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

		ORIGINAL DATE	2/28/2019		
SPONSOR	Campos	**LAST UPDATED**	3/3/2019	**HB**	
SHORT TITLE	Capital Outlay Reform Act			**SB**	455
				ANALYST	Armstrong/Rabin

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Nonrecurring	Fund Affected
FY20	**FY21**		
$100.0	$100.0	Recurring	General Fund
$100.0	$100.0	Recurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

Relates to HB262, SB144, SB280

SOURCES OF INFORMATION
LFC Files

Responses Received From
General Services Department (GSD)
Department of Transportation (DOT)
Higher Education Department (HED)

Responses Not Received From
Department of Finance and Administration (DFA)

SUMMARY

Synopsis of Bill

Senate Bill 455 establishes the Capital Outlay Reform Act, which creates a sixteen-member Capital Outlay Committee composed of legislators and a nine-member Capital Outlay Task Force composed of legislative and executive appointees, and establishes a process for reviewing capital outlay funding requests from state and local entities and for monitoring ongoing capital projects. The task force is required to provide the committee with a state capital improvements plan and a prioritized list of capital funding requests for the upcoming legislative session. The committee is tasked with developing and endorsing the capital outlay bill for the session.

In addition, the bill creates a new "Capital Planning and Assistance" division in DFA and eliminates the department's "Management and Contracts Review" division. The bill establishes the division's powers and duties, which include providing reports to the Capital Projects Task Force and the Capital Outlay Committee, making recommendations to the task force on the development of the state capital improvements plan, assisting government entities in planning, budgeting, and administering capital projects, and maintaining a database for capital projects.

The bill transfers the responsibility of overseeing and monitoring state and local government capital planning and financing from the New Mexico Finance Authority (NMFA) to DFA. SB455 appropriates $100 thousand from the general fund to the Legislative Council Service (LCS) and $100 thousand from the general fund to LFC to implement the provisions of this Act. The bill has a delayed effective date of January 1, 2020.

Timeline. The bill establishes the following process for the submission and review of capital funding requests:

- By **April 1**, the Capital Outlay Committee identifies major categories of need for the following session and establishes objective criteria and a scoring methodology for the evaluation of proposed capital projects.
- By **May 1**, the Capital Projects Task Force develops an evaluation process for proposed capital projects.
- By **May 1**, government entities planning to request capital funding in the following session submit their Infrastructure Capital Improvement Plans (ICIP) to DFA's Capital Planning and Assistance division. The division routes these requests to agencies with relevant subject matter expertise to provide review.
- By **July 1**, state agencies provide recommendations to the task force regarding which capital projects should be funded, using the selection criteria and methodology developed by the committee.
- By **September 1**, the committee provides an estimate of capital outlay capacity available for funding projects in the upcoming legislative session.
- By **September 1**, the Capital Planning and Assistance division makes recommendations to the task force regarding the development of the state capital improvements plan.
- By **November 1**, the task force submits a proposed state capital improvements plan and prioritized list of capital funding requests for the upcoming legislative session to the committee.
- By **December 15**, the committee reports an approved state capital improvements plan and develops an endorsed capital outlay bill for the upcoming legislative session.

Distribution of Funding. SB455 specifies that the capital outlay bill endorsed by the Capital Outlay Committee shall direct at least 40 percent of available capital outlay capacity to state capital improvement projects, which are defined as projects on behalf of state agencies or public institutions of higher education for the purchase of or improvements to property owned by a state agency or public institution of higher education. However, SB455 also requires that the endorsed capital outlay bill not utilize more than 70 percent of available capital outlay capacity; meaning at least 30 percent would be available for legislator-directed projects and up to 30 percent would be available for statewide, regional, or local projects based on the committee's recommendation.

