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LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS
54th Legislature, 1st Session, 2019

Bill Number	<u>HJR1</u>	Sponsor	<u>Maestas/Martinez, J.</u>
Tracking Number	<u>.211978.1</u>	Committee Referrals	<u>HEC/HCEDC;SRC/SFC</u>
Short Title	<u>Permanent Funds for Early Childhood, CA</u>		
Analyst	<u>Rogne</u>	Original Date	<u>1/28/2019</u>
		Last Updated	<u>3/4/2019</u>

BILL SUMMARY

Synopsis of Joint Resolution

House Joint Resolution 1 (HJR1) amends Article XII, Section 7 of the Constitution of the State of New Mexico to increase annual distributions from the land grant permanent fund (LGPF) by 1 percent for all beneficiaries, provided that the amount of the additional distribution from the permanent school fund would be designated for early childhood educational services that are administered by the state for children until they are eligible for kindergarten. The joint resolution requires the approval of voters at the next statewide general or special election and the consent of the United States Congress to become effective.

FISCAL IMPACT

House Joint Resolutions do not carry appropriations.

HJR1 would amend Article XII, Section 7 of the Constitution of the State of New Mexico to increase annual distributions from the LGPF by 1 percent, provided that the amount of the additional distribution from the permanent school fund would be earmarked for early childhood educational services that are administered by the state for children prior to kindergarten. The joint resolution proposes an additional 1 percent distribution of the average of year-end market values for the immediately preceding five calendar years. The additional 1 percent distribution, based on State Investment Council (SIC) estimates, will result in distribution of an additional \$157 million to \$170 million from the fund annually. Of this amount, 85 percent would be distributed from the permanent school fund – which is currently held in trust for the common schools (or public schools) – to the general fund to be appropriated by the Legislature to fund early childhood educational services administered by the state for children before they enter kindergarten. The remaining 15 percent would be distributed to the remaining 20 beneficiaries. In years when the annual distribution is made, the total annual distribution from the LGPF will be 6 percent of the annual year-end market value of the fund for the preceding five years.

Additional Distribution Suspension. Current language in the Constitution prohibits an annual distribution from the fund if the average of the year-end market value of the fund for the preceding five years is less than \$10 billion.

The average year-end market value of the fund over the past preceding five years, when including the projection for 2019, totals \$16.4 billion as shown by the chart below:

**Land Grant Permanent Fund Net Assets
(2015-2018 Actuals, 2019 Projection)
(in billions)**

2015	\$14.4
2016	\$15.2
2017	\$17.3
2018	\$17.1
2019	\$17.9
5-Year Average	\$16.4

Source: SIC and LESC Analysis

The Legislature should note that the \$10 billion threshold to suspend additional distributions may be too low to protect the fund given the average balances over the past five years. For example, if the fund dropped to \$500 million in 2019, the average year-end market value of the fund over the past five years would still be above the \$10 billion threshold, and the annual distribution would still be required. The following chart uses actual year-end fund balances for 2015 to 2018, and an example of \$500 million for 2019:

**Land Grant Permanent Fund Net Assets
"Safety Valve" Example
(in billions)**

2015	\$14.4
2016	\$15.2
2017	\$17.3
2018	\$17.1
2019	\$0.5
5-Year Average	\$12.9

Source: SIC and LESC Analysis

If this provision is intended to act as a “safety valve,” the Legislature may want to consider using an ending balance of \$10 billion for a single year instead of a five-year average to trigger suspension of the annual distribution; alternatively, the Legislature could also consider using a three-year average to trigger suspension of the annual distribution. Given the fact that the current “safety valve” is not activated even with this extreme example, it appears that funds could deteriorate slowly over a long period of time before this provision is enacted to protect the fund.

