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

		ORIGINAL DATE	02/06/21		
SPONSOR	Munoz	**LAST UPDATED**		**HB**	
SHORT TITLE	Use of Some Revenue for School Funding			**SB**	225
				ANALYST	Liu

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY21	FY22	FY23	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total			$0.0 - $51,667.5	$0.0 - $51,667.5	Recurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

Relates to HB6, HB84, HB85, HB86, HB87, SB41, SB249
Relates to Appropriation in the General Appropriation Act

SOURCES OF INFORMATION
LFC Files

Responses Received From
Public School Facilities Authority (PSFA)
Indian Affairs Department (IAD)

No Response Received
Public Education Department (PED)

SUMMARY

Synopsis of Bill

Senate Bill 225 removes the 75 percent credit for federal Impact Aid, local half-mill property tax levy for schools, and federal forest reserve fund revenues from the calculation of the public school funding formula. The effective date of this bill is the beginning of FY23.

FISCAL IMPLICATIONS

The bill eliminates $83 million in recurring credits from the public school funding formula – deductions from the state equalization guarantee distribution to school districts and charter schools for local education agencies (LEAs) with additional sources of funds. Absent any appropriations to offset the loss of these deductions, the formula would redistribute SEG allocations from LEAs with fewer credits to LEAs with significantly more credits. Because $67 million, or 80 percent of all credits, within the formula is attributable to federal Impact Aid payments, LEAs with Impact

Aid would receive a larger share of redistributed SEG allocations, which would decrease SEG allocations for many LEAs that do not receive Impact Aid.

However, the FY21 state operating budget included a partial offset of $31 million for Impact Aid credits (see "Other Substantive Issues"), and the FY22 LFC budget recommendation for public school support includes $52 million to eliminate local and federal credits. Together the two appropriations (totaling $83 million) would offset the full fiscal impacts of this bill, mitigating the proportional shift of SEG distributions from LEAs that do not receive Impact Aid to LEAs that receive Impact Aid and increasing SEG distributions for all schools, particularly LEAs with Impact Aid. Notably, nearly 60 percent of the appropriation would be allocated to the Gallup-McKinley County, Central, and Zuni school districts due to the significant amount of Impact Aid payments budgeted by these districts.

Eliminating credits from the public school funding formula would improve PED's accuracy with setting the initial unit value by removing the need to project federal revenue receipts (which are sometimes late or delayed). An accurate preliminary unit value would maximize the funding schools could budget at the beginning of a fiscal year, subsequently reducing the potential for reversions to school cash balances attributable to mid-year unit value increases.

SIGNIFICANT ISSUES

Provisions of this bill would provide additional state aid for LEAs equal to the amount of credits in the public school funding formula for operational expenditures. This analysis assumes $83 million is appropriated to completely offset distributional impacts, and all LEAs receive additional SEG distributions for the aforementioned purposes.

Elimination of credits in the funding formula would substantially increase operational revenue for LEAs with significant local and federal revenue sources (see Attachment 1). Gallup-McKinley School District, the LEA with the most formula credits, would receive an additional $22 million from eliminated credits, a 26 percent increase in SEG payments. In contrast, the LEA with the fewest formula credits, Pecos Independent Schools, would receive an additional $12.8 thousand, a 0.2 percent increase in SEG payments.

PSFA notes the bill does not restrict uses of the new revenue provided from elimination of the credit and if used for operations, rather than capital outlay, the bill has the potential to destabilize the formula-based state equalization guarantee distribution of operating funds to school districts and charter schools. In the 1999 *Zuni* capital outlay adequacy lawsuit, the court found New Mexico's public school capital outlay funding system, which relied primarily on local property tax wealth to fund public school capital outlay, violated the state constitution provision for a uniform and sufficient education system.

IAD notes many tribal nations in New Mexico advocate for eliminating the credit taken against federal Impact Aid grants within the SEG formula. The agency recommends that information on how districts and charter schools are spending the funds should be made available to tribes. Additionally, tribes have requested more authority over the local school boards and districts to ensure that Native American students are being adequately served. Although consultation with tribes is required under federal Indian Policies and Procedures for Impact Aid, IAD notes this process has not worked to the satisfaction of tribes.

