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

SPONSOR Wirth

ORIGINAL DATE 02/16/21
LAST UPDATED

HB

SHORT TITLE Funds for Teachers and Salaries, CA

SJR 1

ANALYST Iglesias

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY21	**FY22**	**FY23**	**FY24**	**FY25**		
-	*	($169,810.4)	($181,297.2)	($193,655.5)	Recurring	Land Grant Permanent Fund
-	*	$169,810.4	$181,297.2	$193,655.5	Recurring	Common School Fund (a component of the general fund earmarked for public schools)

Parenthesis ( ) indicate revenue decreases
*The provisions of this bill require a constitutional amendment. For the purpose of this FIR, the fiscal impact estimate assumes the constitutional amendment would be sought during FY22 and changes to the distributions would begin in FY23.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

FY21	FY22	FY23	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
	$150.0 - $200.0		$150.0 - $200.0	Nonrecurring	General Fund

Parenthesis ( ) indicate expenditure decreases

Conflicts with HJR1

SOURCES OF INFORMATION
LFC Files

Responses Received From
State Investment Council (SIC)
Attorney General's Office (NMAG)
Department of Finance and Administration (DFA)
State Land Office (SLO)
Public Education Department (PED)

SUMMARY

Synopsis of Bill

Senate Joint Resolution 1 seeks to amend Article XII, Section 7 of the New Mexico Constitution to provide an additional 1 percent annual distribution from the permanent school fund (the largest component of the land grant permanent fund) for teacher salaries and instruction purposes. The other 20 beneficiaries of the land grant permanent fund would not be affected by this additional distribution. The Constitutional Amendment would only be effective if passed by voters in the next general election (2022) or via a statewide special election held for this purpose.

FISCAL IMPLICATIONS

This proposal is different from other constitutional amendment proposals to increase the land grant permanent fund (LGPF) distributions, as it seeks to divide the components of the LGPF by only increasing the distribution for the largest beneficiary, public schools.

Impact on the LGPF. The State Investment Council states the increased distribution from only one component of the LGPF requires complex modeling that is further complicated by the fact that percentages of LGPF ownership change slightly on a monthly basis based on revenues generated by each specific parcel of the 9 million (13 million subsurface) acres assigned to each of the 21 LGPF beneficiaries. For example, over the past decade or so, the percentage of LGPF "ownership" by the public schools has grown from about 81 percent to more than 86.2 percent today, due to the revenues produced by their assigned parcels. Over that same time, nearly all other beneficiaries have seen their percentage shares shrink fractionally, as their land parcels have been less productive on a relative basis. Other beneficiaries generally retain or grow their overall fund values even at smaller percentages however, due to LGPF corpus growth.

On the chart below SIC projects that under this proposal, a 6 percent distribution rate for the permanent school fund will not hinder the continued growth of the LGPF, at least on a nominal basis, during the next quarter century, assuming reasonable continued inflows to the LGPF from New Mexico's extractive resources. That factor, like an expectation of average 7 percent investment returns, while likely, cannot be guaranteed. It is important to note that the LGPF does not receive any revenues from renewable energy sources, which clearly appear to be a substantial and growing source for meeting future global energy demands.

SIC used the following assumptions in developing this projection: initial additional drawdown begins in FY23, 7 percent gross returns annually, inflows of $887 million (most recent 3-year average) for the next 10 years, $705 million (most recent 5-year average) for the next 7 years and $643 million (most recent 10-year average) thereafter. The additional 1 percent draw-down from the permanent school fund will effectively result in an additional 0.86 percent distribution in early years, with slightly lesser percentage draw as years pass and the permanent school fund's share of the total LGPF shrinks. This percentage shrinkage rate can be affected by both revenue produced by beneficiary parcels and other offsetting factors like positive or negative investment returns.

