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FISCAL IMPACT REPORT

ORIGINAL DATE 2-14-07
 SPONSOR Begaye LAST UPDATED 3/01/07 HB 781/aHHGAC
 SHORT TITLE Office of Water Infrastructure Development SB _____
 ANALYST Aubel

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY07	FY08	FY09	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total		*See narrative	.01*	Indeterminate	Recurring	General Fund

(Parenthesis () Indicate Expenditure Decreases)

Relates to HB 2, HB 7, HB 55, HB 228, HB 230, HB 268 and SB 100, HB 274, HB 330, HB 462, HB 859, SB 485, SB 703, and SB 710

Conflicts with HB 53, HB 1179, SB1058, SB 1060 and HB 780

Companion with SB 639 and SB 749

SOURCES OF INFORMATION

LFC Files

Responses Received From

Department of Finance Authority (DFA)

New Mexico Environment Department (NMED)

Office of the State Engineer/Interstate Stream Commission (OSE/ISC)

New Mexico Finance Authority (NMFA)

Attorney General Office (AGO)

Energy, Minerals, and Natural Resources Department (EMNRD)

SUMMARY

Synopsis of HHGAC Amendment

The House Health and Government Affairs Committee Amendment to House Bill 781 would change current references to the New Mexico Finance Authority in the Water Project Finance Act (NMSA Sections 72-4A-1 to 72-4A-10) to the new Office of Water Infrastructure Development with regard to the following:

- Providing staff support for the Water Trust Board;
- Developing application procedures and forms for qualifying entities to apply for grants and loans from the water project fund;
- Approving plans and specifications for a water project; and

- Determining if issuance of revenue bonds is necessary to replenish the principal balance of the water project fund.

The amendment also makes minor stylistic changes.

Synopsis of Original Bill

House Bill 781 would create a new administrative unit known as the Office of Water Infrastructure Development (OWID), which would be administratively attached to the Department of Finance and Administration (DFA).

The primary duties and responsibilities of the OWID would be as follows:

1. Provide staff support to and implement policy decisions of the Water Trust Board (WTB) pursuant to the Water Project Finance Act;
2. Analyze the development of water projects;
3. Monitor the implementation of water projects;
4. Develop and administer a uniform application for water project financing, including applications from the water project fund;
5. Make loans and grants to qualifying entities for water projects;
6. Coordinate financing of water projects from all sources and develop qualifying conditions for funding;
7. Administer technical assistance to water and wastewater systems and acequias;
8. Coordinate reviews of all sanitary surveys and water system inspection reports with the Drinking Water Bureau of NMED;
9. Coordinate review of water projects with the Water Rights Division of the OSE; and
10. Coordinate review of fiscal capacity and budgets of entities applying for funding of water projects with the DFA and the NMFA.

In conjunction with these responsibilities, HB 781 provides that the OWID will administer three existing water and wastewater infrastructure financing programs: the water project fund, the wastewater facility construction loan fund, and the rural infrastructure revolving loan fund. HB 781 amends the related Acts.

In order to effectively carry out these duties and responsibilities, this bill proposes transferring the Construction Programs Bureau (CPB) from NMED to OWID. This transfer would include all powers and duties, staff, existing funds, appropriations, records, equipment, supplies, other property, all memoranda of understanding, joint powers agreements and contracts of the CPB effective on July 1, 2007. HB 781 would also transfer the water project fund from NMFA to the state treasury.

FISCAL IMPLICATIONS

While there is no appropriation included in this bill, the costs are associated with transferring personnel from CPB to OWID. The agency base budget request for CPB for FY08 included \$1.5 million and 17 FTE. Additional personnel will most likely be required to fulfill all of HB 781's mandates, which include the current activities that are already stretching the CPB staff thin. One such expansion will require the 4 FTE currently providing the support function for the Water Trust Board by NMFA.

In addition, DFA notes that HB 781 relates to the \$1.0 million recurring appropriation and 4.0 FTE to provide administrative staff and expenses for implementing OWID that was included in the executive's recommendation for DFA's budget for FY 08. No details of this funding were specified.