PERFORMANCE IMPLICATIONS

Provisions of this bill would direct more operational funding to Impact Aid school districts, which include schools with significant numbers of students living on tribal lands. A 2021 LFC evaluation on implementation of the Indian Education Act found Native American students continue to perform below their peers on state and national measures of achievement, despite recent improvements in their high school graduation rates, college attendance, and Native language fluency. The evaluation noted a history of understaffing in PED's Indian Education Division, difficulties with utilizing Indian education funds, challenges with local collaboration at the district level, and problems with ensuring funds were aligned to specific, targeted outcomes. Provisions of this bill increase revenue for LEAs, rather than the state, to implement programs for Native American students. Substantial local funds could improve implementation of the Indian Education Act and support additional interventions for Native American students, given the state's limited capacity to drive improvements through smaller, statewide grants.

ADMINISTRATIVE IMPLICATIONS

Eliminating the Impact Aid credit in the funding formula would allow school districts to use federal operational Impact Aid payments for expenditures recommended through consultations with tribal government and communities as required under federal Indian Policies and Procedures for Impact Aid funds.

RELATIONSHIP

This bill relates to the SEG appropriation in the General Appropriation Act. The bill also relates to House Bill 6, which eliminates local and federal credits in the formula but requires schools to budget the eliminated credits for specified uses; Senate Bill 41, which also eliminates credits in the formula and changes the public school capital outlay local-state match formula to account for new revenue sources made available from the eliminated credit; and Senate Bill 249, which eliminates only the Impact Aid credit from the formula.

The bill also relates to the tribal remedy framework outlined in House Bill 84, House Bill 85, House Bill 86, and House Bill 87, which request funding for various tribal programs and infrastructure on tribal lands.

OTHER SUBSTANTIVE ISSUES

Overview of Federal Impact Aid. Congress has provided financial assistance to local school districts through the Impact Aid program since 1950. Impact Aid was designed to provide financial support to school districts that lack local revenue through property taxes, due to the presence of tax-exempt federal property (tribal trust lands and military bases). School districts with increased expenditures due to the enrollment of federally connected children (children who reside on Indian lands, military bases, low-rent housing properties, and other federal properties, or have parents in the military or employed on eligible federal properties) are also intended recipients of these funds.

Most Impact Aid funds, except for the additional payments for children with disabilities and construction payments, are considered general aid to the recipient school districts. These funds may be used in whatever manner the school districts choose, so long as it is in accordance with local and state requirements. Most recipients use funding for daily expenditures, but recipients may use the funds for other purposes, such as capital expenditures. School districts are required by federal regulations to consult with tribal governments and parents under the Indian Policies and Procedures about how these monies are spent. LEAs receive Impact Aid funds directly from the federal government through an application process, so states do not receive nor process these funds.

The federal government authorizes a state to “credit,” or supplant, a portion of state aid to LEAs that receive federal Impact Aid payments if the state can demonstrate that disparities in per-student spending or per-student revenues between LEAs in the 95th and 5th percentile are less than 25 percent (i.e., there are minimal differences in funding per student between LEAs). States must account for (and also credit) other federal and local revenues in the same manner. If the state’s funding methodology passes this disparity test, the U.S. Department of Education (USDE) classifies the state as having an “equalized” methodology and allows the state to adjust (credit) appropriations to minimize funding disparities among LEAs caused by differences in local or federal revenue sources.

Public School Capital Outlay. In 2000, the 11th Judicial District Court ruled in the *Zuni Public District v. State of New Mexico* lawsuit that New Mexico’s public school capital outlay system violated constitutional requirements and ordered the state to establish and implement a uniform funding system for capital improvements and for correcting past inequities. Since the *Zuni* lawsuit, the state has created a statewide system for public school capital outlay and spent $2.7 billion to build school facilities up to the approved statewide adequacy standards. Despite significant improvements in statewide facility conditions, the *Zuni* lawsuit was never closed and, in December 2020, the court ruled in favor of plaintiff school districts on new claims of inequity. The major claim of the plaintiffs was their inability to raise sufficient local capital outlay revenue to maintain capital assets and build facilities that were outside of the statewide adequacy standards, an option available to districts with stronger local resources.

School districts that receive federal Impact Aid funds have argued these funds are essentially payments to replace lost property tax revenue because of federal activity. However, legislation has been enacted to provide additional state funding for school districts with low property tax bases. Laws 2018, Chapter 66, (SB30) changed PSCOC’s state and local match calculation to be based on the net taxable value for a school district for the prior five years, the maximum allowable gross square footage per student pursuant to the adequacy planning guide, the cost per square foot of replacement facilities, and each school district’s population density. Overall, plaintiff school districts’ facility conditions (as measured by PSFA’s facilities condition index) are comparable or better than the statewide average.

