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

		ORIGINAL DATE	02/19/21		
SPONSOR	Ortiz y Pino	**LAST UPDATED**	03/04/21	**HB**	
SHORT TITLE	Transfer Above Trend Money from General Fund			**SB**	392
				ANALYST	Iglesias

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY21	**FY22**	**FY23**	**FY24**	**FY25**		
See Fiscal Implications					Recurring	General Fund
See Fiscal Implications					Recurring	Various Endowment Funds

Parenthesis ( ) indicate revenue decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Department of Finance and Administration (DFA)
Department of Transportation (DOT)
Department of Cultural Affairs (DCA)

SUMMARY

Synopsis of Bill

Senate Bill 392 distributes above-trend general fund revenue to various endowment funds, effectively treating above-trend revenue as nonrecurring monies. Specifically, if the general fund grows more than 5 percent above the 10-year average growth in a fiscal year, the excess is distributed as follows:

- 30 percent to the college affordability endowment fund,
- 20 percent to the teacher preparation affordability scholarship fund,
- 20 percent to the early childhood education and care fund,
- 10 percent to the state road fund,
- 10 percent to the severance tax permanent fund, and
- 10 percent to the rural libraries endowment fund.

There is no effective date of this bill. It is assumed the effective date is 90 days following adjournment of the Legislature.

FISCAL IMPLICATIONS

Current revenue estimates do not expect general fund revenues to grow more than 5 percentage points above the 10-year average growth for the forecast period. However, should the extractives industry experience a significant rebound, or if the general fund receives a large, unexpected source of income – such as the record federal bonus payment in FY19 that resulted in an unexpected distribution of over $475 million to the general fund – this bill's provisions could take effect in future years.

Over the last 10 years (FY09-FY20), total general fund revenues have grown at an average of 4.7 percent, as shown in the chart below. However, individual years have seen significant variability, largely due to the state's dependence on volatile oil- and gas-related revenues. For example, the oil production boom that began in late 2017 contributed to double-digit recurring revenue growth in FY18 and FY19. Prior to those fiscal years, the 10-year trend (FY08-FY17) for general fund revenue growth averaged 1.4 percent.

The consensus revenue estimating group's trend analysis of general fund revenues in recent years cautioned that above-trend revenues may not be sustainable over time, and the Legislature has taken various steps to limit the incorporation of above-trend revenue into recurring budgets. Such action includes distributing certain oil and gas severance taxes to the tax stabilization reserve and distributing federal bonus and royalty payments to the new early childhood education and care trust fund when those revenues exceed the previous five-year average. Over time, these previous legislative actions reduce general fund recurring revenue dependence on oil and gas revenues.

However, volatility in general fund revenues remain, particularly for revenues sources other than severance taxes and royalties that are significantly affected by oil and gas activity – namely, the gross receipts tax.

General Fund Appropriations History
(in millions of dollars)

	Recurring GF Revenue	Total GF Revenue	Recurring GF Revenue Growth	Total GF Revenue Growth
FY07	5,774.5	5,774.5	3.5%	4.7%
FY08	6,015.4	6,062.6	4.2%	5.0%
FY09	5,319.6	5,953.5	-11.6%	-1.8%
FY10	4,798.6	5,278.5	-9.8%	-11.3%
FY11	5,408.1	5,507.1	12.7%	4.3%
FY12	5,802.4	5,660.6	7.3%	2.8%
FY13	5,708.6	5,708.6	-1.6%	0.8%
FY14	6,040.1	6,040.5	5.8%	5.8%
FY15	6,194.7	6,235.9	2.6%	3.2%
FY16	5,708.8	5,708.9	-7.8%	-8.5%
FY17	5,885.4	6,461.1	3.1%	13.2%
FY18	6,816.5	6,881.3	15.8%	6.5%
FY19	8,009.5	7,910.3	17.5%	15.0%
FY20	7,859.8	8,182.9	-1.9%	3.4%
Ten Year Avg Growth in Total GF Revenue:				4.7%
FY21 est.	7,194.6	7,257.4	-8.5%	-11.3%
FY22 est.	7,548.1	7,548.1	4.9%	4.0%
FY23 est.	7,917.6	7,917.6	4.9%	4.9%
FY24 est.	8,251.2	8,251.2	4.2%	4.2%
FY25 est.	8,544.8	8,544.8	3.6%	3.6%

Source: DFA General Fund Audits, LFC Post-Session Reports, February 2021 Consensus Revenue Estimate

This bill proposes an additional step to manage general fund volatility and codifies a practice of treating above-trend revenues as nonrecurring funds by distributing a portion of those revenues to various endowment and infrastructure funds when the annual growth is more than 5 percent above the ten-year average growth. For example, because the 10-year average growth for FY11 to FY20 is 4.7 percent, general fund revenues in FY21 would need to grow more than 9.7 percent above the prior year to trigger the distributions identified in this bill.