HB 781 language also transfers all money, appropriations and equipment of CPB to OWID. However, all such property belongs to NMED, not CPB, which raises the issue of whether OWID would need to equip its own office using additional funding.

SIGNIFICANT ISSUES

According to EMNRD, the HHGAC Amendment should clarify the administration of water projects in the state under the new centralized system established by HB 781.

NMED concurs that the HHGAC amendments to the Water Projects Finance Act (Sections 72-4A-5, 6, & 7) make them consistent with other provisions in HB 871. NMED also notes that by replacing NMFA with the new Office in Section 72-4A-9.C as the one to determine when to issue revenue bonds eliminates a potential conflict of having NMFA decide when to issue bonds, but having the Office responsible for the program. According to EMNRD, the Amendment should clarify the administration of water projects in the state under the new centralized system established by HB 781.

NMED expresses concern regarding having sufficient staff to fulfill all the tasks and duties presented in the bill.

Background

Funding agencies for water-related capital outlay include NMED Construction Program Bureau (CPB), New Mexico Finance Authority (NMFA), Department of Administration – Local Government Division (LGD), and the United States Department of Agriculture Rural Development. Additional funding programs include the Water Trust Board, US Environmental Protection Agency's State Tribal Assistance Grants (STAG), Governor's Tax Relief Fund, and the Governor's Innovative Fund.

For infrastructure projects, technical expertise and oversight has been provided by CPB. Since 2001, increases in legislative appropriations for capital projects administered by the CPB have risen more than 2,000 percent, from an average of \$5.2 million to over \$63 million in FY06. For the first half of fiscal year 2007, CPB managed 767 active Special Appropriations Projects (SAPs). CPB also provides oversight and technical assistance for the following additional programs:

- 8 clean water state revolving fund (CWSRF) projects with an outstanding balance of \$46 million; 1 loan in progress for \$7 million; 31 loans in repayment;
- 11 rural infrastructure revolving loan program (RIP) projects with an outstanding balance of \$3.1 million; 120 loans in repayment; and
- 6 active projects in the Solid Waste Facility Grant Fund (SWFGF) with an outstanding balance of \$764 thousand.

CPB has also provided technical assistance to the other funding agencies for over 200 projects

during the same time period.

NMFA assists qualified governmental entities in the financing of capital equipment and infrastructure projects at any stage of completion – from pre-planning through construction – by providing low-cost funds and technical assistance through its five main financing sources:

- Drinking Water Revolving Loan Fund (DWRLF)
- Primary Care Capital Fund (PCCF)
- Public Project Revolving Fund (PPRF)
- State Buildings and Automation Project Financing
- Water and Wastewater Grant Fund (W/WWGF)

The Water Trust Fund (created in 2001) is currently administered by the NMFA, and the NMFA currently provides staff support to the Water Trust Board, which oversees this fund. These water projects include water storage, conveyance, or delivery of water to end users; implementation of federal Endangered Species Act of 1973 collaborative programs; restoration and management of watersheds; flood prevention; or water conservation.

As of June 30, 2003, the NMFA has financed more than \$627.1 million in capital projects across New Mexico, from all of its funding programs.

Capital Outlay for Water and Wastewater Projects

During the interim, testimony was presented to the Capital Outlay Subcommittee of the Legislative Council and the Legislative Finance Committee on the history of the capital outlay process and on how New Mexico compared with other states in capital outlay procedures and processes. It was noted that New Mexico received a low ranking from Governing Magazine on its capital outlay process mainly due to the perceived lack of planning for funding projects (which can leave projects “stranded” during some stage of the project pipeline), lack of consistent qualifying factors for recipients, and lack of state-wide prioritization.

HB 781 proposes to address these issues by consolidating funding under one agency for water and wastewater projects. That would allow prioritization of projects and imposition of conditions for funding as envisioned under prior legislative efforts.

