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

		ORIGINAL DATE	01/25/11		
SPONSOR	Trujillo	**LAST UPDATED**	03/07/11	**HJR**	1
SHORT TITLE	Land Grant Fund Annual Distributions, CA			**SB**	
				ANALYST	Burrows

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY11	**FY12**	**FY13**		
$0.0	$0.0	$24,323.7	Recurring	General Fund
$0.0	$0.0	$4,956.6	Recurring	Other LGPF Beneficiaries

(Parenthesis ( ) Indicate Expenditure Decreases)

Relates to SB1

SOURCES OF INFORMATION
LFC Files

Responses Received From
State Investment Council (SIC)
Attorney General's Office (AGO)
New Mexico Corrections Department (NMCD)
Higher Education Department (HED)
Public Education Department (PED)
State Land Office (SLO)
Department of Finance and Administration (DFA)

SUMMARY

Synopsis of Bill

House Joint Resolution 1 proposes to amend Article XII, Section 7 of the New Mexico constitution in order to permanently increase annual distributions from the Land Grant Permanent Fund (LGPF) to 5.8 percent beginning in FY13. Currently, distributions are constitutionally set at 5.8 percent through FY12 and are subsequently scheduled to decrease to 5.5 percent from FY13 to FY16 and to 5.0 percent thereafter.

The proposed constitutional amendment also removes the provisions allowing suspension of distributions above 5.0 percent if the five-year average market value of the fund falls below $5.8 billion or with three-fifths' vote of the legislature. Moreover, House Joint Resolution 1 will remove language restricting distributions above 5.0 percent to "implement and maintain educational reforms."

If House Joint Resolution 1 passes both houses of the legislature, the proposed constitutional amendments will require approval by New Mexico voters during the next statewide general election or at any special election prior to that date that is called for this purpose.

FISCAL IMPLICATIONS

The proposed amendment would have a significant fiscal impact on the LGPF and its beneficiaries. In FY10 the LGPF made $525.5 million in distributions to a variety of beneficiaries.

FY10 LGPF Distributions by Beneficiary	
Common Schools (GF)	$437,127,589
University of NM	$8,447,972
NM State University	$2,626,981
Western NM Univ	$154,598
Eastern NM Univ	$445,886
NM Highlands Univ	$153,689
Northern NM College	$120,434
NM Inst Mining & Tech	$1,085,531
NM Military Inst	$17,789,968
NM School for the Deaf	$10,853,958
NM Sch for Visually Imp	$10,825,778
Miners Medical Ctr	$5,491,589
NM State Hospital	$1,262,780
NM State Penitentiary	$10,600,005
NM Boys School	$35,788
Char Penal & Reform	$4,781,321
Public Buildings	$6,161,957
Water Reservoirs	$6,061,534
Rio Grande Improvmt	$1,453,879
UNM Saline Lands	$31,289
	$525,512,526

Source: State Land Office

These distributions play an important part in the operating budgets of each beneficiary. For instance, the distributions to the general fund typically represent approximately 10 percent of total recurring general fund revenue. If the proposed legislation is adopted by the Legislature and New Mexico voters, the overall distributions from the LGPF to beneficiaries will be approximately $745.2 million greater than current law over the ten fiscal years from FY13 to

FY22. These calculations are approximations based upon an average annual fund return of 8.5 percent less transaction costs of 0.3 percent. Estimated contributions to the LGPF are consistent with consensus revenue oil and gas price and volume forecasts through calendar year 2014 and set equal to $350 million thereafter (the approximate 10-year contribution average). The chart below shows the increase by fiscal year.

	Current LGPF Distribution $MM	**HJR1 LGPF Distribution** $MM	**Distribution Impact HJR1** $MM
FY2013	$536.8	$566.1	$29.3
FY2014	$547.0	$576.7	$29.7
FY2015	$596.6	$628.4	$31.8
FY2016	$641.4	$674.8	$33.4
FY2017	$620.5	$716.8	$96.3
FY2018	$659.1	$759.3	$100.2
FY2019	$700.3	$803.7	$103.4
FY2020	$743.7	$849.6	$105.8
FY2021	$789.3	$896.7	$107.4
FY2022	$837.2	$945.1	$108.0
			$745.2