SIGNIFICANT ISSUES

During boom years, particularly for FY19 and FY20 prior to the pandemic, state revenue estimators have frequently been asked to comment on how much of the recurring revenue estimate is "nonrecurring." State economists began regularly producing trend analyses demonstrating the relationship between current revenue estimates and the historical 10-year trend. However, the Legislature has not codified a specific method to determine whether and how above-trend revenue should be treated as nonrecurring funding.

Some states use trend analyses to manage long-term revenue fluctuations, avoid committing short-term gains to long-term obligations, and assure adequate and justifiable resources in reserve. For example, when revenue estimates are above the 15-year trend, Utah requires some of the surplus be used to restore specified fund withdrawals and maintain reserves. Virginia sets a threshold for above-normal general fund revenue at growth that exceeds the prior six-year average growth rate and deposits half into the state's rainy day funds. Each of these policies are intended to prevent the state from becoming overly dependent on revenue growth that is one-time, unexpected, unsustainable over time, or a combination of those three.

Some states also set rules for how to use identified nonrecurring revenues. For example, Louisiana requires nonrecurring revenues be spent on retiring bonds in advance, making payments against the unfunded liability of the public retirement systems, funding capital outlay projects, making deposits into the budget stabilization fund, making deposits into its coastal protection and restoration fund, or funding new highway construction for which federal matching funds are available.

The Department of Finance and Administration (DFA) states this bill will have a stabilizing effect on general fund revenues. This bill identifies a specific mechanism for determining above-trend growth (set in the bill as general fund revenue growth above 5 percent of the 10-year average) and identifies specific rules for treatment of those above-trend revenues by sending certain percentages to the identified endowment and infrastructure funds.

For example, FY19 revenues grew 15.8 percent over FY18, whereas the previous 10-year average growth (FY09-FY18) was 1.5 percent. If this bill were in place in FY19, a total of $581 million would have been statutorily treated as nonrecurring funding and distributed as illustrated in the chart below.

Example of Bill Mechanisms using FY19 General Fund Revenue			
Total General Fund Revenue	General Fund Revenue Growth	Previous 10-Year Average Revenue Growth	5% Above Previous 10-Year Trend
$ 7,910.3	15.0%	1.5%	$ 581.0
Distribution of Excess Revenue		**Percent**	**Amount**
College Affordability Fund		30%	$ 174.3
Teacher Affordability Scholarship Fund		20%	$ 116.2
Early Childhood Education and Care Fund		20%	$ 116.2
State Road Fund		10%	$ 58.1
Severance Tax Permanent Fund		10%	$ 58.1
Rural Libraries Endowment Fund		10%	$ 58.1

Note: dollars in millions

Notably, each of the funds identified in the bill as recipients of above-trend revenues are investable, income-earning funds. By distributing to these funds, the state would be able to capitalize on above-trend revenues through compound interest earnings.

TECHNICAL ISSUES

Section 1(A) states "…*total revenue and transfers are greater than* *<u>five percent</u>* *above the ten-year average growth*…"; however, this language should be amended to say "*<u>five percentage points</u>*" to align with the intent of the bill.

An amendment is needed in Section 1(A), line 23 after the comma, to add "*as determined by the department of finance and administration*", since the department will be responsible for calculating any excess amounts to be transferred pursuant to this bill.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Relates to Senate Bill 273 (SB273) Definition of Rural Library which changes the definition of a "rural library" for the purposes of eligibility for Rural Libraries Endowment funding for municipal public and tribal libraries from being based on population size of 3000 or under at the time of the library's establishment to their population size on or after July 1, 2019; and establishes that once qualified a library will continue to be qualify if their population size increases over 3000.

OTHER SUBSTANTIVE ISSUES

The Department of Cultural Affairs (DCA) notes that transfers of 10 percent of future excess general funds to the Rural Library Endowment Fund would increase the grant amounts paid to rural libraries each year.

Beginning FY22, the rural library endowment fund pays out the difference, if positive, between all fund investment income yielded through the immediately preceding calendar year and all fund distributions, up to 5 percent of the year-end market value of the fund for the immediately preceding calendar year, with 95 percent distributed to developing and established rural libraries and grants for the establishment of new rural libraries, and 5 percent to the New Mexico State Library to provide specialized services to rural libraries. Approximately half of the public and tribal libraries in the state currently qualify as a rural library. The 2020 year-end market value of the rural library endowment was $3,094,194.

DI/rl/sb/al