NMFA maintains that developing a comprehensive funding mechanism that ties system readiness, project need and fiscal responsibility will, over time, create more self-sufficient water systems that will not require as many significant outlays of state support for emergencies caused by inadequate design, maintenance and replacement.

DFA maintains that OWID, by the centralization, will be able to better match projects with funding sources. NMED adds that the centralization would facilitate state-wide prioritization of projects.

PERFORMANCE IMPLICATIONS

DFA anticipates that water infrastructure projects, by the centralization in OWID and the one-stop shop concept, will receive better technical review and better oversight of these projects

because DFA envisions that everyone dealing with the projects will be housed in one place, working together on each project. Also, DFA sees fewer instances of funding sitting underutilized because preparatory requirements were left undone, such as obtaining the necessary water rights. DFA also believes that the state will save money from the regionalization of projects, the appropriate scaling of projects, and the reduced duplication of projects in the same region. DFA assumes that that OWID will be electronically linked to the Office of the State Engineer's Water Rights Division, which will report information on water rights statewide. This will assist OWID in prioritizing and regionalization of water systems in accordance with HJM 86.

NMFA asserts that the development and implementation of a uniform application and qualifying criteria will provide additional efficiencies at the local level as systems will know what to expect when they seek state grant or special legislative appropriation support. However, NMFA notes that requiring this process for already self-sufficient systems seeking only to borrow money to finance their improvements creates an unnecessary bureaucratic burden on them. Systems that need to proceed quickly with their projects may be forced to issue bonds on their own in the tax-exempt markets and forgo the benefits and low-cost financing available.

NMFA relates that HB 781 continues to place the responsibility of issuing bonds against the federally-funded wastewater facility construction loan fund (WFCLF) with the State Board of Finance (BOF), with two consequences. One, while the bonds allowed under HB 781 do not pledge the state's general fund or impact its balance sheet, any technical or financial default on the bonds or loans pledged to the bonds could negatively impact the state's bond ratings. Second, NMFA notes that the BOF expertise lies in issuing general obligation bonds and severance tax bonds, and not bonds backed by loans. This is the expertise held by NMFA, as demonstrated by its handling of the federally-funded drinking water loan program. NMFA concludes that amending HB 781 to include the centralization of loan funding for water and wastewater systems under NMFA would allow for leveraging both programs, which will result in larger subsidized loan funds for critical drinking water and wastewater projects and increase the performance of the federal dollars being translated into projects in New Mexico.

ADMINISTRATIVE IMPLICATIONS

HB 781 appears to underestimate the administrative impact on CPB, which would be significant. Water project fund ventures range from watershed projects undertaken by water conservation districts to those projects undertaken under the Endangered Species Act. Currently, NMFA contracts with the relevant agency to provide needed technical expertise, such as with CPB for those related to water infrastructure. Many of projects are particularly time-consuming and of long duration, most likely beyond the expertise of the current CPB staff and certainly beyond their available resources.

NMFA also notes that portions of HB 781 duplicate current responsibilities of the finance authority. NMFA also expresses concern over The Rural Infrastructure and Wastewater Facility Construction Loan Acts are amended by HB 781 to replace the bureau with the "Office". HB 781, in effect, transfers all actively-managed grant funds to the office, but keeps the administration of committed loan funds in less active programs dispersed among several agencies. Lastly, while HB 781 keeps the Water and Wastewater Facility Grant Fund with the finance authority, it moves the administration of water project grants and loans to the office.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

The executive capital outlay budget recommends a \$25 million appropriation to the water trust fund and an appropriation of \$1.0 million and 4.0 FTE to provide for administrative staff and expenses for implementation of the OWID.

HB 2 contains an appropriation and FTE for the FY08 operating budget for the Construction Programs Bureau at the NMED.

HB 7 seeks a general appropriation of \$50 million to the water trust fund for fiscal year 2008.

HB 53 amends the Water Project Finance Act to add the DFA Secretary as a member of the WTB and provides for the WTB Chair to be elected by the membership.

HB 55 appropriates \$60 million from the general fund to the water trust fund for implementation of the Water Project Finance Act.