Calendar Year	Corresponding Fiscal Year	LGPF Value ($B) at CY-end at current 5.0%	LGPF Distribution @5.0%	LGPF Value ($B) at CY-end w/SJR1 (6.0% SPF)	LGPF Distribution including SJR1	Compounded Difference between 5% & SJR1 Distribution	Difference in LGPF Value ($B)
2020	**2022**	21.599	$908,375,136	21.599	$908,375,136	$0	**$0.000**
2021	**2023**	23.061	$987,269,621	23.061	$1,157,079,995	$169,810,374	**$0.000**
2022	**2024**	24.545	$1,059,838,673	24.460	$1,241,135,836	$351,107,537	**($0.085)**
2023	**2025**	26.053	$1,149,826,353	25.787	$1,343,482,147	$544,763,331	**($0.266)**
2024	**2026**	27.581	$1,228,392,734	27.109	$1,430,036,482	$746,407,079	**($0.471)**
2025	**2027**	29.127	$1,303,667,937	28.426	$1,510,046,894	$952,786,036	**($0.701)**
2026	**2028**	30.699	$1,380,050,200	29.747	$1,585,702,952	$1,158,438,788	**($0.952)**
2027	**2029**	32.301	$1,457,609,707	31.080	$1,663,150,264	$1,363,979,345	**($1.221)**
2028	**2030**	33.933	$1,536,412,943	32.425	$1,740,810,317	$1,568,376,719	**($1.509)**
2029	**2031**	35.597	$1,616,574,208	33.782	$1,818,880,439	$1,770,682,950	**($1.815)**
2030	**2032**	37.293	$1,698,232,438	35.153	$1,897,582,152	$1,970,032,664	**($2.140)**
2031	**2033**	38.839	$1,779,628,039	36.355	$1,971,509,789	$2,161,914,414	**($2.484)**
2032	**2034**	40.407	$1,860,686,433	37.561	$2,047,209,560	$2,348,437,541	**($2.846)**
2033	**2035**	41.999	$1,941,342,467	38.773	$2,121,359,437	$2,528,454,511	**($3.226)**
2034	**2036**	43.617	$2,021,542,424	39.992	$2,193,886,283	$2,700,798,370	**($3.625)**
2035	**2037**	45.263	$2,101,246,290	41.218	$2,264,734,226	$2,864,286,306	**($4.045)**
2036	**2038**	46.939	$2,182,250,404	42.456	$2,331,994,789	$3,014,030,691	**($4.483)**
2037	**2039**	48.647	$2,264,653,613	43.707	$2,403,657,478	$3,153,034,556	**($4.940)**
2038	**2040**	50.326	$2,347,924,888	44.910	$2,475,218,929	$3,280,328,597	**($5.416)**
2039	**2041**	52.035	$2,432,102,592	46.123	$2,546,710,985	$3,394,936,990	**($5.912)**
2040	**2042**	53.774	$2,517,214,489	47.345	$2,618,150,120	$3,495,872,621	**($6.429)**
2041	**2043**	55.545	$2,603,276,240	48.578	$2,684,922,106	$3,577,518,487	**($6.967)**
2042	**2044**	57.350	$2,690,299,160	49.824	$2,756,126,926	$3,643,346,253	**($7.525)**
2043	**2045**	59.188	$2,778,919,257	51.085	$2,827,997,060	$3,692,424,056	**($8.103)**
2044	**2046**	61.062	$2,869,193,702	52.358	$2,900,577,952	$3,723,808,306	**($8.704)**
2045	**2047**	62.972	$2,961,176,107	53.645	$2,973,909,089	$3,736,541,288	**($9.327)**
2046	**2048**	64.919	$3,054,916,070	54.945	$3,042,786,236	$3,724,411,454	**($9.974)**
2047	**2049**	66.904	$3,150,458,603	56.261	$3,117,584,168	$3,691,537,019	**($10.643)**
2048	**2050**	68.927	$3,247,843,489	57.593	$3,193,214,304	$3,636,907,834	**($11.333)**
2049	**2051**	70.989	$3,347,107,744	58.940	$3,269,689,681	$3,559,489,771	**($12.049)**
2050	**2052**	73.090	$3,448,288,513	60.300	$3,347,022,457	$3,458,223,715	**($12.790)**

The fiscal impact table assumes voters approve the amendment in the next general election (November 2022) and that Congressional approval is granted by July 1, 2022. Depending on the timing of potential voter approval of the constitutional amendment, it is possible for additional distributions to begin sooner.

The additional distribution will provide another $170 million to public schools for teacher salaries and instruction purposes in the first year of implementation. The proposal does not contain a delayed repeal date; therefore, the additional 1 percent distribution from the permanent school fund would continue into perpetuity.

Increasing the distribution rate results in more common school fund revenue in the short term, but reduces the total value of the fund. Doing so limits the fund's ability to grow over time and reduces the general fund distributions in the long term. SIC states that after 25 years of additional distributions, public schools will have received approximately $3.7 billion to LGPF beneficiaries relative to a 5 percent distribution, but also would have cost the LGPF roughly $10 billion in lost earnings. At a 5 percent distribution rate, that $10 billion would have delivered additional annual revenue of around $500 million.