According to the SIC, HJR1 would deliver significant revenue to the state – an estimated \$157 million in year one, and just under \$2.1 billion over the first 12 years – though only 85 percent of that amount would be available for the state to fund state-administered early childhood educational services. SIC notes if healthy inflows from oil and natural gas are poised to continue for the next 20 to 30 years, the permanent fund should continue to grow on a real-dollar basis, despite the 1 percent in additional distributions, even if investment returns are below-average over the coming decade. However, SIC notes that the opposite also holds true, and if oil and gas prices become depressed, especially if coupled with lower investment returns – which many predict over the next

decade – along with a higher spending rate would have a much greater potential to negatively impact the health and growth of the LGPF long term.

SIC notes that from a long-term, multi-decade perspective, an endowment fund like the LGPF that distributes 5 percent of its corpus will ultimately deliver more money to early childhood educational services overall than a fund distributing 6 percent. According to SIC, the key question for policymakers comes down to whether the added cost over the long-run is an appropriate and attractive trade-off for the added benefits HJR1 is expected to deliver to state-administered early childhood educational services and the 20 other beneficiaries (excluding public schools) over the next 30 years. SIC also questions whether there are other existing avenues to fund early childhood educational services, while also protecting and growing the existing hundreds of millions of dollars in benefits the LGPF already delivers annually to New Mexico schools.

SIC cautions that it should not be forgotten that a permanent fund dollar is more valuable than a general fund dollar, in the sense that there is a reasonable expectation that an invested permanent fund dollar will double in value in 10 years because of the benefits of compounding interest. Based on SIC estimates, and not adjusting for inflation, the LGPF with a 5 percent distribution rate will double by 2030, while the LGPF with a 6 percent distribution rate will double in value by 2032.

HJR1’s passage would incur additional one-time costs related to bringing the measure to voters, either in a special election or through a scheduled statewide referendum. Section 1-16-13 NMSA 1978 requires the Secretary of State (SOS) to print the full text of each proposed constitutional amendment, in both Spanish and English, in an amount equal to 10 percent of the registered voters in the state. The SOS is also constitutionally required to publish the full text of each proposed constitutional amendment once a week for four weeks preceding the election in newspapers in every county in the state. Legislative Finance Committee (LFC) staff estimate each constitutional amendment may cost from \$50 thousand to \$100 thousand in printing and advertising costs based on 2016 actual expenditures, the most recent year in which data was available.

SUBSTANTIVE ISSUES

HJR1 amends Article XII, Section 7 of the Constitution of the State of New Mexico to increase annual distributions from the LGPF by 1 percent, with the annual distribution from the permanent school fund earmarked for state-administered early childhood educational services for students prior to kindergarten; however, this could potentially open the State of New Mexico to lawsuits.

Background and History on the LGPF. In anticipation of New Mexico’s pending statehood, the United States transferred 13.4 million acres of federal land to the then-Territory of New Mexico via the *Ferguson Act of 1989* and the *Enabling Act of 1910* to be held in trust for the benefit of “common schools” – hereafter referred to as public schools – and other specifically identified state institutions. Currently, there are 21 beneficiaries that receive LGPF distributions. See **Attachment 1, Land Grant Permanent Fund Balance and Income Distribution for FY18**. Public school districts account for about 85 percent of LGPF distributions through the permanent school fund. HJR1 increases distributions to all beneficiaries, and requires only that additional distributions from the permanent school fund be used for early childhood educational services prior to kindergarten. While additional distributions from the LGPF would produce more revenue for LGPF beneficiaries, the additional distribution will lessen future earnings of the LGPF and reduce the increased benefits that a larger fund would produce long-term at a lower distribution rate.

The LGPF is funded by income from non-renewable resources, such as oil and gas revenues that make up over 90 percent of contributions to the fund, and was designed to provide for future generations of New Mexicans when those resources are exhausted. It is one of the largest sovereign wealth funds in the country, with a fund balance of \$17.3 billion as of March 2018. Currently, 5 percent of the LGPF five-year average year-end balance is distributed to 21 beneficiaries based on land ownership. In FY18, total LGPF distributions were about \$689 million, with about \$587 million distributed to public schools.