The state modified its method of funding public school capital outlay projects in FY19, earmarked $34 million for Impact Aid districts to build teacher housing and facilities outside of the adequacy standards in FY20, and appropriated $18.9 million to Impact Aid districts for maintenance and infrastructure in FY21. Between FY19 and FY21, PSCOC awarded over half of all standards-based construction awards, or $262.4 million, to Impact Aid districts.

USDE Determination. In FY20, the Gallup-McKinley County, Central, and Zuni school districts requested a USDE predetermination hearing to evaluate PED’s request to credit federal Impact Aid payments in the FY20 funding formula. The plaintiff districts argued that specific revenue sources, like “SB9” capital improvement funds and transportation distributions, should be considered operational revenue within New Mexico's disparity test calculations. USDE sided with the plaintiff districts' methodology, which caused New Mexico to fail the FY20 disparity test. As a result, USDE determined the state could not credit Impact Aid payments in FY20.

PED appealed and then withdrew its appeal of USDE's FY20 determination. However, the department submitted a revised disparity test calculation for FY21, which incorporated the new revenue sources requested by plaintiff districts and a new methodology for crediting Impact Aid payments by LEA. The Gallup-McKinley County, Grants, and Zuni school districts filed an injunction to prohibit PED from providing inaccurate information to USDE for the FY21 determination; however, this motion was overturned by the 1st Judicial District Court.

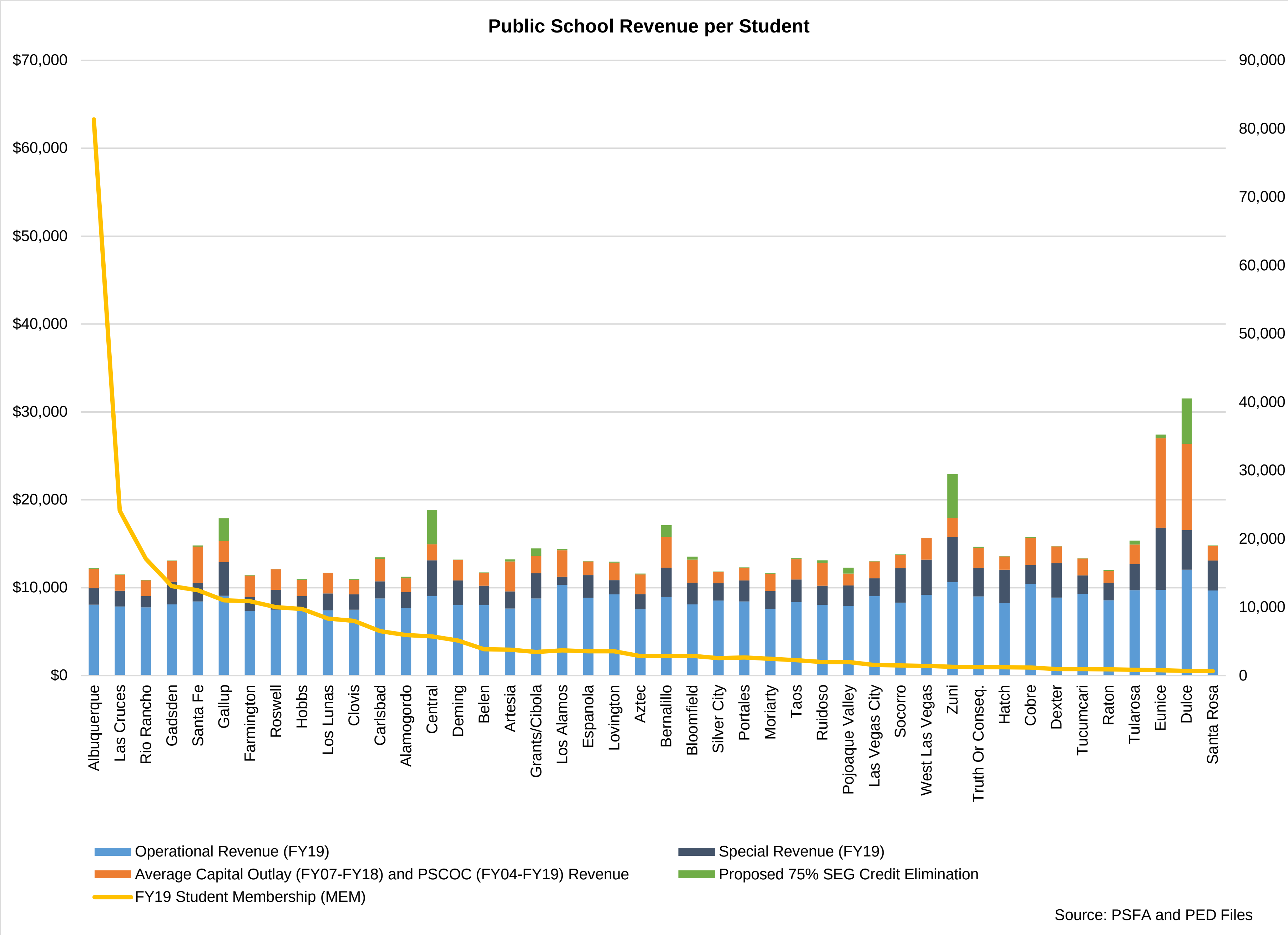
During the 2020 first special legislative session, the Legislature appropriated $31 million to partially offset the potential loss of the $67 million Impact Aid credit within the FY21 funding formula. The recurring appropriation anticipated USDE's ruling would prohibit the state from crediting Impact Aid in future years. PED has continued to credit Impact Aid payments in accordance with state law pending a final determination on the state's ability to do so for FY20 and FY21.

