LFC Requester:	Ellen Rabin

AGENCY BILL ANALYSIS
2019 REGULAR SESSION

WITHIN 24 HOURS OF BILL POSTING, EMAIL ANALYSIS TO:

LFC@NMLEGIS.GOV

and

DFA@STATE.NM.US

{Include the bill no. in the email subject line, e.g., HB2, and only attach one bill analysis and related documentation per email message}

SECTION I: GENERAL INFORMATION

{Indicate if analysis is on an original bill, amendment, substitute or a correction of a previous bill}

Check all that apply:

Original X **Amendment** ____
Correction ___ **Substitute** ____

Date 3/11/19
Bill No: HB634

Sponsor: Rep. Larry R. Scott
Rep. James G. Townsend et al.

Short Title: DELETE LOCAL REVENUE FROM SEG CALCULATION

Agency Name and Code Number: PED-924

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SECTION II: FISCAL IMPACT

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Nonrecurring	Fund Affected
FY19	FY20		

(Parenthesis ( ) Indicate Expenditure Decreases)

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY19	FY20	FY21		
	$21,333.9	**$21,333.9**	Recurring	General Fund (SEG)

(Parenthesis ( ) Indicate Expenditure Decreases)

<u>ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)</u>

	FY19	FY20	FY21	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total						

(Parenthesis ( ) Indicate Expenditure Decreases)

Duplicates/Conflicts with/Companion to/Relates to:
Duplicates/Relates to Appropriation in the General Appropriation Act

<u>SECTION III: NARRATIVE</u>

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BILL SUMMARY

<u>Synopsis:</u>

HB 634 amends the Public School Finance Act to eliminate the local revenue credit in the public school funding formula in FY20 and subsequent years.

FISCAL IMPLICATIONS

Using FY18 local revenue credits, school districts will generate and additional in SEG formula dollars, assuming the state appropriated the additional $21.3 million in SEG dollars necessary to not lower the unit value. These school districts would receive these local property tax dollars and the same amount of these funds from state SEG sources as well. If the state did not appropriate from the General Fund additional SEG dollars to offset this amount in the calculated program cost, SEG funding would be distributed in lower amounts proportional to the FY18 distribution because the unit value would decline.

SIGNIFICANT ISSUE5S

The practice of taking credit for local revenue in equalized state aid formulas like New Mexico's dates to the early 1970's when states enacted new laws to promote greater equity in their school finance systems. In New Mexico, the 1974 creation of the current public school funding formula calculates a state equalization guarantee (SEG) that considers (and offsets) the ability for wealthy and poor districts to raise money from schools using property taxes, and attempts to equalize funding so that a similarly situated student in a poor district receives education funding on the same basis as a child in a wealthy district. In education finance literature this is termed "horizontal equity", or "equal treatment of equals."[1] The funding formula does so by limiting access to education funding for local property tax revenues, or federal revenues that are

[1] The public school funding formula in New Mexico also incorporates elements of vertical equity", or" equal treatment of unequals;" wherein the formula distributes additional funding for students that are more costly to educate like those with higher levels of special education needs or higher grades.

payments in lieu of property taxes (PILT) – most notably Impact Aid.

In New Mexico and other states, to help address inequities between wealty and poor school districts caused by receipt of property taxes and federal PILT payments, the state considers and offset (takes credit) for 75 (formerly 95) percent of those local property tax revenues received. This practice reduces state aid (SEG) payments to those districts for 75 percent of the amount of their federal local property tax offsets. The school districts keep 100 percent of the local property taxes. If the state no longer offsets local property tax wealth, the school districts will generate additional state aid funding and retain their local property wealth which increases the inequity between wealthy districts and poor districts.

Under current law, the state takes credit for 75 percent of: receipts from local ½ mill levy property taxes; receipts from the assessed value of products severed and sold and the value of equipment in the school district under the Oil and Gas; federal Impact Aid funds ; and federal forest reserve (Secure Rural Schools) funds. Impact Aid revenue received by school districts for federal children (basic support and children with disabilities) payments and construction grants are excluded from this property wealth offset.

When school districts (and charter schools) retain property taxes for operational purposes, education finance researchers say that the practice has a "disequalizing effect". This is because of the reintroduction of property wealth impacts into the education finance system. In this instance of HB 634 some districts would now be able to generate local property taxes, while others would still have SEG offsets for Impact Aid (though that would likely be subject to change). For example, when the state reduced the amount of credits from 95 percent to 75 percent, education policymakers and stakeholders will speak generally about how that decision had a disequalizing effect between wealthy populated districts whose residents are supportive of, and can afford to pay the practice of, levying additional property taxes and those in more property-rich and cash-flow poor, rural districts where local residents are more averse to tax increases or cannot afford such increases.

