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

SPONSOR	Sanchez, M.	ORIGINAL DATE	02/06/14	LAST UPDATED	02/17/14	HB	
SHORT TITLE	Public Money Water Project Changes					SB	198/aSRC
						ANALYST	Kehoe/Canney

### APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Nonrecurring	Fund Affected
FY14	FY15		
	\$750.0	Recurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

Relates to Senate Bills 20, 42, 65, 112, 295, and 324; and House Bills 55, 146, and 299

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

New Mexico Environment Department (NMED)  
Energy Minerals & Natural Resources Department (EMNRD)  
New Mexico Finance Authority (NMFA)  
Office of the State Engineer/Interstate Stream Commission (OSE/ISC)  
Department of Finance & Administration (DFA)

### SUMMARY

#### Synopsis of SRC Amendment

The Senate Rules Committee amendment requires that the Water Trust Board, following recommendations by the technical review team, must take into consideration all regions of the state when making funding-relating decisions.

#### Synopsis of Original Bill

Senate Bill 198 appropriates \$750 thousand from the general fund to the Office of the State Engineer for the purpose of creating a new Water Trust Office, as an adjunct agency. The new office is to be overseen and directed by the Water Trust Board (WTB). The purpose of the newly created office is to require all state agencies that fund or administer water projects to participate in a unified process intended to provide effective planning and effective use of the state's monetary resources and coordinating the water application process. The bill amends the

New Mexico Water Project Finance Act, New Mexico Finance Authority Act, Tribal Infrastructure Act, Colonias Infrastructure Act, New Mexico Community Assistance Act, Rural Infrastructure Act, Wastewater Facility Loan Construction Act, the Drinking Water State Revolving Loan Act, and the Severance Tax Bonding Act.

The bill expands eligible “water projects” to include the following:

- (a) storage, conveyance or delivery of water to end users;
- (b) wastewater treatment, collection and disposal;
- (c) recoverable water, including brackish water, produced water, gray water and wastewater reuse;
- (d) implementation of federal Endangered Species Act of 1973 collaborative programs;
- (e) restoration and management of watersheds;
- (f) flood control; or
- (g) water conservation or recycling, treatment or reuse; and eligible projects are further clarified as, “a project for which the service area is wholly within the boundaries of the state, or is determined by the water trust board, to be an interstate water project that directly benefits New Mexico.”

The amendments to the Water Project Finance Act change the powers and duties of the Water Trust Board (WTB), the appointing powers for certain members, and requires the board to develop a standardized application form and process for funding water projects; and develop funding requests for the Legislature and the governor for capital outlay funds. An “Interagency Technical Review Team” (Team) is created and is composed of state agencies currently responsible for administering water projects, including the NMFA. The Team will be responsible for developing the full funding package of the appropriate combination of service rates, federal, state, local and private loans, grants, and matching funds.

The revisions require that all programs under the Act submit eligible water projects to the Water Trust Board for evaluation, and prioritization of all water projects to be funded from all state administered funds. A section of the bill establishes threshold requirements for evaluations of water project applications, including compliance with the State Audit Act, appropriate rate and governance structures, and provides that if applicants fail to meet the thresholds, the “team” is required to work with applicants for the next application cycle.

Other duties of the WTB are as follows:

- Requires the WTB to publish a schedule of water project request deadlines each year;
- Mandates that an applicant can only submit one application,
- Sets out a process for the Team to evaluate applications,
- Requires a qualifying water project to fund a whole project or a project phased so that each phase stands on its own,
- Places the burden on the Team to develop the full funding package of the appropriate combination of service rates, federal, state, local and private loans, grants and matching funds before ranking a water project as a priority for the WTB’s consideration,
- Requires the WTB to submit tentatively adopted projects to the state agencies or other entities from which funding are sought for approval or denial. If denied, the WTB can consider other funding mixes, change its priority ranking, or reject the application, and
- Based on recommendations from the technical review team and feedback from the agencies and others, the board shall make its final decisions on priority ranking of applications, funding sources, and project conditions.

A new section of the Water Project Finance Act requires the WTB to develop a statewide comprehensive multi-year water capital plan to be updated at least bi-annually.

WTB members increased from 16 to 18, increasing the public membership from five to seven members. The public membership shall be appointed by the Legislative Council rather than by the governor. The two new public members would represent water associations organized under the Sanitary Projects Act and a representative of the colonias. The representative appointed by the president of the Navajo Nation must be a representative of the Navajo Nation that lives in New Mexico. The bill removes the executive directors of the New Mexico Municipal League and the New Mexico Association of Counties from the board and only requires a representative of statewide associations representing municipalities and counties to be represented on the board.

The effective date of this bill is July 1, 2014.