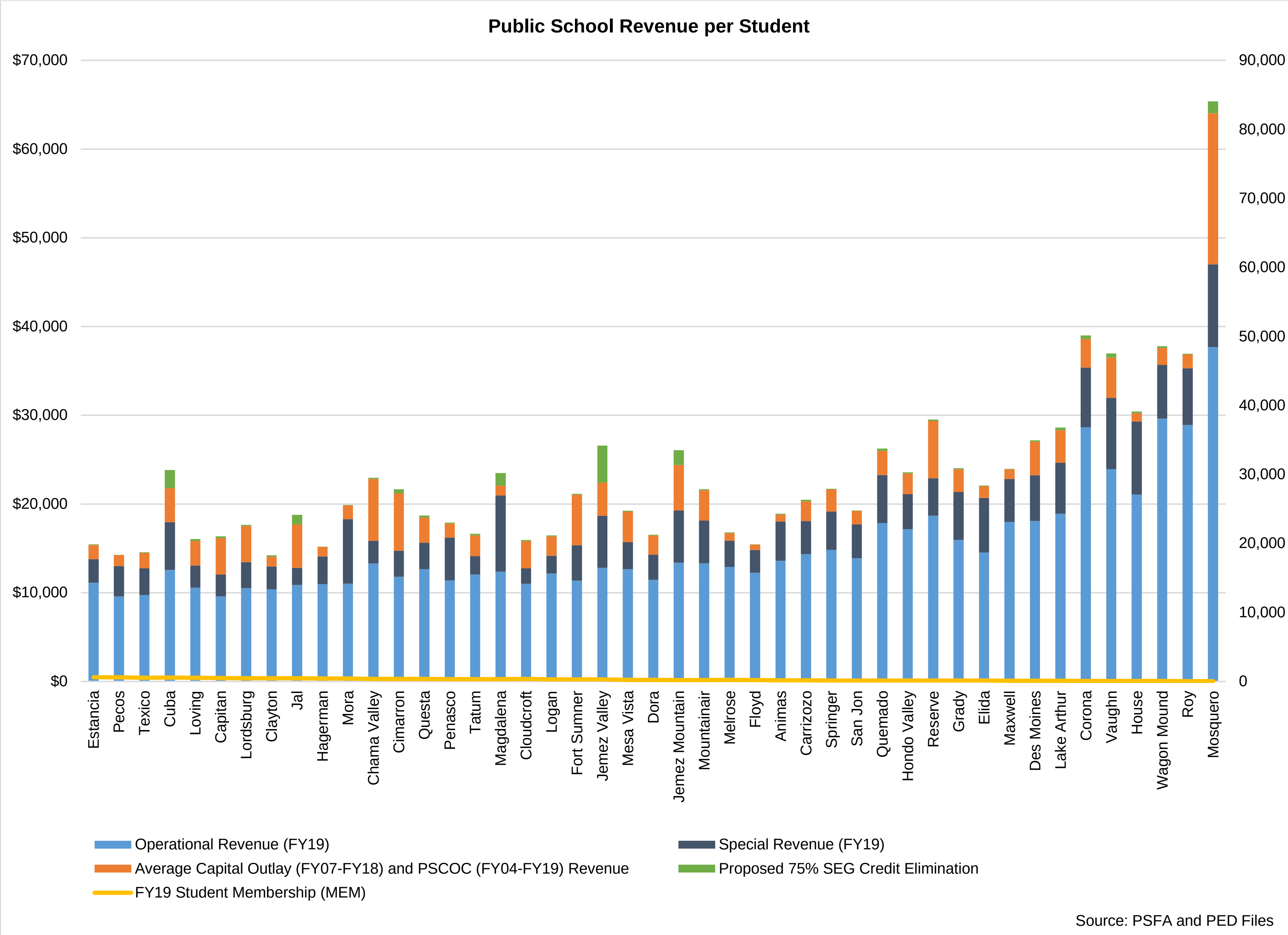
ALTERNATIVES

During the 2019 interim, LFC and LESC staff held regional stakeholder engagement sessions to discuss ways to address concerns brought by Impact Aid districts. Some suggestions included

- Amending the Public School Capital Improvements Act (commonly known as SB9) to shift more state funding to low property-wealth districts,
- Increasing the SB9 state program guarantee, allowing PED to advance SEG payments to cover delayed federal Impact Aid payments,
- Creating a new PSCOC program to retroactively update schools that received an early standards-based award (given the evolution of adequacy standards since 2003),
- Reprioritizing existing PSCOC programs to support facilities needed by Impact Aid schools,
- Increasing emergency support for schools with declining enrollment or property valuation (Central Consolidated Schools anticipates significant revenue loss from the closure of the San Juan Generating Station.),
- Centralizing all capital outlay project funding and oversight through the state,
- Restricting expenditures to specified revenue sources, and
- Changing the public school funding formula, including increased funding for at-risk students and reducing SEG credits.

SL/sb/rl


Public School Revenue per Student
$70,000
$60,000
$50,000
$40,000
$30,000
$20,000
$10,000
$0
90,000
80,000
70,000
60,000
50,000
40,000
