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## FISCAL IMPACT REPORT

ORIGINAL DATE 2/19/21

SPONSOR Ortiz y Pino LAST UPDATED \_\_\_\_\_ HB \_\_\_\_\_

SHORT TITLE Charter School Changes SB 318

ANALYST Liu

### APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Nonrecurring	Fund Affected
FY21	FY22		
	\$1,000.0	Nonrecurring	Public Project Revolving Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

### REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY21	FY22	FY23		
	(\$1,000.0)		Nonrecurring	General Fund Operating Reserve

(Parenthesis ( ) Indicate Revenue Decreases)

### ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY21	FY22	FY23	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
<b>NMFA</b>		\$20.0	\$20.0	\$40.0	Recurring	NMFA Operating Budget
<b>PSFA</b>		\$632.8	\$632.8	\$1,265.6	Recurring	Public School Capital Outlay Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Public Education Department (PED)

Public School Facilities Authority (PSFA)

New Mexico Finance Authority (NMFA)

## SUMMARY

### Synopsis of Bill

Senate Bill 318 requires school districts to make facilities not currently used for educational purposes and land not currently used or planned to be used for such purposes available for lease, lease purchase, or purchase by charter schools; the bill requires districts to notify charter schools of such availability and tasks PSFA with ensuring the notifications occur. The bill also expands the facilities eligible for the Public School Capital Outlay Council's (PSCOC) lease assistance program beyond classroom facilities. The bill further amends the Public School Capital Outlay Act to create a "charter facility fund," which will be distributed by PSCOC to pay off lease-purchase agreements. In addition, the bill amends sections of the Public School Capital Improvements Act (commonly referred to as SB9) and the Public School Building Act (commonly referred to as HB33) to establish a process for charter schools to be included in school district resolutions under these acts.

The bill appropriates \$1 million from the general fund operating reserve to the public project revolving fund to finance charter school facilities. The bill requires PSCOC and NMFA to develop rules and policies regarding the distribution of funding from the charter facility fund and public project revolving fund (PPRF), respectively, including ensuring lease-purchase agreements are in compliance with the Public School Lease Purchase Act, ensuring the recipient school's charter has been renewed at least once, and reviewing the school's last two audits.

This bill also makes minor technical changes to the Public School Capital Outlay Act.

## FISCAL IMPLICATIONS

The \$1 million appropriation contained in this bill is a nonrecurring expense to the general fund operating reserve. Any unexpended or unencumbered balance remaining at the end of a fiscal year shall not revert to any other fund. The LFC and executive budget recommendations target spending at levels needed to reach specific general fund reserve targets considered necessary to maintain fiscal solvency for the next fiscal downturn. The \$1 million appropriation from the general fund operating reserve contained in this bill would lower the reserve level.

The public school capital outlay fund is the source of funding for the standards-based and systems-based capital outlay programs for public schools statewide, as well as for the state match for the Public School Capital Improvements Act (SB9), lease assistance program, facility security program, master plan assistance program, and other programs under the Public School Capital Outlay Act. Revenues to the fund are derived from supplemental severance tax bonds and allocations from the fund are authorized by PSCOC.

PED notes the bill expands the square footage of school facilities eligible for funding from PSCOC's lease assistance program, which will increase annual lease assistance awards. In FY21, PSCOC awarded approximately \$16.5 million to charter schools as part of the lease assistance program, covering about 69 percent of total lease costs. Expanding eligible facilities from "classroom space" (which is limited to classroom space and direct administrative space) to "facilities" (defined as "the space needed, as determined by the five year facilities master plan (FMP) aligned with statewide adequacy standards, for school activities") may allow charter schools to receive funding for the entirety of their lease costs. This could increase annual statewide

lease assistance payments by up to \$632.8 thousand, or 4 percent, annually – decreasing the balance available in the public school capital outlay fund for other programs.

PSFA notes the bill proposes to pay off lease purchase agreements from a nonreverting fund administered by the agency. The lease purchase arrangements approved by PED that currently receive lease assistance have outstanding balances exceeding \$50 million. The bill does not include an appropriation to the charter facility fund to cover the costs of paying off all lease-purchase arrangements, and establishing this program may create an expectation that additional appropriations will be made in the future to completely pay down the cost of outstanding arrangements.