HB 228 appropriates \$130 thousand from the general fund to the DFA to provide staff support to the Acequia Commission.

HB 230 appropriates \$500 thousand from the general fund to the LGD of DFA to provide governance education, training and technical assistance to the Acequia Commission.

HB 268 and SB 100 (duplicates) authorize the NMFA to make loans and grants from the water project fund for 30 qualifying projects on terms and conditions established by the WTB and the NMFA.

HB 274 appropriates \$280 million from the general fund for expenditure on seven statewide water projects.

HB 330, among other provisions, would allow the Interstate Stream Commission to use funds received for the Strategic Water Reserve (SWR) to be used to develop and construct infrastructure related to the SWR.

HB 462 appropriates \$100 million from the general fund to the Water Trust Fund for implementation of the Water Project Finance Act.

HB 780 would increase, from 10 percent to 15 percent, the annual set-aside from severance tax bonding capacity for use by the Water Trust Board to fund water projects statewide.

HB 859 would appropriate \$4 million to create a new cesspool fund to help lower income residents install septic or hookup to a wastewater facility.

HB 1058 would include wastewater in property valuation.

HB 1179 (SB 1058) amend the Rural Infrastructure Program.

SB 105 appropriates \$4 million from the public project revolving loan fund to the drinking water state revolving loan fund to provide state matching funds for water projects funded through the

federal Safe Drinking Water Act.

SB 485 appropriates \$225 million from the general fund to the OSE to initiate, plan and implement five water projects statewide.

SB 639 and SB 749 (duplicates) would establish a Capital Projects Council composed of twelve members including the State Engineer. The primary responsibilities of the Council would be to: a) prioritize proposals for capital projects and make recommendations to the legislature for funding the prioritized projects; and, b) coordinate all planning, oversight, monitoring and reporting functions of state government regarding capital projects authorized by law.

SB 703 appropriates funds from the general fund for implementation of a wide variety of capital projects statewide including water and wastewater projects.

SB 710 appropriates \$52.4 million from the general fund for implementation of a wide variety of capital projects statewide including water and wastewater projects.

SB 1060 sets up an administrative fund for the wastewater facility construction loan fund.

TECHNICAL ISSUES

The bill uses customary language that reflects standard practices for governmental reorganization where such transfers occur.

NMFA points out a potential conflict of interest issue:

Authority to Issue Revenue Bonds (Page 5, line 18)

A potential conflict of interest is created by having the bonds issuance in one agency and the need for the money managed elsewhere.

NMED relates that language regarding funds that included federal grants most likely will require EPA approval:

Administrative Costs (Section 5)

The amount of the administrative costs is not specified and would most likely require confirmation by the United States Environmental Protection Agency. For example, NMFA is currently capped at 4 percent.

OTHER SUBSTANTIVE ISSUES

Based on a study by the National Association of State Budget Officers, *Capital Budgeting in the States*, best management practices (BMPs) for quality capital budgeting require:

- Defining capital expenditures
- Defining maintenance expenditures and identifying funding for maintenance
- Developing a system to prioritize projects and identify criteria used for selection
- Identifying operating costs of each project over a multi-year period
- Effective communication between the legislature and the executive during the capital

budget process

- Strengthened review of long-range capital plans
- Integrated planning with debt affordability
- Review of cost-benefit comparisons for private sector participation in capital projects
- Review of long-term leases
- Defining of outcomes for capital investments
- Validating cost estimating methods
- Establishing a tracking system to keep projects on schedule and within budget
- Maintaining an updated inventory system of capital assets
- Maintaining a centralized oversight for capital projects

DFA has developed a unified loan application, but a true implementation of this BMP is seriously hampered by so many loan and grant agencies. Not only is it difficult to bring everyone to the table with the potential recipient, so many “voices” only seem to confuse rather than elucidate the potential recipient.