HJR1 specifies that only the additional 1 percent annual distribution from the permanent school fund would be designated for early childhood educational services, a notable difference from prior versions of this bill. The other 20 LGPF beneficiaries would also be receiving a 1 percent distribution, but would not have to apply these funds towards early childhood educational services. According to SIC, the impact of passage of HJR1 would result in tens of millions of additional dollars flowing to the other beneficiaries in the coming years, but cautions that these beneficiaries will ultimately receive less benefits from LGPF in aggregate due to lessened investment earnings.

Intended Beneficiaries and Standing to Sue. HJR1 anticipates the need for congressional approval, and also defines early childhood educational services as nonsectarian and nondenominational, making it appear that the intent of HJR1 is to appropriate the additional 1 percent permanent school fund distribution to entities other than public schools for early childhood educational services. This may open the state up to a lawsuit from the current beneficiaries of the permanent school fund – public schools – for whom these distributions are intended. It is unclear whether a school district or its board of education or a school aged child, as the intended beneficiaries, would be able to bring a successful lawsuit against the state for allocating the additional 1 percent distribution to an entity other than a public school.

Early Childhood Issues. HJR1 defines “early childhood educational services” as nonsectarian and nondenominational services for children until they are eligible for kindergarten that are administered by the state. HJR1 does not allow funding to the public schools, but increases early childhood educational services. The agencies which would receive funding under HJR1 are the Children, Youth, and Families Department (CYFD), Department of Health (DOH), and the Human Services Department (HSD).

Currently, New Mexico’s early childhood education and care system spans several state agencies: CYFD, DOH, HSD, and PED. The table below shows the early childhood educational services provided by each agency and the age range of children served.

Early Childhood Education and Care System

State Agency	Program	Age Range
CYFD	Head Start and Early Head Start	prenatal-4
CYFD	Childcare Assistance	3 weeks-13
CYFD	Home Visiting	prenatal-4
CYFD	Prekindergarten	3-4
DOH	Family, Infants, and Toddlers	birth-3
DOH	Women, Infants, and Children	birth-5
HSD	Home Visiting	prenatal-4
PED	Prekindergarten	4
PED	K-3 Plus	5-8
PED	Services for Developmentally Delayed Students	3-4

Source: LFC and LESC Analysis

Although several bills proposing to expand early childhood education in New Mexico have been introduced in the 2019 legislative session, New Mexico has already demonstrated a significant investment in early childhood education programs by growing funding from \$136 million in FY12 to \$309.1 million in FY19, an increase of 125 percent. According to the LFC, New Mexico's 4-year-old service capacity, when taking into account both state and federal care and education services, is at nearly 90 percent. See **Attachment 2, Early Childhood Service Capacity**. This indicates public schools would likely not be the beneficiaries of the additional 1 percent annual distribution in HJR1. Oversaturation of early childhood educational services can have several negative effects, including the return of federal Head Start dollars as a result of student migration from Head Start to other state-funded programs, such as prekindergarten.

New Mexico has a limited workforce qualified in early childhood education. Early childhood educational services encompass a range of programs with differing degree and licensure requirements for providers. Disparities in workforce qualifications, licensure requirements, and compensation can create an environment in which programs compete for highly-qualified early childhood educational service providers. Expansion of early childhood educational services cannot outpace the development of a highly-qualified early childhood workforce.

Consolidated *Martinez* and *Yazzie* Lawsuit. The decision in the consolidated *Martinez* and *Yazzie* lawsuit indicated educational services in public schools are insufficiently funded; yet it is important to note that public schools are the primary beneficiaries of the permanent school fund, so the Legislature may want to consider the legal and fiscal impact of increasing distributions from the permanent school fund for services other than public school services, and over which the department has minimal authority. Costs to bring the state into compliance with the consolidated *Martinez* and *Yazzie* lawsuit could be considerable, as a plaintiff group has suggested more than \$1 billion is needed to comply with the court ruling. The court found current public school support to be inadequate, noting, “simply put, the outputs reflect a systemic failure to provide an adequate education as required by the New Mexico Constitution.” This means public school appropriations in future years will likely need to be increased to achieve necessary outputs. The executive requested \$3.3 billion for public schools for FY20, an increase of \$503 million or 18 percent, and the LFC recommended \$3.2 billion for public schools for FY20, an increase of \$416 million or 14.9 percent.