Leveraging the charter facility fund to pay off lease-purchase arrangements for schools currently receiving lease assistance could reduce annual costs for lease assistance, which could help offset the cost of increasing eligible square footage under the bill. However, these savings depend on available monies in the fund (which are not included in this bill) and which schools are allocated funding to pay off their lease-purchase arrangements and when those payoffs occur.

NMFA notes the public project revolving fund (PPRF) can only fund charter schools through lease purchase agreements, and NMFA needs to hold title and own the property. The agency may require additional resources to manage a real estate portfolio of charter school facilities. NMFA states these costs will be nominal and estimates them at \$20 thousand annually. This cost is included as estimated additional operating budget impacts in the tables above.

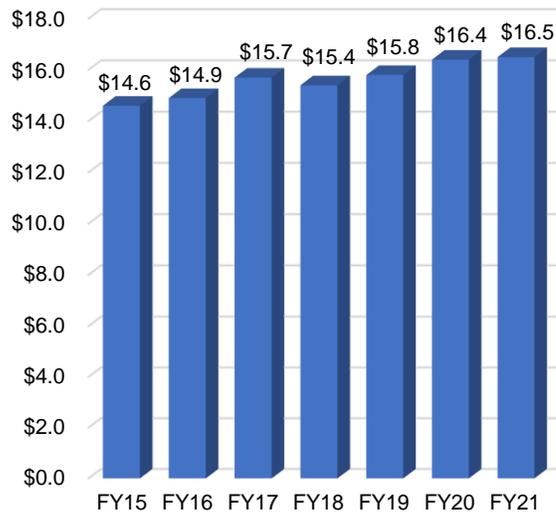
## **SIGNIFICANT ISSUES**

In 2000, the 11th Judicial District Court ruled in the *Zuni Public District v. State of New Mexico* lawsuit that New Mexico's public school capital outlay system violated constitutional requirements and ordered the state to establish and implement a uniform funding system for capital improvements and for correcting past inequities. Since the *Zuni* lawsuit, the state has spent \$2.7 billion to build school facilities up to the approved statewide adequacy standards.

Despite significant improvements in statewide facility conditions, the *Zuni* lawsuit was never closed and, in December 2020, the court ruled in favor of plaintiff school districts on new claims of inequity. The major claim of the plaintiffs was their inability to raise sufficient local capital outlay revenue to maintain capital assets and build facilities that were outside of the statewide adequacy standards like other districts with available local resources. Expanding the use of the public school capital outlay fund for charter school lease assistance may divert funding from the state's effort to address the *Zuni* findings and PSCOC's core function of replacing and renovating school facilities.

According to PSFA, lease assistance grants are a discretionary program. Awards have historically increased year-over-year, with the exception of FY18.

**PSCOC Lease Assistance  
(in millions)**



While the bill requires charter schools be notified of available land or facilities, there is no requirement that charters accept and use it. Further, PSFA notes there is no indication the facilities offered must meet the educational program of the charter or the requirements of the Charter Schools Act regarding charter school facility standards. PED adds that requiring districts to make land or facilities available to charter schools within their district may pose legal concerns because it might require districts to offer land or facilities to state-authorized charters, which are separate local education agencies not associated with the district. Additionally, the bill does not impose any requirements regarding the purchase price of available facilities or land.

PSFA notes the bill proposes a charter facility fund for the purchase, construction, expansion or renovation of facilities. However, if the fund is used for the expansion or renovation of a privately owned facility, it may violate the New Mexico Constitution’s anti-donation clause. Although the bill requires proof of certain items for a loan, one of which is the review of audit reports for the prior two years, the bill is silent regarding the type of audit required and whether a loan should be denied if significant audit findings are reported in the audits.

NMFA has existing PPRF policies for charter school loans. Charter school loans are classified as appropriation loans by NMFA. Appropriation loan capacity within the PPRF is defined in PPRF bond indentures, which NMFA notes is limited at this time.

### **PERFORMANCE IMPLICATIONS**

Provisions of this bill would increase the cost of lease assistance grants, which would reduce available funding for school facility replacement and renovation and affect overall facility conditions statewide. However, providing charter school loans through state sources could reduce the costs of financing charter school facilities compared with loans provided by private financial institutions.