The impact of an additional 1 percent distribution of the permanent school fund can also be swayed substantially by investment returns and annual revenue inflows to the permanent fund, which are driven primarily by oil and gas royalties. Put simply, higher oil and gas inflows to the

LGPF and higher than expected investment returns significantly help mitigate the long-term effects of spending additional investment earnings through an increased drawdown. However, the opposite holds true as well, where depressed oil and gas prices, coupled with lower investment returns (which many predict over the next decade), and a higher spending rate have a greater potential to negatively impact the growth of the endowment and distributions from the fund over the long-term.

Regarding the trade-off of the additional benefits of an increased distribution now versus a higher distribution from a higher corpus fund later, SIC staff offer the following:

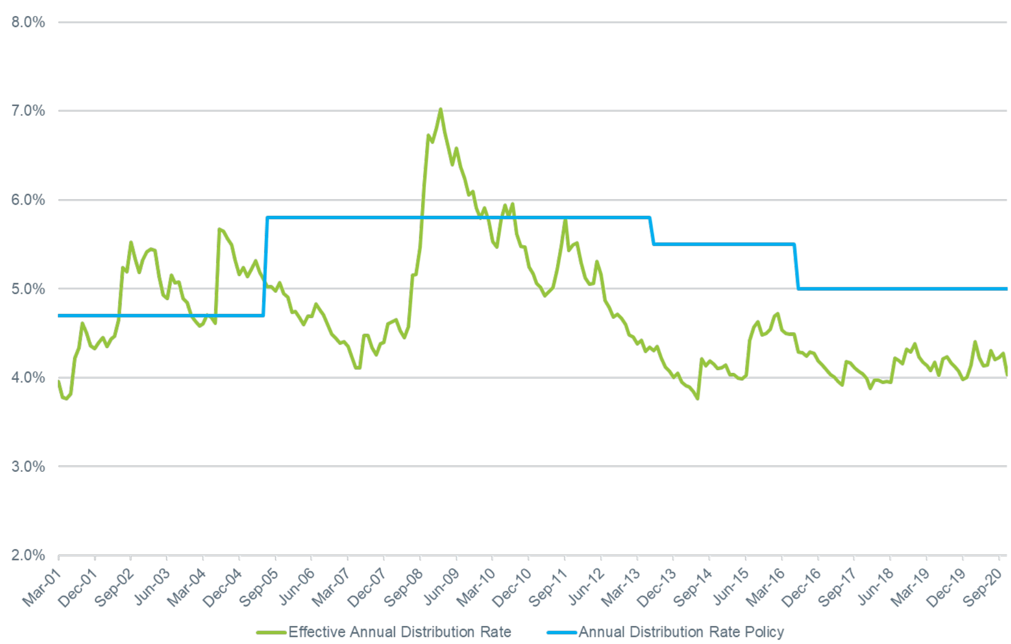
> "From a long-term, multi-decade perspective, there is also an unavoidable conclusion that an endowment fund like the LGPF that distributes 5 percent of its corpus will ultimately deliver more money to NM education overall than a fund distributing 6 percent. This is due to the power of compounding interest, which on a long-term basis will create a larger endowment at the lower spending rate, due to increased investment gains over time. The question as to whether spending an additional amount from the fund today can help satisfy current (and future) needs of New Mexico via creation of greater returns in human capital, remains a matter of public policy, and will likely hinge on execution of an effective plan over time."

Constitutional Amendment. Under Section 1-16-4 NMSA 1978 and the New Mexico constitution, the SOS is required to print samples of the text of each constitutional amendment, in both Spanish and English, in an amount equal to ten percent of the registered voters in the state. The SOS is also required to publish them once a week for four weeks preceding the election in newspapers in every county in the state. The estimated cost per constitutional amendment is $150 thousand-$200 thousand depending upon the size and number of ballots and if additional ballot stations are needed.

SIGNIFICANT ISSUES

Intergenerational Equity. SIC has periodically used an "intergenerational equity index" to assess the long-term health of each of its permanent funds. The index – like long-term projections - is not overly precise and can show volatility at times. It uses a score out of 100 to represent balance between generations. The index is best for identifying trends over time, rather than a specific year's score. In 2019, the LGPF rose to a score of 57/100, indicating a slight overweighting to future generations over current ones. However, in 2020 – pre-pandemic, and boosted by record inflows strong investment returns and lower than historic inflation expectations – the index spiked to 79/100. SIC stated the council will reassess this figure and see whether the trend continues in 2021.

