F I S C A L   I M P A C T   R E P O R T

ORIGINAL DATE 01/26/12
SPONSOR Sanchez, M. **LAST UPDATED** 01/30/12 **HB**

SHORT TITLE Permanent Funds for Education, CA **SJR** 9

ANALYST Smith

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY12	**FY13**	**FY14**		
		$124,564.0	Recurring	General Fund
		$24,436.0	Recurring	Other LGPF Beneficiaries
		$149,000.0	Recurring	Land Grant Permanent Fund

(Parenthesis ( ) Indicate Revenue Decreases)

This FIR is being corrected to incorporate responses from interested parties. No estimates have changed.

SOURCES OF INFORMATION
LFC Files

Responses Received From
State Investment Council (SIC)
State Land Office (SLO)

No Response From
Attorney General's Office (AGO)

SUMMARY

Synopsis of Bill

Senate Joint Resolution 9 amends Article 12, Section 7 of the State Constitution to make permanent the current 5.5% annual distribution from the Land Grant Permanent Fund (LGPF) to public schools and other LGPF beneficiaries starting in FY 2013. It also calls for additional distributions from the LGPF of 1.5% specifically earmarked for early childhood education programs, to be operated by the public schools or through contracts with authorized private administrators.

The proposal allows that should the 5-year average of the LGPF drop below $8 billion, the additional 1.5% be suspended for the fiscal year. The proposal also allows the additional 1.5% to be suspended by a 3/5 vote by both House & Senate.

If approved by the legislature, the constitutional amendment would be brought to voters in the next general election or at a special election for this purpose.

FISCAL IMPLICATIONS

In the short term, additional contributions from the LGPF will produce significant revenue to the general fund and other LGPF beneficiaries, primarily being public education. In the long term, and taking into consideration Fund contributions from the oil and gas revenues, as well as expectations for general inflation and fluctuations in investment income, this proposal increases the risk that the LGPF will not be able to deliver the same benefits to the general fund and other beneficiaries as the Fund does today.

This bill is scored assuming it passes judicial muster. However, analysts have cast doubt as to it's constitutionality.

SIGNIFICANT ISSUES

This increased distribution will deplete the fund over time. Under the distribution schedule of 7.0% which ratchets down to 5.5% in 2025, SIC notes the following:

- 20 years after implementation, the LGPF has $5.5 billion less in its corpus than it would under current expectations
- That translates to more than $275M/yr less in distribution at 5% rate after 2031
- The LGPF growth rate is significantly decreased
- This chart again assumes growth of oil and gas revenues, and a positive long-term investment environment

However, the concept of a perpetual endowment is not in itself "good policy". Julius Rosenwald was President of Sears and Roebuck and major 20th century philanthropist. He wrote that "I am opposed to the permanent or what might be styled the never-ending endowment… Permanent endowment tends to lessen the amount available for immediate needs; and our immediate needs are too plain and too urgent to allow us to do the work of future generations."

In short the decision to deplete an endowment is a policy decision rather than a financial dictum or "best practice". The real question is whether the benefits of the expenditures today will outweigh the benefits of greater income tomorrow.

TECHNICAL ISSUES

The LGPF was created pursuant to the New Mexico Enabling Act, under which the federal government granted land to the State of New Mexico for specified purposes and required that the land and proceeds derived from the land be held in trust and used only for those specific purposes. The largest part of the land grant was for "common schools," and the common schools permanent fund is the largest of the LGPF. Section 2 of the Enabling Act required that the State consent to the Enabling Act restrictions, incorporate them into the state constitution, and prohibited any change in those restrictions without the consent of Congress. Accordingly, this language was incorporated into the compact between the federal government and the State of New Mexico, set forth as Article 21 of the New Mexico Constitution, with specific reference to the land grant trust fund in Section 9 of Article 21.

(A) Use of common schools funds for early childhood education. It is not clear that the distribution of common schools permanent fund money for early childhood education complies with the Enabling Act requirement that the funds be used for "common schools." Historically, "common schools" has been understood to mean public primary (K-6) and secondary (7-12) schools, and LGPF distributions for common schools have been made for primary and secondary education.

(B) Contracting with private entities, which may be sectarian. It is not clear that the distribution of common schools permanent fund money for contracting with private entities complies with the Enabling Act requirement that the funds be used for "common schools," particularly given the requirement in Section 8 of the Enabling Act that the schools supported "shall forever remain under the exclusive control" of the State. In addition, Section 8 of the Enabling Act prohibits the use of LGPF money "for the support of any sectarian or denominational school." Thus, to the extent that contracts are entered into with sectarian schools or entities, the use of LGPF may violate the Enabling Act.

(C) Distributions in excess of the 5% provided for under the 1997 Enabling Act amendments. In 1996, the NM Constitution was amended to provide that annual distributions from the LGPF would be 5% percent of the average of the year-end market value for the preceding five calendar years. Recognizing that this required an amendment to the Enabling Act, Congress amended the Enabling Act in 1997 to provide that LGPF distributions be made "as provided in Article 12, Section 7 of the New Mexico Constitution," specifically referencing the constitutional amendment that had been made in 1996 to provide for annual distributions of 5% of the 5-year average value. No amendment of the Enabling Act was sought for the additional annual distributions enacted in 2003.
State land Office makes the following argument:

The Enabling Act trust encompasses both the lands and associated natural resources granted by the federal government and the proceeds generated from sales and leases, which are deposited into the LGPF and the maintenance funds. To the extent that funds are generated from sales or extraction of oil, gas and other minerals, those funds should be considered part of the corpus of the trust. Because the trust is perpetual and certain provisions of the Enabling Act require the proceeds of sales and other permanent dispositions of trust assets go into a "permanent inviolable fund," the State's trust responsibility requires that the trust corpus be preserved and that distributions be limited to income and increased value derived from investment of the LGPF.

SS/svb:amm