The actual legal determination of the amount of disequalization in our funding formula is required to be calculated yearly by PED via a disparity calculation and submitted to the USDE Impact Aid Office for certification to continue the practice of taking consideration of Impact Aid in the public school funding formula. In essence, the USDE requires states to show that horizontal equity is being maintained in the funding formula by using the federal range ratio,[2] a 95 – 5 percent confidence interval. New Mexico has not historically needed to engage in wealth neutrality or exceptional circumstances tests; although, for FY19 a recent funding formula change did mean that the state was only provisionally certified. Threats to increasing disparity include: proliferation of entities with high or low revenues per MEM (charter schools); funding formula changes that are not studied for impacts to disparity; and the increasing receipt of property taxes or revenues that act like property taxes for which the state does not take credit. In recent years this would include, but is not limited to: wind farm tax offsets, local county gross receipts revenues (Taos and Spaceport taxes); and offsets from local private businesses as part of tax infrastructure.

[2] The federal range ratio is a common metric of horizontal equity in education finance literature. Other common metrics include (but are not limited to): the range, the restricted range, the relative mean deviation, the McLoone index, the variance, the coefficient of variation, the standard deviation of logarithms, and the Gini coefficient. New Mexico's funding formula has historically performed well on these measures.

If the state fails the disparity test, it must repay the school districts which had Impact Aid credited in any given year the total amount of credits. HB 634 and similar bills introduced in this Legislative session increase the possibility that PED would need to request a supplemental deficiency appropriation in the amount of $58.6 million in future years**.**

PERFORMANCE IMPLICATIONS

ADMINISTRATIVE IMPLICATIONS

If local revenue was eliminated as a credit from the public school funding formula, it would likely disrupt the calculation of equity in our system. HB 634's elimination of local revenue credits may end the practice of equitable funding in our state as defined by federal statute. In the larger sense, it would also end the era of equalized funding and reintroduce the influence of property wealth into our state aid (SEG) formula.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

HB 634 is similar to SB 172 Exclude Impact Aid as Fed Revenue in SEG is similar to SB 170, Phase Out Impact Aid as Fed Revenue in SEG.

TECHNICAL ISSUES

OTHER SUBSTANTIVE ISSUES

PED believes it is very likely that Impact Aid school districts would seek the elimination of the credit. As that fact pattern reverts the state back to a property tax basis for education funding, it is likely the constitutional caps on Operational taxes would be reexamined as well potentially adding even more inequities into the system of state education financing. The provisions of HB 634 and similar bills introduced this session propose shifting the state to a system of financing much more dependent on local property taxes, and PED believes it likely that state aid financing would be decreased as local property taxes increase in wealthy areas as an attempt to promote school districts to have "skin in the game".

This particular education financing scheme, wherein the state provides about half of the funding and half is generated through local property taxes, has led to multiple sufficiency lawsuits in other states (i.e. the Abbott v. Burke cases in New Jersey, the Serrano v. Priest cases in California, the San Antonio ISD v. Rodriguez in Texas, and most recently Lobato v. State in Colorado) with mixed results. However, it was just this education financing scheme which the state considered when establishing the practice of offsetting local property tax wealth and PILT payments via credits in 1974, and developed the current system where the state has a higher effort than local property taxes. This education finance schema has kept the state largely insulated from arguments that the state aid structure is structurally insufficient. Indeed, even the recent Yazzie/Martinez case focused on insufficient inputs (appropriations) and outcomes (test scores) in its opinion, with criticisms of the structure of the SEG noticeably lacking. PED believes reinjecting local property wealth into the state aid formula will lead to future sufficiency lawsuits.

ALTERNATIVES

If policy makers believe that those areas of the state receiving local property taxes need additional services or cost offsets, the PED recommends other methods that maintain an equalized funding system. This could include increased urban or oil/gas education programming and related recurring (below the line) revenues.

As many of the school districts with high local property taxes are urban populated areas, or areas with oil/gas revenues, it is recommended that the state reexamine education program for urban youth or vocational programming for industry in the oil/gas school districts.

The PED has long supported increasing the scope of property tax credits as the education finance landscape changes, and would recommend more bills to take credit on local option property tax, wind farm receipts, the spaceport revenues and other tax infrastructure district PILT payments to school districts, rather than bills such as HB 634 and similar bills.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

AMENDMENTS