### **FISCAL IMPLICATIONS**

The appropriation of \$750 thousand contained in this bill is a recurring expense to the general fund. Any unexpended or unencumbered balance remaining at the end of fiscal year 2015 shall revert to the general fund.

The Office of State Engineer reported that a recurring source of funding for continued operation and administration of the Water Trust Office is not proposed or identified.

Regarding the change in statute for the Water Trust Fund, the Office of the State Engineer reported that The State Investment Council has determined the Water Trust Fund will run out of money by approximately 2033 under present operations. Lowering the annual distribution was one recommendation to prolong the life of the fund. Lowering the distribution will also adversely affect the budget of the Office of the State Engineer (OSE) intended to accelerate water right adjudications that currently receives 10 percent of the annual distribution from the Trust Fund. A reduction below \$4M will have budget and progress implications to the statewide adjudication process.

There is no provision within the bill as to who would service the outstanding WTB loans or how the service would be funded. During fiscal year 2013, the NMFA disbursed \$42.0 million of grants and disbursed \$6.4 million of loans. In addition, new obligations of \$25.4 million were tracked from application to board approval. The costs that were incurred and charged for these activities, exclusive of direct project and memorandum of understanding costs, were \$730 thousand including the overhead indirect costs of processing requisitions, preparing budgets, tracking budgets, human resource services, and informational technology.

### **SIGNIFICANT ISSUES**

Section 1 of the bill lists findings by the Legislature similar to those in an August 2007 *LFC Hearing Brief* which identified the fragmentation of programs as the fundamental problem for New Mexico's infrastructure process. With no less than seven separate funding programs for water projects, few share resources or coordinate funding to maximize financing. To date, the fragmentation still exists and the root causes include:

- Programs continue to operate independently of each other;
- Programs compete for the same customers;
- Funding comes from different sources and have widely different eligibility criteria;
- A long-term statewide capital plan is not centrally coordinated; and

- No single agency is held accountable for a coordinated and centralized reporting function.

The LFC Program Evaluation of the Water Trust Board, “*A Review of Planning, Spending, and Outcomes*”, dated November 21, 2013, included five key recommendations to address water program fragmentation. The recommendations state the Water Trust Board should: 1) establish a centralized funding process for funding water projects statewide through collaboration by all water funding programs; and 2) require the use of a single uniform funding application process to serve all taxpayers requesting water-related funding, to be accessed by all water funding agencies; and that the Legislature should: 1) require the use of a single application process for all water infrastructure projects through a uniform funding application process to serve all applicants as well as all funding agencies for water programs; 2) establish a single, interagency committee responsible for coordinating all water funding programs for water infrastructure projects and require a centralized reporting process to measure effectiveness; and 3) require a statewide, comprehensive, multi-year capital plan for water projects.

Senate Bill 198 addresses and accommodates all five of the recommendations and tasks the Water Trust Board with providing the necessary interagency coordination. The bill requires the Water Trust Board to establish a standardized water project application form that would be used by all entities applying for state-administered water funding programs. Once the uniform applications are received by the Water Trust Office, they are reviewed and prioritized by the technical review team using Water Trust Board criteria, which is aligned with the principals of 2005 House Joint Memorial 86 as well as the State Water Plan. Each water project application results in a priority ranking and recommendation for funding package to leverage available sources of funds. The bill provides detailed requirements for the proposed Water Trust Office to make periodic and annual reports to interim committees, the Legislature, and the governor, providing the centralized reporting process that is currently lacking.

The bill further addresses each funding program’s statutory requirements, limiting changes only to water projects, while improving coordination and centralized planning. The programs affected the most include the public project revolving loan fund, the colonias project fund, the tribal infrastructure fund, the Rural Infrastructure Program, clean water state revolving fund, and the drinking water state revolving fund.

The NMFA analysis identified the following significant issues: 1) the bill “removes legislative authorization for projects funded from the water project fund and for water project loans made from the public project revolving fund; 2) having multiple decision makers, namely the WTB, the interagency team and other agencies where funding might reside, regarding approval of water projects raises concerns regarding appeals raised from qualified entities and potential due process issues; and 3) raises inefficiency issues amongst several agencies because of administrative overlapping of duties, such as grant and loan servicing and monitoring.

According to NMFA, the bill broadens the use of eligible programs to which the legislature may appropriate portions of the governmental gross receipts tax after bond payments are made. Currently, NMFA uses these funds to make loans at below market interest rates to borrowers with low median household incomes. The legislature regularly appropriates these funds to the local government planning fund and the drinking water state revolving fund. Additional appropriations out of the governmental gross receipts tax could curtail appropriations to these funds and impact funding to small, disadvantaged communities.

