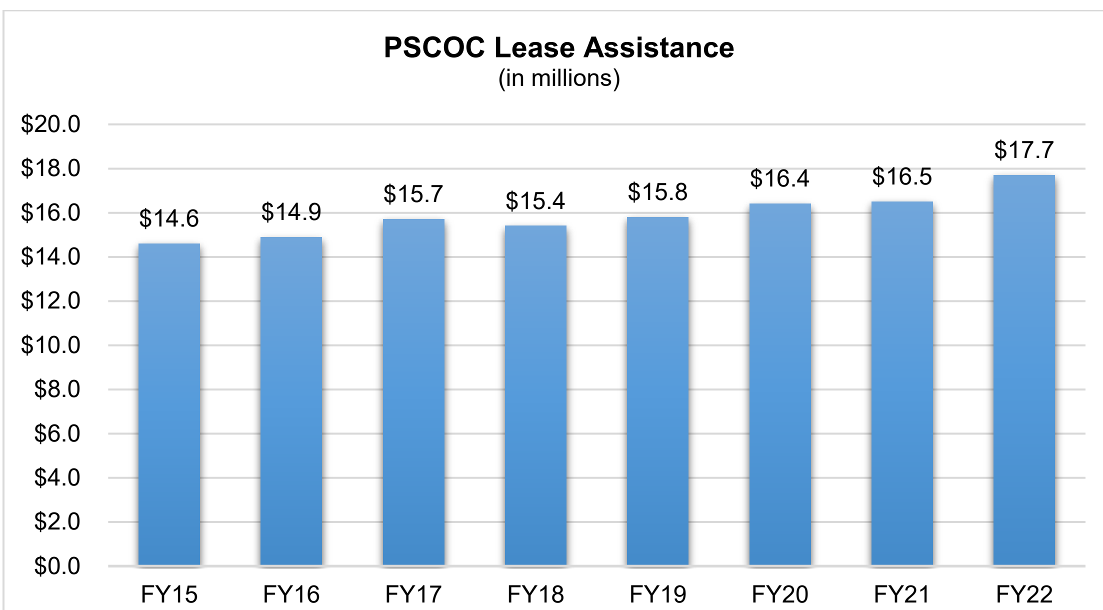
TECHNICAL ISSUES

PSFA notes proposes changes to the grant criteria amending the definition of space from "classroom facilities" to "facilities," defined as "space needed for school activities." This proposed definition is vague and overly broad, and may require clarification to ensure the facility is used solely for educational and operational purposes of a functioning charter school. The proposed vague language could potentially be interpreted to include secondary spaces, such as parking, sports stadiums, performing art centers, livestock corrals and acreage for gardens and other such type facilities "needed for school activities." These types of spaces are not eligible for PSCOC funding. In addition, this definition could lead to the lease of excess space by charter schools who could then sublease the extra space as is currently occurring with two charter schools. Due to the oversight of the PSFA, this extra square footage has not been eligible for PSCOC funding. However, this proposed definition could lead to the funding of excess space with PSCOC funds, which then could potentially be subleased.

PSFA notes the bill uses the term "lease purchase agreements" to identify a lease purchase; however, the term in the Public School Lease Purchase Act in Subparagraph A of Section 22-26A-2 NMSA 1978 identifies a lease purchase as either a "financing agreement," or "lease purchase arrangement."

OTHER SUBSTANTIVE ISSUES

Lease assistance is a PSCOC discretionary program. Awards have historically increased year-over-year, with the exception of FY18. In FY22, the PSCOC approved a 2 percent CPI adjustment to the lease assistance award amount per student (MEM), resulting in $762.24 per MEM and an increase in the total award amount. Below are the total lease assistance awards for the last few years.



ALTERNATIVES

NMFA notes placing the $10 million appropriation in PPRF and requiring NMFA to establish charter school policies within PPRF rather than making a $10 million appropriation to NMFA to establish a charter school fund outside PPRF will likely result in little change in NMFA policies on charter school financing. NMFA can easily operate a charter school fund outside the PPRF and develop more charter school friendly and innovative policies if not constrained by PPRF indentures and rating criteria.

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