TECHNICAL ISSUES

The Legislature may want to consider a time limit on congressional action so that the legislation is acted on in a reasonable time frame, as HJR1 does not specify a timeline for congressional authorization.

The New Mexico Attorney General suggests moving the definition of “early childhood educational services” in Section 1, Subsection H to Section 1, Subsection B to keep all the definitions together.

OTHER SIGNIFICANT ISSUES

Substantial evidence demonstrates experiences in early childhood are critical for brain development, and children who participate in high-quality early learning programs have better health, social-emotional, and cognitive outcomes than students who do not participate. Recent advances in neuroscience have shown early childhood years also provide the foundation for literacy skills. The U.S. Department of Education suggests effective early learning programs,

including high-quality prekindergarten, provide a return on investment of \$8.60 for every \$1 spent. New Mexico has focused on expanding early childhood education programs over the last 10 years, despite two economic downturns; however, improving access to high-quality early childhood education programs remains a critical policy issue.

The National Conference of State Legislatures international study of world-class educational systems, *No Time to Lose*, identified four common elements for educational success, the first of which is students come to school ready to learn, with extra support given to struggling students so all students have the opportunity to achieve high standards. The first three years of a child's life are critical for brain development; during this time the brain creates 1 million connections every second that will establish pathways for future development, according to the Center on the Developing Child at Harvard University. When children have adverse childhood experiences (ACEs) or do not have adequate opportunities to create these connections, their future educational achievement and life outcomes are negatively impacted. According to Child Trends, a nonpartisan research center, 18 percent of children in New Mexico experienced three or more ACEs, outpacing the national average of 11 percent. However, early childhood education can reduce the impacts of ACEs by providing children with rich social experiences needed to succeed in school.

ALTERNATIVES

Provide an additional 1 percent annual distribution from the permanent school fund for the purposes of funding nonsectarian and nondenominational early childhood education services administered by the state.

Increase the distribution for the current beneficiaries, which would free up general fund dollars.

SOURCES OF INFORMATION

- LESC Files
- Children, Youth and Families Department (CYFD)
- State Investment Council (SIC)
- New Mexico Attorney General (AG)
- State Land Office (SLO)

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Land Grant Permanent Fund
FUND BALANCE AND INCOME DISTRIBUTION SUMMARY FOR THE FISCAL YEAR ENDED JUNE 30, 2018
(Unaudited)