30,000
20,000
10,000
0
Albuquerque
Las Cruces
Rio Rancho
Gadsden
Santa Fe
Gallup
Farmington
Roswell
Hobbs
Los Lunas
Clovis
Carlsbad
Alamogordo
Central
Deming
Belen
Artesia
Grants/Cibola
Los Alamos
Espanola
Lovington
Aztec
Bernalillo
Bloomfield
Silver City
Portales
Moriarty
Taos
Ruidoso
Pojoaque Valley
Las Vegas City
Socorro
West Las Vegas
Zuni
Truth Or Conseq.
Hatch
Cobre
Dexter
Tucumcari
Raton
Tularosa
Eunice
Dulce
Santa Rosa
Operational Revenue (FY19)
Special Revenue (FY19)
Average Capital Outlay (FY07-FY18) and PSCOC (FY04-FY19) Revenue
Proposed 75% SEG Credit Elimination
FY19 Student Membership (MEM)
Source: PSFA and PED Files


Public School Revenue per Student
$70,000
$60,000
$50,000
$40,000
$30,000
$20,000
$10,000
$0
90,000
80,000
70,000
60,000
50,000
40,000
30,000
20,000
10,000
0
Estancia
Pecos
Texico
Cuba
Loving
Capitan
Lordsburg
Clayton
Jal
Hagerman
Mora
Chama Valley
Cimarron
Questa
Penasco
Tatum
Magdalena
Cloudcroft
Logan
Fort Sumner
Jemez Valley
Mesa Vista
Dora
Jemez Mountain
Mountainair
Melrose
Floyd
Animas
Carrizozo
Springer
San Jon
Quemado
Hondo Valley
Reserve
Grady
Elida
Maxwell
Des Moines
Lake Arthur
Corona
Vaughn
House
Wagon Mound
Roy
Mosquero
Operational Revenue (FY19)
Special Revenue (FY19)
Average Capital Outlay (FY07-FY18) and PSCOC (FY04-FY19) Revenue
Proposed 75% SEG Credit Elimination
FY19 Student Membership (MEM)
Source: PSFA and PED Files