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

ORIGINAL DATE 1/23/18
SPONSOR Ely **LAST UPDATED** 2/9/18 **HJR** 2

SHORT TITLE Land Grant Fund for Public Safety, CA **SB**

ANALYST Iglesias

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY18	**FY19**	**FY20**	**FY21**	**FY22**		
$0.0	$0.0	($79,512.0)	($83,724.0)	($88,109.0)	Recurring	LGPF
$0.0	$0.0	$67,585.0	$71,165.0	$74,893.0	Recurring	General Fund (education)
$0.0	$0.0	$11,926.0	$12,559.0	$13,216.0	Recurring	Other LGPF beneficiaries

Parenthesis ( ) indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

FY18	FY19	FY20	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
	$50.0		$50.0	Nonrecurring	Election Fund

Parenthesis ( ) indicate expenditure decreases

Related to HJR1, HJR3, SJR2, SJR3, SJR7

SOURCES OF INFORMATION
LFC Files

Responses Received From
State Investment Council (SIC)
NM Attorney General's Office (NMAG)
State Land Office (SLO)
Administrative Office of the District Attorneys (AODA)
Children, Youth and Families Department (CYFD)

Responses Not Received From
Department of Public Safety (DPS)
New Mexico Corrections Department (NMCD)
Administrative Office of the Courts (AOC)

SUMMARY

Synopsis of Bill

House Joint Resolution 2 proposes an amendment to Article 12, Section 7 of the Constitution to provide additional annual distributions of one-half percent of the average of the year-end market value of the Land Grant Permanent Fund (LGPF) for the immediately preceding five calendar years, for the purposes of funding criminal justice and public safety, including education programs, law enforcement, district attorneys, public defenders, courts, correctional facilities and programs, pre-trial and post-trial services, and behavioral health/substance abuse programs. The additional funding will only be deployed from the LGPF should the balance of the five-year average of the LGPF exceed $15 billion.

The constitutional amendment requires approval by voters in a statewide election, either in the 2018 general election or at a special statewide election held for this purpose. Subsequent approval by the U.S. Congress is also required before the amendment can be enacted.

FISCAL IMPLICATIONS

Land Grant Permanent Fund

This bill does not indicate how the new distribution might interact with or override the existing distributions to the LGPF beneficiaries. However, assuming adoption by voters, and resolution of complex legal and constitutional obstacles the bill appears to entail, this bill would deliver significant revenue from the LGPF to the state in coming years, to address a wide-ranging number of budgetary challenges related to crime, the justice system, the corrections system, behavioral health and related societal ills. The State Investment Council, however, notes that funding comes at a premium and ultimately reduces the effectiveness of the endowment as well as the total dollars the LGPF can generate for New Mexicans.

The State Investment Council indicates that, unlike general fund dollars, permanent fund dollars carry a greater implied value of not only their current dollar denomination, but also the investment earnings that dollar will produce for every subsequent year it is invested. Like most endowment dollars, there is a reasonable expectation that a dollar in the LGPF will double in value after about 10 years, assuming average earnings of around 7 percent (the fund’s current target rate of return). SIC states, if a LGPF dollar is spent rather than invested, it cannot compound its value over time, and cannot contribute to future generations of NM citizens. This is one of the reasons university endowments, foundations, trusts, permanent funds, sovereign wealth funds and similar entities typically limit their distribution rate, or spending policy, to an annual rate of 5 percent or less.

Though only taking an additional one-half of one-percent, this bill would deliver more than a billion dollars to the state over the first 12 years of its existence, but not without accompanying hundreds of millions of dollars in “opportunity cost” that comes from spending those dollars rather than investing them.