Distributions as a Percent of the Five-Year Average. It has been discussed that due to the use of a 5-year rolling average to determine what distributions will be for the fiscal year starting six months after the end of year valuation (and ending 18 months after that mark), the 5 percent is in fact "below 5 percent" by the time the percentage of the 5-year rolling average amount is deployed as much as 17 months later. This statement, taken using a snapshot in time, is technically correct – as long as the fund is growing as the LGPF currently is. Should the fund's value be falling over a multi-year period, the reverse would apply, and resulting in a distribution rate higher than 5 percent based on current market values. The following chart provided by SIC below illustrates this historically.



SIC notes that using a 5-year rolling average of the fund value to determine a spending/distribution policy is standard among permanent funds and endowments; and therefore, New Mexico is not an outlier. The average is used to assist policy-makers better plan and avoid significant drops in year-over-year distributions.

Teacher Salaries. Despite significant investments to New Mexico teacher pay in recent years, other neighboring states have also increased teacher compensation at a similar rate. As such, average teacher salaries in the region have effectively remained the same, comparatively. Notably, Texas and Oklahoma have statewide minimum new teacher salary levels of $33.6 thousand and $36.6 thousand, respectively – making New Mexico's starting minimum salary of $41 thousand the highest in the region.

PED and the Higher Education Department (HED) recently released the educator accountability reporting system (EARS) annual report for 2018 (the last published EARS report was in 2015). Statutorily, PED and HED are required to publish an annual EARS report to examine trends in educator preparation programs (EPP) across the state. In FY18, in-state EPPs produced 718 teachers, a decrease of 91 teachers or 11 percent from the prior year. Only two-thirds of these in-state EPP completers (about 480 teachers) taught in New Mexico after graduation. In FY18, PED issued 2,749 individuals their initial teacher credentials, suggesting more than 80 percent of new teachers were alternatively certified or hired from out-of-state programs.

Education Sufficiency Lawsuits. On February 14, 2019, the 1st Judicial District Court issued a final judgment and order on the consolidated *Martinez v. New Mexico* and *Yazzie v. New Mexico* education sufficiency lawsuits, and found that New Mexico's public education system failed to provide a constitutionally sufficient education for at-risk students, particularly English language learners, Native American students, and special education students. The court's findings suggested overall public school funding levels, financing methods, and PED oversight were deficient. As such, the court enjoined the state to provide sufficient resources, including instructional materials, properly trained staff, and curricular offerings, necessary for providing the opportunity for a sufficient education for all at-risk students.

Additionally, the court noted the state would need a system of accountability to measure whether the programs and services actually provided the opportunity for a sound basic education and to assure that local school districts spent funds provided in a way that efficiently and effectively met the needs of at-risk students. However, the court stopped short of prescribing specific remedies and deferred decisions on how to achieve education sufficiency to the legislative and executive branch instead.

Public School Funding. The Legislature allocates $3.2 billion, or 45 percent of general fund appropriations, to public schools annually, along with about half a billion dollars in federal revenues for public education expenses. According to the U.S. Census Bureau's 2018 Annual Survey of School System Finances, New Mexico ranks fourth in the nation for the share of school revenue attributable to state sources by providing over two-thirds of every dollar to schools for their operations and capital expenses. Although the state has an enormous role in funding public schools, New Mexico school districts and charter schools exercise significant local control over budget priorities and programs, similar to schools in other states that rely more heavily on local property taxes. While a local governance and state financing model offers schools more flexibility to address unique regional circumstances, this structure can complicate efforts to implement uniform standards or programs statewide.

Between FY17 and FY20, the Legislature increased recurring public school appropriations by nearly $567 million, or 21 percent, and planned to increase appropriations by another $206 million, or 6.4 percent, in FY21. However, precipitous declines in state revenue forced the Legislature to revise budgets downward, resulting in public school general fund appropriations returning back to FY20 funding levels. Although federal CARES Act funding provided $108 million to help New Mexico schools defray costs related to the Covid-19 health emergency, the transition to remote and hybrid learning highlighted inefficiencies from centralized control and revealed stark disparities in local capacity to deliver educational services to all students.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Conflicts with House Joint Resolution 1, which adds a 1 percent distribution from the LGPF for all beneficiaries, and adds a beneficiary of the permanent school fund by dedicating the additional distribution for early childhood educational services.