## **ADMINISTRATIVE IMPLICATIONS**

PSCOC and PSFA will need to develop guidelines and a process to allocate funds from the charter facility fund, which may include an application and ranking methodology.

In 2019, PSFA measured and verified all eligible classroom net square footage and gross square footage at all charter schools to obtain accurate data to calculate accurate awards and to ensure compliance with statute. In the two years since, approximately 20 percent to 25 percent of charter schools report facility changes, requiring the need for PSFA to re-measure and verify square footage. Provisions of this bill would require PSFA to assess the charter school's facilities master plan (FMP) to ensure the FMP is consistent with the "space needed" by the charter school. This may be more involved than assessing the eligible classroom square footage, increasing the administrative processes to be performed by PSFA every year.

NMFA will need to set up a charter school loan fund within the PPRF to hold the charter school appropriation and to segregate those funds from other PPRF funds. NMFA will need to revise charter school loan policies to allow charter school loan debt service to be paid from the charter school loan fund and to not be counted against appropriation loan capacity that is used to make charter school loans, administrative office of the courts loans and similar loans.

## **TECHNICAL ISSUES**

The sponsor should consider adding the word "geographically" or "physically" into Section 2, subsection F, so the language reads as follows:

"A school district that has available land or one or more available facilities not currently used for other educational purposes shall make the land and facilities available for lease, lease-purchase or purchase to the charter schools [physically] located in the school district for their operations and shall notify them of that availability no later than May 1st of each year."

A locally authorized charter school is both physically located in the school district and a part of the district. A state-authorized charter school can be physically located in the same geographic location as a school district but is considered independent and not a part of the school district.

The bill provides that lease assistance provided to a district or charter school shall not exceed either "the actual annual lease payments owed for leasing a facility; or seven hundred dollars (\$700) multiplied by the MEM using the leased facilities" (page 12, lines 5 to 9). While "facilities" is defined, "a facility" is not defined and may be interpreted as more restrictive than the definition of "facilities." For example, it could be determined to only refer to a building but not surrounding land. This could be resolved by amending lines 5 to 7 to read "the actual annual lease payments owed for leasing facilities.

The bill references "five-year facilities master plan" on page 14, lines 5 to 6, in its definition of "facilities," which determines what facilities may be eligible for lease assistance; however, Subsection K references "five-year facilities plans" (without the word "master") on page 15, line 7. This language should be consistent.

The bill does not contain an effective date, but it may be desirable to include one because deadlines

established within the bill (May 1 and June 1) may otherwise pass prior to the bill taking effect.

### **OTHER SUBSTANTIVE ISSUES**

In an analysis of a similar bill, PSFA notes the bill does not indicate a prioritization methodology to determine how expenditure of the charter school facility fund will be authorized. Laws 2007, Chapter 214, (Senate Bill 634) created a charter school capital outlay fund, the balances of which were intended to assist state-chartered charter schools with the local match needed for an approved public school project. Awards made to state-chartered charter schools for capital projects were made using the same standards-based prioritization method as other traditional public schools. According to PSFA, it is important to note the underlying premise behind standards-based funding has been to prioritize awards based on facility condition.

In an analysis of a similar bill, NMFA states the PPRF is authorized to provide loan financing to charter schools for school facilities through lease-purchase arrangements, with NMFA taking on the role of titleholder and property owner of the facility. To date, NMFA has only reported one lease-purchase financing agreement directly for a charter school facility through PPRF. Current PPRF loan management policies require charter schools to meet either a 75 percent loan-to-value ratio or an 80 percent loan-to-value ratio if the overseeing school district of a locally chartered charter school is involved in the lease purchase arrangement. According to NMFA, charter schools have found it challenging to meet the minimum loan-to-value ratios. The loan-to-value ratios were developed so charter schools have an equitable interest at stake, as well as to help mitigate the ‘walk-away’ risk that is inherent with lease purchase agreements.

According to PSFA, school districts are required to include their locally chartered district charter schools in their FMP. However, the district charter schools are often not a district priority, and the identified needs provided for the district charters is often minimal or non-existent in district FMPs. The “space needed” and anticipated needs for charter facilities may not be incorporated into the district FMP, thereby providing insufficient data to justify and assesses the “space needed” at a given charter facility. Therefore, district charter schools may need to obtain an individual FMP, which in many instances may cost \$10 thousand to \$20 thousand to produce.

SL/sb