SIC provides the following chart, which tracks the first 30 years of additional distributions from the LGPF pursuant to this legislation:

Calendar Year	Corresponding Fiscal Year	($B) LGPF Value Current (5%)	LGPF Distribution @5%	($B) LGPF Value w/HJR2 (5.5%)	LGPF Distribution @5.5%	Compounded Difference in 5% & 5.5% LGPF Distribution	Difference in LGPF Value ($B)
2017	2019	17.25	$747,170,300				
2018	**2020**	18.20	$795,345,513	18.20	$874,857,381	$79,511,868	($0)
2019	**2021**	19.17	$841,966,786	19.13	$925,691,039	$163,236,121	**($0.04)**
2020	**2022**	20.17	$899,596,558	20.04	$987,705,664	$251,345,227	**($0.13)**
2021	**2023**	21.18	$959,722,158	20.96	$1,051,426,904	$343,049,973	**($0.22)**
2022	**2024**	22.22	$1,009,418,117	21.90	$1,102,533,208	$436,165,064	**($0.32)**
2023	**2025**	23.28	$1,060,212,308	22.84	$1,153,588,973	$529,541,729	**($0.44)**
2024	**2026**	24.37	$1,112,213,477	23.81	$1,205,056,356	$622,384,608	**($0.56)**
2025	**2027**	25.49	$1,165,469,531	24.80	$1,257,387,799	$714,302,876	**($0.69)**
2026	**2028**	26.64	$1,220,066,687	25.81	$1,310,698,336	$804,934,525	**($0.83)**
2027	**2029**	27.83	$1,276,151,656	26.85	$1,365,171,668	$893,954,537	**($0.98)**
2028	**2030**	29.05	$1,333,827,400	27.91	$1,420,932,309	$981,059,446	**($1.14)**
2029	**2031**	30.30	$1,393,141,924	29.00	$1,478,030,204	$1,065,947,726	**($1.30)**
2030	**2032**	31.59	$1,454,141,971	30.11	$1,536,506,349	$1,148,312,104	**($1.48)**
2031	**2033**	32.92	$1,516,873,242	31.26	$1,596,396,711	$1,227,835,573	**($1.66)**
2032	**2034**	34.28	$1,581,380,537	32.42	$1,657,734,587	$1,304,189,623	**($1.86)**
2033	**2035**	35.68	$1,647,708,409	33.62	$1,720,551,686	$1,377,032,900	**($2.06)**
2034	**2036**	37.12	$1,715,901,951	34.85	$1,784,879,360	$1,446,010,309	**($2.27)**
2035	**2037**	38.60	$1,786,007,134	36.10	$1,850,749,193	$1,510,752,368	**($2.50)**
2036	**2038**	40.12	$1,858,070,895	37.39	$1,918,193,177	$1,570,874,650	**($2.74)**
2037	**2039**	41.69	$1,932,141,198	38.70	$1,987,243,807	$1,625,977,259	**($2.99)**
2038	**2040**	43.29	$2,008,267,083	40.05	$2,057,934,150	$1,675,644,326	**($3.25)**
2039	**2041**	44.94	$2,086,498,702	41.43	$2,130,297,881	$1,719,443,505	**($3.52)**
2040	**2042**	46.64	$2,166,887,353	42.84	$2,204,369,305	$1,756,925,457	**($3.80)**
2041	**2043**	48.38	$2,249,485,502	44.28	$2,280,183,373	$1,787,623,328	**($4.10)**
2042	**2044**	50.17	$2,334,346,811	45.76	$2,357,775,697	$1,811,052,214	**($4.42)**
2043	**2045**	52.01	$2,421,526,169	47.27	$2,437,182,567	$1,826,708,612	**($4.74)**
2044	**2046**	53.90	$2,511,079,714	48.81	$2,518,440,957	$1,834,069,855	**($5.09)**
2045	**2047**	55.84	$2,603,064,862	50.39	$2,601,588,544	$1,832,593,537	**($5.44)**
2046	**2048**	57.83	$2,697,540,340	52.01	$2,686,663,720	$1,821,716,917	**($5.82)**
2047	**2049**	59.88	$2,794,566,206	53.67	$2,773,705,599	$1,800,856,310	**($6.21)**
2048	**2050**	61.98	$2,894,203,887	55.36	$2,862,754,039	$1,769,406,462	**($6.61)**

SIC's projections are based on the following assumptions: estimated value of the LGPF as of December 31, 2017; State Land Office (SLO) contributions of $495 million for CY2018 increasing by 1.5 percent annually; and investment net-of-fee returns of 6.8 percent. The 10- and 15-year average contributions from SLO are $501 million and $440 million respectively, and last calendar year's LGPF contribution was $488 million. LGPF net investment returns for the one-, three-, five-, and 10-year periods ending November 2017 were 15.4 percent, 6.7 percent, 8.9 percent, and 5.2 percent, respectively over those time periods.