INSTITUTIONS	July 1, 2017 BEGINNING BAL	% OF FUND	INCOME DISTRIBUTION	LAND TRANSFER	CAPITAL G/L	UNREALIZED G/L	INCOME EARNINGS	BOOK VALUE ENDING BAL June 30, 2018
COMMON SCHOOLS	\$13,829,968,010.28	85.01%	(\$586,560,648.91)	\$545,761,722.27	\$950,344,525.62	\$201,848,804.82	(\$44,245.18)	\$14,941,318,168.90
UNIVERSITY OF N.M.	\$214,912,359.31	1.32%	(\$9,029,524.74)	\$3,211,546.25	\$14,688,063.93	\$3,114,251.36	(\$2,183.83)	226,894,512.28
UNM SALINE LANDS	\$7,292,624.17	0.04%	(\$311,792.25)	\$306,157.00	\$503,806.54	\$109,239.74	(\$8.55)	7,900,026.65
NM STATE UNIVERSITY	\$68,102,132.74	0.42%	(\$2,852,237.89)	\$409,902.15	\$4,645,914.40	\$986,738.26	(\$897.66)	71,291,552.00
WESTERN NM UNIV	\$3,996,269.76	0.02%	(\$167,638.54)	\$39,862.00	\$272,873.16	\$57,959.02	(\$47.71)	4,199,277.69
N.M. HIGHLANDS UNIV	\$3,975,763.28	0.02%	(\$166,782.01)	\$39,862.00	\$271,476.44	\$57,662.59	(\$47.40)	4,177,934.90
NO. NM COLLEGE	\$3,227,086.29	0.02%	(\$135,512.96)	\$39,978.00	\$220,484.30	\$46,840.32	(\$36.17)	3,398,839.78
EASTERN NM UNIVERSITY	\$12,462,212.73	0.08%	(\$522,694.35)	\$108,422.00	\$850,878.20	\$180,863.15	(\$152.70)	13,079,529.03
NM INST. MINING & TECH	\$30,462,790.13	0.19%	(\$1,280,670.65)	\$406,959.00	\$2,082,683.16	\$443,652.57	(\$337.60)	32,115,076.61
N.M. MILITARY INSTITUTE	\$494,634,711.08	3.04%	(\$20,876,844.35)	\$15,033,137.00	\$33,890,874.05	\$7,176,097.38	(\$2,624.11)	529,855,351.05
NM BOYS SCHOOL	\$876,612.91	0.01%	(\$36,614.75)	\$0.00	\$59,708.00	\$12,672.14	(\$13.13)	912,365.17
DHI MINERS HOSPITAL	\$142,356,387.40	0.88%	(\$5,965,501.59)	\$1,044,744.00	\$9,714,493.45	\$2,064,702.44	(\$1,808.07)	149,213,017.63
N.M. STATE HOSPITAL	\$54,203,241.22	0.33%	(\$2,302,493.97)	\$2,304,682.00	\$3,727,966.06	\$789,802.21	(\$59.20)	58,723,138.32
NM STATE PENITENTIARY	\$305,241,922.36	1.88%	(\$12,842,777.41)	\$5,403,494.00	\$20,878,786.46	\$4,433,821.47	(\$2,910.63)	323,112,336.25
NM SCHOOL FOR THE DEAF	\$301,934,648.03	1.86%	(\$12,699,833.04)	\$5,276,800.28	\$20,648,507.56	\$4,384,392.15	(\$2,930.14)	319,541,584.84
SCH. FOR VISUALLY HAND.	\$301,302,062.78	1.85%	(\$12,673,476.00)	\$5,279,988.81	\$20,605,480.99	\$4,375,266.48	(\$2,919.53)	318,886,403.53
CHAR. PENAL & REFORM	\$126,323,698.80	0.78%	(\$5,295,140.30)	\$1,035,817.36	\$8,621,966.40	\$1,830,554.36	(\$1,570.85)	132,515,325.77
WATER RESERVOIR	\$159,090,616.82	0.98%	(\$6,664,822.04)	\$1,116,551.90	\$10,854,704.52	\$2,304,461.74	(\$2,030.42)	166,699,482.52
IMPROVE RIO GRANDE	\$35,593,009.12	0.22%	(\$1,490,234.06)	\$185,893.00	\$2,427,704.38	\$515,340.53	(\$475.42)	37,231,237.55
PUBLIC BLDGS. CAP. INC.	\$172,530,783.07	1.06%	(\$7,306,251.17)	\$7,694,108.50	\$11,844,836.97	\$2,499,064.77	(\$308.81)	187,262,233.33
CARRIE TINGLEY HOSPITAL	\$221,028.34	0.00%	(\$9,232.02)	\$0.00	\$15,054.77	\$3,195.15	(\$3.30)	230,042.94
	\$16,268,707,970.62	100%	(\$689,190,723.00)	\$594,699,627.52	\$1,117,170,789.36	\$237,235,382.65	(\$65,610.41)	\$17,528,557,436.74

Source: State Investment Council

Early Childhood Service Capacity