ALTERNATIVES

One option would be to designate one loan agency (NMFA) and one grant agency (OWID) to create a synergy of strengths and optimize efficiencies of scale. The two agencies could then collaborate with the potential “customer” to develop the optimal project financing package by first establishing the loan parameters and then looking to a grant for any final funding amount required. DFA’s current unified application could then be used in the most effective fashion.

NMFA maintains it could administer the rural infrastructure loan and federally funded clean water state revolving loan programs to become New Mexico’s primary state lender for water and wastewater projects. By adding these funds to the finance authority’s program listing, the finance authority specifies it will be better able to match public entities with the most appropriate finance mechanism available from the state and add to the funding available for critical water and wastewater projects by leveraging the federal funds. NMFA lists additional benefits that would accrue:

- It would dramatically increase the number of borrowers for the finance authority, which would add to the economies of scale.
- It would replicate the successful BMP of leveraging federal funding by issuing state revolving fund revenue bonds, which will increase the availability of low-cost funding for water and wastewater projects. The most efficient of these bonding programs involves the “cross-collateralization” of both the federal grants. Because the clean water program is an older program, the loans made under the program are considered more mature and provide a stronger repayment stream than the newer drinking water program. However, the benefits to the state of this “cross-collateralized” bonding program are weakened if the finance authority does not manage the loan funds.
- It would utilize NMFA’s reputation among the Wall Street credit rating agencies, bond insurers and bond purchasers has as an efficient packager of loans and superior manager of bonding programs.
- It would build a successful loan program with no or few defaults.
- It would provide greater flexibility than a state-run program for default work-outs and

recovering the state's resources.

- It would reduce costs associated with establishing a loan managing computer system at OWID since NMFA already maintains a separate accounting system dedicated solely to tracking loans and making payments to bondholders.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Water and wastewater project administration will remain fragmented among several state agencies. NMFA would continue to provide programmatic and administrative support to the water trust board and issue loans and grants from the water project fund pursuant to provisions of the water project finance act. CPB would remain in NMED and continue to issue grants and loans pursuant to the provisions of the wastewater facility construction loan act and the rural infrastructure act.

AMENDMENTS

Section 7, 74-6A-8.E, Page 16, line 25: Delete “division” and replace with “office”.

NMFA recommends clarifying language on Section 1.B. (6) on page 2, lines 17 and 18. As currently drafted, this responsibility appears to duplicate authority given to office of state engineer, game & fish, NMSU and NMFA on loan funds they currently administer. Recommend replacing in its entirety Section 1.B. (6) with “coordinate prioritization of water and wastewater projects and develop qualifying criteria for all grant and special appropriation funding.”

Amend further sections of the Water Project Finance Act to effectuate the goals of HB 781. Specifically, Section 72-4A-5 B: replace the “authority” with the “office.” Similarly, in Section 72-4A-7B: replace “authority” with “office.” Lastly, repeal section 72-4A-6 Authority; duties section to not conflict with other provisions of HB 781. In HB 781, Section 4B, on page 5, line 20, replace “authority” with “office.”

POSSIBLE QUESTIONS

1. What is the structure of “administratively attached” to DFA? What is the reporting structure? Who is in charge—DFA or the Water Trust Board or CPB?
2. How will the current grant and loan payment transfer be seamless? What plan has been structured to make sure the recipients do not experience delays, such as those precipitated by SHARE implementation?
3. What are the realistic resources in terms of FTE and property that will be required to fulfill the OWID?
4. How would the financial expertise developed by NMFA be transferred or utilized?
5. Who will be making the final project recommendations to the Legislature?
6. If bills such as HB 859 are enacted, how will the new funds—such as the Cesspool fund—be managed?

7. Who will take over the solid waste capital outlay responsibilities currently handled by CPB, and will the resources be provided?
8. Who will provide oversight of the domestic mutual water associations?
9. Who would administer the Sanitary Projects Act?
10. Were all stakeholders, such as NMFA, the Rural Water Association, the Acequia Association, the Environmental Finance Center, USDA Rural Development, the Rural Community Assistance Corporation invited to participate in crafting the OWID?
11. How would the various timelines for grants and loans be coordinated?

MA/mt