TECHNICAL ISSUES

This bill does not contain a delayed repeal date. LFC recommends adding a delayed repeal date.

OTHER SUBSTANTIVE ISSUES

LGPF Beneficiaries. The chart below lists the 21 existing beneficiaries of the LGPF as determined by the federal Enabling Act of 1910 and the Ferguson Act of 1898, and the percentage of the distributions they receive on a monthly basis.

Land Grand Permanent Fund (LGPF) Beneficiaries Percent distribution as of December 1, 2020	
COMMON SCHOOLS	86.247%
UNIVERSITY OF N.M	1.189%
UNM SALINE LANDS	0.041%
N.M. STATE UNIVERSITY	0.364%
WESTERN N.M. UNIVERSITY	0.022%
N.M. HIGHLANDS UNIVERSITY	0.022%
NO. N.M. COLLEGE	0.018%
EASTERN N.M. UNIVERSITY	0.067%
N.M INST. MINING & TECH	0.166%
N.M. MILITARY INSTITUTE	2.832%
N.M. BOYS SCHOOL	0.005%
DHI MINERS HOSPITAL	0.768%
N.M. STATE HOSPITAL	0.330%
N.M. STATE PENITENTIARY	1.709%
N.M. SCHOOL FOR THE DEAF	1.687%
SCH. FOR VISUALLY HAND.	1.683%
CHARITABLE PENAL & REFORM	0.680%
WATER RESERVOIR	0.852%
IMPROVE RIO GRANDE	0.190%
PUBLIC BUILDINGS	1.127%
CARRIE TINGLEY HOSPITAL	0.001%
Total	100%

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ATTACHMENT 1 – LGPF Quick Facts

What is the Land Grant Permanent Fund?

- Established in 1912 through New Mexico's entry into statehood.
- Tied to the federal Enabling Act of 1910, which stipulated that such land grants were to be held in trust for the benefit of the public schools, universities, and other specific beneficiary institutions.
- Oil and gas revenues (rents, royalties, and bonuses) make up over 90 percent of contributions to the fund – 2020 contributions totaled about $918 million.
- One of the largest sovereign wealth funds in the country – currently about $21.6 billion.
- General fund distributions are earmarked for public schools.

Current Distributions from LGPF

Currently, 5 percent of the LGPF five-year average is distributed to 21 beneficiaries of the fund based on land-ownership. The general fund (earmarked for common schools) is the largest fund beneficiary, receiving approximately 85 percent of the distribution. Other beneficiaries include universities, hospitals, and other public institutions. In FY21, LGPF distributions to the general fund for public schools will be about $674 million.

Distribution History

- Originally, only interest earnings were distributed to beneficiaries.
- 1996, voters passed a constitutional amendment to raise the distribution amount to 4.7 percent of the five-year average value of the fund.
- 2003, by a slim margin (92.2 thousand for, 92.0 thousand against), voters passed a constitutional amendment to:
  - Raise the annual distribution to 5 percent,
  - Provide an additional distribution of 0.8 percent from FY06 – FY12 (totaling 5.8 percent),
  - Reduce the additional distribution to 0.5 percent from FY13 – FY16 (totaling 5.5 percent),
  - Earmark the general fund portion of the additional distributions to implement educational reforms.
- FY17, the distribution reverted back to 5 percent.

Important Considerations

LGPF was established and is required by law to benefit public schools and other beneficiaries indefinitely. It is funded by income from non-renewable resources and was designed to provide for future generations of New Mexicans even when those resources are exhausted.

As the fund grows, distributions grow.

- While increasing the distribution rate results in more general fund revenue in the short term, doing so reduces the total value of the fund, limiting the funds' ability to grow and reducing the general fund distributions in the long term.
- If the 2003 amendment to LGPF were never passed, the fund would have been $1.5 billion greater in FY18. For CY17 an additional $1.5 billion would have generated another $223 million in net earnings for the fund.
- ***The "Tipping Point"*** - By 2017, distributions to the general fund were smaller than they would have been if the 2003 amendment had never occurred. If the distribution had never increased from 4.7 percent, the annual general fund distribution would have been about $20 million higher in FY17 and $25 million higher in FY18. The original FIR for this legislation (SJR6, 2013) accurately projected the timeframe of this tipping point.