The projected differences between the 5 percent distribution rate and the 5.5 percent distribution rate are significant:

- 12-years into the scenario, the LGPF would have delivered an additional $1.1 billion to beneficiaries, earmarked for criminal justice funding. At that time, the LGPF balance would be $1.5 billion less than had the fund been distributed at the base 5 percent rate.
- The difference of $411 million dollars represents the opportunity cost of expending

investment dollars for this purpose. That $411 million dollars would be expected to earn $28 million in year 13, as well as tens of millions more in every subsequent year.

- Looking forward, those estimated revenue losses grow and accelerate, and by fiscal year 2047 – just 27 years into this increased distribution formula – it is projected that the LGPF at that point would have been producing more at the 5 percent rate due to growth of the fund, than the smaller fund would produce at a 6 percent rate.
- By 2047, the LGPF would also have $5.4 billion less in its corpus than it otherwise would if this bill were never passed. An average one-year's earnings on $5.4 billion would be about $370 million.

Other factors can impact these projections significantly, including variance in inflows to the permanent fund from oil and gas royalties, higher or lower than expected rates of investment return, and to a lesser degree the impact of inflation as well as growth of the state's population.

Other points for consideration:

- The most recent constitutional amendment, which increased distributions from the LGPF from 2004-2016, resulted in $747 million dollars of additional distribution over and above the 5 percent base rate.
- This bill does not include a sunset provision as the 2003 constitutional amendment did.
- RVK, an independent fiduciary advisor to the SIC, estimates that had the 2003 constitutional amendment never passed, the LGPF would be $1.5 billion larger today.

The State Land Office (SLO) provides a similar analysis, in which the proposed additional distributions increase the risk that the corpus of the LGPF will be diminished and that less money will be available in future years. The analysis depends on new money contributed by the State Land Office from state trust land royalties and fluctuations in investment returns. SLO's internal financial analysis indicates that if all analytical variables other than the distribution rate were held constant, comparing a 5 percent distribution (current law) to a 5.5 percent distribution (proposed), the total amount distributed would increase by approximately $810 million during the next ten years and would decrease by $2.1 billion over the next fifty years. The analysis indicates that total distributions from the fund would decrease within 27 years if this resolution is enacted and approved. The SLO analysis also indicates that the value of the fund will be approximately $14.9 billion dollars higher in fifty years if current distribution rates remain in place as compared to those proposed in this resolution.

Public Safety

The Administrative Office of District Attorneys (AODA) indicates the resolution itself has no direct fiscal impact on the district attorneys, although if it passes the legislature may provide funding for the district attorneys through use of the land grant permanent funds. For such funding to occur, the resolution must pass, the constitutional amendment it proposes must pass at the next election, the state must get consent of the United States Congress, and if the legislature provides by law to use the funds to pay for the criminal justice and public safety purposes listed in this resolution and chooses to include funding for the district attorneys, funds from the land grant permanent funds will reach the district attorneys.

AODA did not provide information how potential additional funding may be utilized. No responses were received from the Corrections Department, the Department of Public Safety, the Administrative Office of the Courts, or the Children, Youth and Families Department indicating how the additional funding may be utilized.

SIGNIFICANT ISSUES

The New Mexico Attorney General's Office (NMAG) points out the LGPF derives from the *Enabling Act* grant made specifically to support "common schools," with permanent school fund income historically being used to support schools falling within the traditional definition of "common schools" (i.e., compulsory and universal primary and secondary education). Thus, by directing that the additional distributions be for specified public safety purposes, the amendment would significantly expand the range of programs to be supported by the original grant.

NMAG indicates it is possible the beneficiaries of the LGPF would pursue litigation challenging the constitutionality of the additional distributions. The permanent fund is required by law to benefit public schools and other beneficiaries indefinitely. The LGPF is funded by income from non-renewable natural resources and was designed to provide a steady revenue source for future generations of New Mexico children even after those resources are exhausted.