State Agencies	Statewide, Regional, or Local	Legislature
40%-70%	30%-60%	30%-60%

FISCAL IMPLICATIONS

The appropriations totaling $200 thousand contained in this bill are recurring expenses to the general fund. Any unexpended or unencumbered balance remaining at the end of FY20 shall revert to the general fund. This analysis reflects the appropriation as recurring as additional funding would be needed to operate these programs going forward. Generally, if an appropriation creates the expectation that the program will be continued in the future, it is considered recurring.

The proposed new division within DFA is required to provide extensive assistance and outcomes related to the proposed capital outlay process, including compliance and performance audits, evaluations of capital projects, and reporting. DFA did not provide analysis of SB455, so whether current staffing levels are sufficient to meet these assigned duties is unknown, as is the impact of eliminating the Management and Contracts Review Division. No appropriation is included for DFA to implement the provisions of the Capital Outlay Reform Act. The bill's delayed effective date of January 1, 2020, would allow DFA to assess the need for additional resources and request funding for the first year of the new process during the 2020 legislative session.

GSD notes the bill does not provide additional funding to state agencies to prepare and submit ICIPs, which would occur during the legislative session and could require temporary staff to handle the compressed workload. Like DFA, agencies would have the opportunity to request funding during the 2020 legislative session to support the process provided by SB455.

SIGNIFICANT ISSUES

While infrastructure spending is vital, New Mexico's capital outlay process is inefficient, and the practice of earmarking funding for individual lawmakers to allocate is unique among the states. Efforts to improve the process for selecting and funding local capital outlay projects have been largely unsuccessful. Without legislative changes, the process continues to divert funding away from critical needs at state-owned facilities. The lack of procedures to ensure projects are adequately planned and funded means communities' deficient roads and water systems linger and conditions at state facilities continue to pose risk to clients, creating a liability for the state.

Given the volatility of severance tax revenue and the inability of available capital outlay funding to meet all of the state's infrastructure needs, legislators and the executive branch continue to scrutinize the vast amount of unexpended appropriations and large number of projects that remain inactive. Poor project selection (including insufficient planning, a piecemeal approach to funding, and unknown construction costs) continues to delay project completion. These problems should compel policymakers to carefully distinguish future project funding by priority, readiness to proceed, need, public purpose, and merit.

As of December 2018, approximately $639.9 million from all funding sources for 1,608 projects remains outstanding, including $71.5 million of earmarked fund balances for water ($29.7 million), colonias ($19.8 million), and tribal ($21.9 million) infrastructure projects. Additionally, about $395.8 million remains outstanding from supplemental severance tax bonds for public schools. Of the outstanding funds, $121.7 million is for 1,110 "local" projects.

Over the years, proposals have taken aim at developing an efficient process for planning, prioritizing, and funding capital outlay projects. Proposed reforms have included defining the process of selecting and funding projects, clarifying the definitions and limitations on what projects are eligible for capital outlay appropriations, improving how the state monitors projects and ensures they are successfully completed, and increasing transparency by identifying which legislators sponsor each project included in capital outlay legislation.

Prioritization. To assess proposed capital projects, the federal Government Accountability Office recommends quantitatively assessing needs and evaluating alternatives. While some of New Mexico's local governments, state agencies, and higher education institutions have implemented scoring systems, there is no requirement to do so and project priorities and requests often change from year to year.

DFA, Aging and Long-Term Services Department, and Public School Capital Outlay Council use scoring systems based on consistent criteria. Examples of the factors used in project scoring include criticality of need, benefits to public health and safety, readiness to proceed, feasibility, cost-benefit, potential to leverage other funding sources, and opportunity for operational cost-savings. Agencies and local governments should adopt similar scoring practices to improve their ICIPs – documents submitted annually that outline a five-year capital plan.

Although agencies and local governments submit ICIPs, funding is not always awarded in accordance with these priorities, and in some cases projects not included on ICIPs are funded while higher priority projects are neglected. The Indian Affairs Department requires that projects receiving tribal infrastructure fund awards appear on the applying entity's ICIP. A similar requirement for projects funded during the legislative session would ensure funding corresponds with agency and local government priorities; alternatively, inclusion on an ICIP could be considered as a component of a project's overall score rather than automatic disqualification.