The New Mexico Environment Department (NMED) reported that the review and ranking process would drastically slow down the funding process to communities, leaving communities vulnerable and without recourse when in need of quick funding or for emergencies.

NMED also provided the following:

“The purpose of the Drinking Water State Revolving Loan Fund (DWSRLF) is to provide local authorities in New Mexico with low-cost financial assistance in the construction and rehabilitation of necessary drinking water facilities through the creation of a self-sustaining revolving loan program so as to improve and protect drinking water quality and public health.” Senate Bill 198 proposes that the loan recipients will be subject to the Water Trust Board’s priorities *and* that they must be in compliance with Safe Drinking Water Act requirements. This proposed change undermines the original purpose of the DWSRLF Act in that it suggests only water systems already in compliance will be awarded financial assistance. The purpose of the DWSRLF is to increase the number of compliant systems in New Mexico by providing an affordable loan program and capacity development assistance to rehabilitate drinking water systems. The number of systems out of compliance would likely increase with the implementation of Senate Bill 198, thereby decreasing NMED performance measures that track the number of systems providing safe, clean drinking water.”

The Energy, Minerals & Natural Resources Department (EMNRD) states its specific concern of the bill is “the provision that includes the “restoration and management of watersheds” as a category of “water project” that will be controlled by the Water Project Finance Act. Currently, EMNRD’s State Forestry Division has long-established application and priority ranking procedures in place for watershed health projects with federal, state and local agencies. Further, these protocols have served the programs well over the years and incorporate trained staff that are fully cognizant of the interagency rules, policies and procedures. EMNRD has not sought funding from the Water Trust Board for watershed projects in the past.” According to NMFA, since 2007, the WTB has funded \$18.6 million, or eight percent of total projects funded, for watershed projects.

## **ADMINISTRATIVE IMPLICATIONS**

The EMNRD indicates the extra steps necessary for the “water technical review team” to review and rank applications then submit the rankings to the water trust board for review and ranking could delay the process, thus increasing levels of unassigned obligations within the funds and could delay the local community and rural projects.

The Office of the State Engineer stated that sixteen members is a cumbersome number and adding to that will only increase the difficulty of conducting business.

## **RELATIONSHIP**

Senate Bill 20 and Senate Bill 162 create the Capital Outlay Planning and Monitoring Act for the purpose of increasing fiscal accountability and programmatic scrutiny of capital outlay projects and expenditures.

## **Senate Bill 198/aSRC – Page 6**

House Bill 55 authorizes approximately \$112.4 million from severance tax bond capacity, and approximately \$64 million from other state funds for the purpose of funding various capital outlay projects statewide.

House Bill 146 makes several changes to the Severance Tax Bonding Act that would reduce capacity for severance tax bonds and notes while increasing the amount of severance tax revenue that flows to the Severance Tax Permanent Fund (STPF).

House Bill 299 amends the Water Finance Act to provide that at least 10 percent of funds transferred to the water project fund for water projects each year be expended to benefit water supply associations subject to the Sanitary Projects Act and acequia associations.

Senate Bill 42 appropriates \$18 million from the general fund to the water trust fund for the purpose of carrying out the purpose of the fund.

Senate Bill 65 amends Section 72-4A-4 NMSA 1978 that creates the Water Trust Board. The board is composed of 16 members. Current legislation states that the board chair be elected by a quorum of board members but does not designate any particular members. The bill adds that the chair shall be elected from the public members.

Senate Bill 112, for the New Mexico Finance Authority Oversight Committee, authorizes the NMFA to make loans or grants for 120 projects from the water project fund and to make grants to five acequia projects from the acequia project fund. The loans or grants are based on terms and conditions established by the Water Trust Board (WTB) and the NMFA in accordance with the Water Finance Act.

Senate Bill 295 and Senate Bill 324 amends the Water Project Finance Act to remove the adjudication set-aside of 10 percent of all Water Project Fund dollars annually dedicated to the Office of the State Engineer and the administrative office of the courts and inserts an annual allocation of only the severance tax bonding capacity funds deposited into the Water Project Fund be transferred to the Natural Heritage Conservation Fund for forest and watershed restoration projects.

## **TECHNICAL ISSUES**

According to the NMFA, any transfer that would occur would require a significant amount of planning, time, and system implementation for the tracking and servicing of the existing \$20 million loans and approximately \$40 million annual grant disbursements.

Transfer and servicing of existing loans, grants and obligations would require new staff training and potentially raise audit concerns.

The Office of the State Engineer reported that many of the new requirements are already included in Water Trust Board rules and policies. For example, the technical review team is already used to review and rank projects for the WTB and many of the minimum threshold requirements are already listed in the WTB rules and policies.

**OTHER SUBSTANTIVE ISSUES**

The bill removes Water and Natural gas Associations as qualified entities.

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