The State Land Office (SLO) states the proposed constitutional amendment would be an unprecedented fundamental change and partial abolition of the trust established in the Enabling Act. Under the *Enabling Act*, the money generated from the leasing and sale of state trust lands is "subject to the same trusts as the lands producing the same," meaning that the money may be used only for the benefit of the beneficiary institution. Use of the money "for any object other than that for which such particular lands . . . were granted or confirmed" constitutes "a breach of trust." (See Enabling Act § 10). For over 100 years, from prior to statehood and up to the present time, the LGPF has been used to generate income to support the state purposes and institutions specified in the *Enabling Act* and the New Mexico Constitution. This would be the first time that LGPF corpus or income was used for some other purpose.

The State Investment Council states, while some of the LGPF beneficiaries arguably have missions related to crime and public safety, the other 16 beneficiaries will likely be hard-pressed to satisfy the scope and requirements of spending their additional distribution windfall for the intended purpose. The five potential beneficiaries with at least a possible connection to criminal justice matters in their core missions currently have a 3.8 percent share of the LGPF distributions, while the other 16 beneficiaries retain more than 96 percent.

Land Grand Permanent Fund (LGPF) Beneficiaries Percent distribution as of Dec. 1, 2017	
COMMON SCHOOLS	85.095328 %
UNIVERSITY OF N.M	1.311620 %
UNM SALINE LANDS	0.045397 %
N.M. STATE UNIVERSITY	0.414673 %
WESTERN N.M. UNIVERSITY	0.024367 %
N.M. HIGHLANDS UNIVERSITY	0.024243 %
NO. N.M. COLLEGE	0.019696 %
EASTERN N.M. UNIVERSITY	0.076008 %
N.M INST. MINING & TECH	0.186236 %
N.M. MILITARY INSTITUTE	3.029412 %
N.M. BOYS SCHOOL	0.005324 %
DHI MINERS HOSPITAL	0.867286 %
N.M. STATE HOSPITAL	0.333710 %
N.M. STATE PENITENTIARY	1.866190 %
N.M. SCHOOL FOR THE DEAF	1.844919 %
SCH. FOR VISUALLY HAND.	1.841087 %
CHAR. PENAL & REFORM	0.769716 %
WATER RESERVOIR	0.968725 %
IMPROVE RIO GRANDE	0.216647 %
PUBLIC BLDGS. CAP. INC.	1.058073 %
CARRIE TINGLEY HOSPITAL	0.001342 %
Total	100 %

PERFORMANCE IMPLICATIONS

The Administrative Office of District Attorneys indicates this resolution itself has no performance implications for the district attorneys. If the amendment is adopted, however, it will provide an additional potential funding source for criminal justice and public safety purposes, including the funding of district attorney's offices.

ADMINISTRATIVE IMPLICATIONS

The State Land Office notes each parcel of state trust land is held for the benefit of a particular beneficiary institution, and the state land office distributions to the LGPF are designated for the benefit of a specified beneficiary institution, based on the land that generated the money. SIC administers the LGPF and makes LGPF distributions to the beneficiaries. While it is clear the proposed constitutional amendment would cause significant administrative changes for the state investment office, it is not clear a change in the law requiring distributions of some portion of the LGPF for non-beneficiary purposes would involve administrative changes and additional burdens for the state land office.

The resolution is silent as to who or what agency would be tasked with determining whether the additional disbursements are qualified under the terms of the bill.

RELATIONSHIP

Similar to HJR1, which seeks additional annual LGPF distributions by 1 percent for educational programs and early childhood education. Similar to HJR3, which seeks additional annual STPF distributions by 0.5 percent for public safety. Similar to SJR2, which seeks to increase LGPF distributions by 1.5 percent for early childhood education. Relates to SJR3, which seeks to create the Early Childhood Education Department. Similar to SJR7, which seeks to increase distributions by 0.8 percent from the STPF for early childhood education.

TECHNICAL ISSUES

Other proposed constitutional amendments pertaining to distributions from the LGPF specify that they take effect as of a specified fiscal year. This legislation does not so specify. If it goes into effect in the middle of a fiscal year or calendar year, it is unclear how it would be implemented in that fiscal year or calendar year.

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APPENDIX A

Quick Facts on the Land Grant Permanent Fund

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 – 2016 contributions totaled about $371 million.
- One of the largest sovereign wealth funds in the country – about $17 billion as November 30, 2017.
- 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 FY18, LGPF distributions to the general fund will be about $585 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.