Minimum Funding Amount. Projects receiving less than $10 thousand are slower to spend state funds. The Legislature should consider a $50 thousand minimum level for projects funded from capital outlay, unless a lesser amount is needed to complete a project. Larger projects are more likely to realize savings to state and local governments, provide for completion of projects in a timely manner, streamline state and local administrative efforts, and ensure projects fulfill a need in the community.

Grantee Accountability. To ensure state capital outlay funds are awarded to entities that will be good stewards of taxpayer money, the request evaluation process should consider entities' history with prior awards. Federal law and state capital outlay legislation require 5 percent of funds to be encumbered within six months of the bond sale and 85 percent to be expended within three years, but many grantees fail to meet these requirements. Entities that consistently fail to meet legislative requirements and do not demonstrate they have taken steps to ensure future compliance should not receive new awards.

Boilerplate Language. In 2016, recognizing the inadequacies of the capital outlay process, representatives of the Association of Counties (now "New Mexico Counties") and the Municipal League and staff of the executive and legislative branches reviewed and developed administrative improvements. The group proposed changes to the "boilerplate" introductory language of the capital outlay bill to improve the timeliness of bond proceed expenditure, encourage compliance with the State Audit Act, and reduce the number of capital assets that sit unfinished as a result of insufficient funding.

ADMINISTRATIVE IMPLICATIONS

Currently, staff from executive and legislative agencies hear agency ICIP presentations in October of each year, and LFC staff uses this information to develop a framework capital outlay recommendation. If SB455 is enacted, these hearings would likely be unnecessary, as the task force and committee would be charged with preparing a capital outlay bill for introduction during the legislative session. Eliminating the October hearings could result in some savings for participating agencies.

HED has statutory authority to approve programs, budgets, construction, purchases of real property, and capital funding recommendations for all public post-secondary institutions in the state. The creation of a capital outlay committee and capital projects task force under SB455, do not allow for representation from HED in the development of the criteria for project review and vetting. HED regulations establish criteria specific to higher education institutions as it relates to educational settings, enrollment growth, instructional space, library, administration, and research. These items are important in the evaluation and ranking of higher education institution projects. SB455 could be amended to preserve HED's existing review process in place of the required state agency subject matter expert review of capital project requests from colleges and universities, and allowing HED to report directly to the task force by the September 1 deadline rather than reporting to DFA on July 1.

RELATIONSHIP

House Bill 262 and Senate Bill 144 require publication of capital outlay project sponsorship information after enactment of capital outlay appropriation legislation. Senate Bill 280 is the capital outlay appropriation bill for the 2019 legislative session.

OTHER SUBSTANTIVE ISSUES

SB455 exempts road projects funded by DOT pursuant to the statewide transportation improvement plan (STIP). Some projects are included in the STIP to ensure eligibility for federal funding. If a project will be receiving federal funds, only a portion of the project will be funded by DOT through the use of road funds. DOT analysis recommends clarification if SB455 intends to exclude state sponsored projects that receive any federal funding due to their inclusion in the STIP.

DOT suggests revising Section 2.A.(3)(b) to provide that projects receiving federal funding pursuant to the STIP are exempted from the Capital Outlay Reform Act, rather than all projects funded by NMDOT. NMDOT also suggests that a better definition of a road project be provided. There are other types of projects, besides road projects, that are included in the STIP in order to be eligible for federal funding. NMDOT suggests the use of the word "transportation" instead of "road", which would be consistent with the terminology used by the Federal Highway Administration. Finally, NMDOT suggests that Section 2.A.(3)(b) be amended to clarify that if a project appears on the STIP, it is subject to or not subject to the Act if any state funds are sought.

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