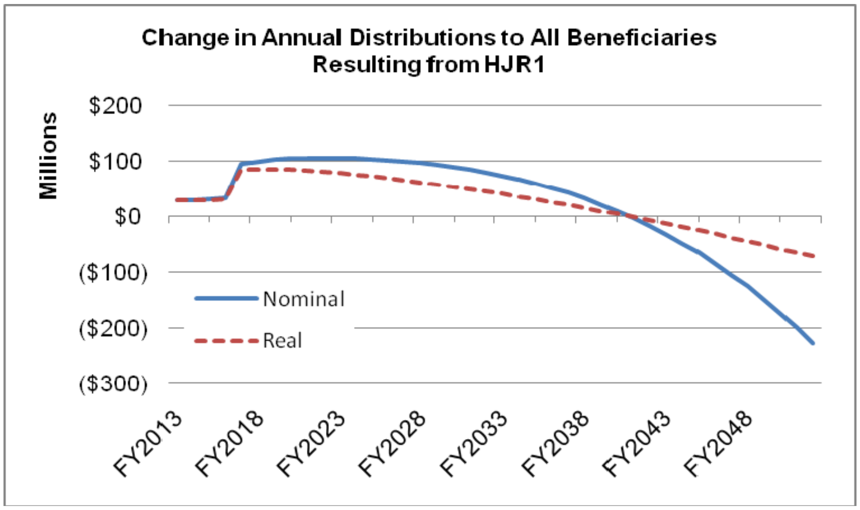
Source: LFC Files

DFA has estimated a positive impact to the general fund of $32.7 million and to the LGPF beneficiaries of $7.5 million in FY12, or approximately $10 million more than the above estimate. DFA's analysis uses the market value of the fund as of December 31, 2007 as a starting point, and applies the new rates to the projected fund corpus. Low returns on investment in calendar years 2008 and 2009, however, have decreased the five-year market value, which will impact future distributions. The analysis outlined above uses the market value of the LGPF as of December 31, 2010, which may be a more accurate starting point of projected fund value.

SIGNIFICANT ISSUES

In current law, distributions to beneficiaries will decrease by approximately 0.3 percent in FY13 and 0.5 percent in FY17, but distributions are expected to grow in other fiscal years due to positive returns on fund investment. If House Joint Resolution 1 is not approved, those beneficiaries who currently rely on LGPF distributions to supplement operating budgets could experience a decrease in revenue during FY13 and FY17 that may have to be offset through general fund appropriations. This offset, coupled with the decrease in distributions to the general fund in those fiscal years, could create future budgetary challenges. However, the true impact to beneficiaries will depend on oil and gas royalty contributions, market performance, investment return and any other legislation that might affect the balance of the fund.

Although the general fund and other LGPF beneficiaries will experience an initial increase in distributions with approval of House Joint Resolution 1, at the higher rate of 5.8 percent beneficiaries will begin to receive less revenue than they would under current law within 30 years. The following graph illustrates the change in total distributions with approval of the resolution.



Source: LFC files. Real distributions calculated based on a 3 percent discount rate.

By raising the base distribution level of 5.0 percent to 5.8 percent, House Joint Resolution 1 removes the failsafe previously governing the additional distribution of the LGPF mandated by Amendment 2 should the fund's corpus fall below $5.8 billion. It also removes the secondary safety net which allows the legislature to reduce distributions to the current base of 5.0 percent with a three-fifths' vote.

DFA notes that there are concerns that New Mexico's current public school funding formula does not meet the constitutional requirement to provide a uniform system of free public schools sufficient for the education of all school aged children. According to the funding formula study task force, New Mexico's education system is currently underfunded by $332 million per year.

RELATIONSHIP

Senate Bill 1 proposes to issue bonds of up to $300 million from the Severance Tax Permanent Fund (STPF) and/or the Land Grant Permanent Fund with a maximum investment return of 4.9 percent.

OTHER SUBSTANTIVE ISSUES

The estimates in this analysis are based on an assumption of 8.5 percent investment growth. However, the SIC has expressed some concern that such a growth rate is no longer achievable.

State Investment Council:

> "As of 9/30/10 – the last quarterly audited numbers available – Land Grant Fund annualized Investment returns are as follows:

One year return:	12.6%
Three year return:	(3.0)%
Five year return:	3.1%
10 year return:	3.1%
15 year return:	6.8%

> The view of the Council, and many other investment professionals around the country, is that expectations regarding long-term investment returns should be tempered, and many have revised their expectations downward from the former standard of 8% per year. Some are using 6.5% as a long term return target."

At a 6.5 percent rate of return, general fund and other LGPF beneficiaries will experience an increase in distributions from FY13 to FY22 of $676.8 million.

Moreover, to avoid long term erosion of the fund, the impact of inflation on real dollar value should be taken into account.

DFA notes that the LGPF was established under the Ferguson Act of 1898 and confirmed by the Enabling Act for New Mexico in 1910. These acts transferred about 9.2 million surface areas of federal lands and 13.1 million of federal mineral interests to the territory of New Mexico. These lands were to be held in trust for the benefit of public schools and 19 other state institutions.

Moreover, DFA reports the LGPF corpus consists of proceeds from the sale of state lands, royalties from natural resource production, and 5 percent of the proceeds from the sale of federal lands in New Mexico. Rental revenue, bonuses from land leases and other income from public land are also distributed to LGPF. The common school fund, which is an account in the general fund, is the beneficiary of approximately 83 percent of income from the LGPF.

As of December 31, 2010, the market value of the LGPF was $10.2 billion.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

If the proposed legislation is not enacted by the legislature or approved by New Mexico voters, the current LGPF distribution schedule will remain as follows:

Current LGPF Distribution Schedule

Fiscal Year	Distribution Rate
2012	5.80%
2013	5.50%
2014	5.50%
2015	5.50%
2016	5.50%
2017	5.00%

LKB/mew:svb